

# The New State Aid Rules for Services of General Economic Interest (SGEI): the Commission Decision and Framework of 20 December 2011

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## 1. Introduction: the 2011 package

On 20 December 2011, the European Commission adopted a new package of State aid rules for services of general economic interest (SGEI)<sup>2</sup>, which replaced the 2005 package<sup>3</sup>.

The 2011 package consists of four instruments that apply to public authorities that grant compensation for the provision of SGEI:

- A new **Communication**<sup>4</sup>, clarifying basic concepts of State aid relevant for SGEI<sup>5</sup>;
- A new proposal for a ***de minimis* Regulation**<sup>6</sup>, providing that compensation below EUR 500.000 over three years does not fall under State aid scrutiny (the final text is expected to be adopted in spring 2012);
- A revised **Decision**<sup>7</sup>, defining the conditions under which public service compensation is compatible with the internal market and does not need to be notified to the Commission pursuant to Article 108(3);

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<sup>2</sup> For an overview of this package, see "*The New State Aid Rules for SGEIs*" in Competition Policy Newsletter 2012-1.

<sup>3</sup> The 2005 package consisted of three instruments:

- a Commission Decision of 28 November 2005 on the application of Article 86(2) EC to State aid in the form of public service compensation (OJ L 312, 29.11.2005, p. 67),

- a Community Framework for State aid in the form of public service compensation (OJ C 279, 29.11.2005, p.4)

- an amendment to the Transparency Directive (Commission directive 2006/111/EC of 16 November 2006 on the transparency of financial relations between Member States and public undertakings as well as on financial transparency within certain undertakings; OJ L 318, 17.11.2006, p.318).

The 2005 Decision and the 2005 Framework have been replaced by the 2011 Decision and Framework, whereas the transparency Directive remains in force.

<sup>4</sup> Communication from the Commission on the application of the European Union State aid rules to compensation granted for provision of SGEIs (OJ C 8, 11.01.2012, p. 4-14).

<sup>5</sup> For an analysis of the SGEI Communication, see "*The SGEI Communication*" in Competition Policy Newsletter 2012-1.

<sup>6</sup> Draft Commission Regulation (EU) of 20.12.2011 on the application of Articles 107 and 108 TFEU to de minimis aid granted to undertakings providing SGEIs (OJ C 8, 11.01.2012, p. 23-27).

<sup>7</sup> Commission Decision of 20 December 2011 on the application of Article 106(2) TFEU to State aid in the form of public service compensation granted to certain undertaking entrusted with the operation of SGEI (OJ L 7, 11.01.2012, p. 3-10).

- A revised **Framework**<sup>8</sup> for assessing large compensation amounts granted to operators outside the social services field: those cases have to be notified to the Commission and may be declared compatible if they meet certain criteria.

This article analyses the Decision and Framework.

## 2. General overview of the Decision and Framework

### 2.1. Compatibility conditions: a diversified and proportionate approach based on common principles

The Communication and the draft *de minimis* Regulation mainly relate to the conditions under which a measure escapes the qualification of State aid under Article 107 TFEU (and therefore escapes the application of State aid rules). The Decision and the Framework define the conditions under which a measure qualified as State aid is deemed to be or can be found compatible with the internal market on the basis of Article 106(2).

Both the Decision and Framework are based on the principles set out in Article 106(2) and were adopted on the basis of Article 106(3).

Article 106(2) provides that "Undertakings entrusted with the operation of SGEIs or having the character of revenue-producing monopoly shall be subject to the rules contained in the Treaty, in particular to the rules on competition, in so far as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them; the development of trade must not be affected to such an extent as would be contrary to the interests of the Union". So the general prohibition of State aid under Article 107 also applies to undertakings providing SGEIs. However, if the aid is necessary to ensure the provision of the SGEI and does not affect trade to an extent that would be contrary to Union interests, the aid can be compatible with the internal market on the basis of Article 106(2).

Although both the Decision and the Framework are based on the same articles of the Treaty and so on the same principles (mainly necessity and proportionality), the Decision provides compatibility conditions which are simpler than under the Framework, as well as an exemption from the obligation to notify pursuant to Article 108(3).

This is because the Decision covers aid which *a priori* has less impact on competition and trade than aid which has to be assessed under the Framework. The Commission aims to keep the administrative burden proportionate to the aid's likely impact on competition and trade, so the requirements under the Decision are less strict than under the Framework.

This two-tier approach was already there in the 2005 package. However, in line with the objectives set out by the Commission Communication adopted on 23 March 2011 on the reform of the EU State aid Rules on SGEIs, this approach has now been reinforced, so as to offer a more proportionate response to the different types of SGEIs and make the degree of State aid scrutiny more dependent on the nature and scope of the services provided.

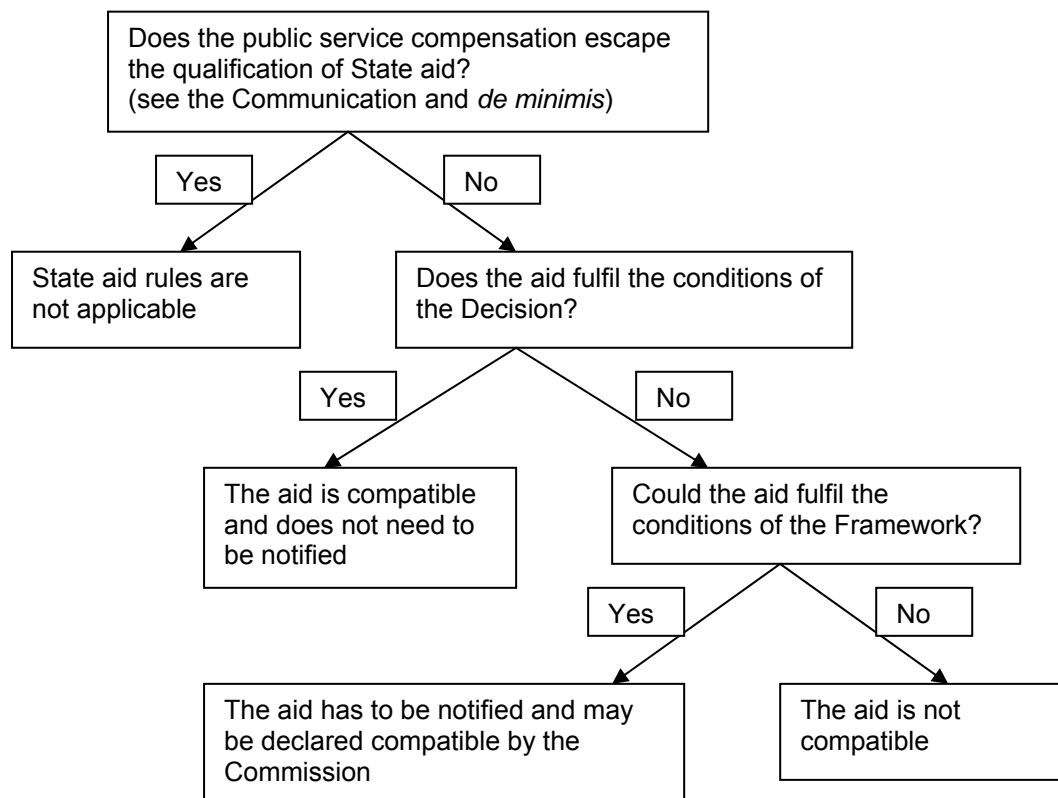
### 2.2. Complementary scopes of application

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<sup>8</sup> Communication from the Commission: European Union Framework for State aid in the form of public service compensation (OJ C 8, 11.01.2012, p. 15-22).

The Decision is applicable to aid in the form of compensation for SGEI below EUR 15 million and to aid in the form of compensation for SGEI provided by hospitals or for social services<sup>9</sup>. Other types of aid are assessed on the basis of the Framework.

Graph 1: analysis tree



This article presents the Decision (3) and the Framework (4); it highlights the changes compared to the 2005 Decision<sup>10</sup> and 2005 Framework<sup>11</sup>.

### 3. The Decision

Compared to the 2005 Decision, the main changes relate to the scope of application of the Decision (3.1). There are also new elements regarding the compatibility conditions (3.2).

#### 3.1 Scope of application

To define the Decision's scope of application, the Commission identified the characteristics of aid having a relatively minor effect on competition and trade:

- the amount of aid should be relatively small (3.1.1); however in certain sectors, even high amounts of aid involve limited distortions of competition (3.1.2); in the air and maritime

<sup>9</sup> If other conditions of applicability are complied with.

<sup>10</sup> Commission Decision of 28 November 2005 on the application of Article 86(2) EC to State aid in the form of public service compensation (OJ L 312, 29.11.2005, p.67).

<sup>11</sup> Commission Framework for State aid in the form of public service compensation (OJ C 297, 29.11.2005, p.4).

transport sectors, the number of passengers is a more relevant indicator of the impact on trade than the amount of compensation (3.1.3);

- the duration of entrustment should be limited to what is necessary to attract a public service provider (3.1.4).

Different from the 2005 Decision, the turnover of the beneficiary is no longer used as a criterion to distinguish between cases in terms of their likely impact on competition and trade (3.1.5).

### **3.1.1. The Decision is applicable to aid below EUR 15 million**

As in the 2005 Decision, the aid covered by the 2011 Decision cannot exceed a certain amount. Above this amount, the aid is considered likely to affect trade and competition to such an extent as to make its notification necessary.

Compared to the 2005 Decision, the threshold of application of the 2011 Decision has been reduced from EUR 30 million per year and per SGEI to EUR 15 million per year and per SGEI.

The main reason for lowering this threshold is that intra-Community trade – including for SGEIs – has since developed. This is due to several factors, in particular the emergence of large multi-national providers, the increasing use of public procurement procedures, and the reduction of exclusive rights. Indeed, the public consultation carried out in 2010 showed that stakeholders generally think the 2005 rules withdrew a large number of sizeable compensation measures from State aid scrutiny, especially in some sectors which are more and more open to competition like water management<sup>12</sup>. The lowering of the threshold to EUR 15 million should bring additional important cases to the Commission's attention.

This lowering of the compensation threshold has to be seen also in the light of the objective of having a more diversified and proportionate approach. Under the 2005 Decision, only hospitals and social housing benefitted from its application, regardless of the amount of compensation. For other services, a threshold of EUR 30 million applied. This relatively high threshold implicitly ensured that most social services could benefit from the exemption as well. The new Decision now explicitly extends the exemption to social services (without threshold; see below).

### **3.1.2. The Decision is applicable to aid to hospitals and social services regardless of the amount**

Although the amount of aid is considered to be the best criterion to estimate the likely impact of the aid on competition and trade, it may also be appropriate to take into account the sector of the beneficiary.

The 2005 Decision used to cover aid to hospitals and social housing regardless of the amount of compensation. This exemption has now been extended to social services.

Like hospitals and social housing, social services have specific characteristics, so the intensity of competition distortion is not necessarily proportionate to the level of compensation. For example:

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<sup>12</sup> See Commission Staff working paper, Impact assessment (SEC 2011)1581:

[http://ec.europa.eu/governance/impact/ia\\_carried\\_out/cia\\_2011\\_en.htm#comp](http://ec.europa.eu/governance/impact/ia_carried_out/cia_2011_en.htm#comp).

- at the current stage of the internal market's development, social services are mainly local (although, as for hospitals, multi-national operators are developing);

- when a social service has an important qualitative human dimension (as opposed to services of a more administrative or standardised nature), it may be difficult to assess and improve the efficiency of such services. As the Framework makes efficiency incentives compulsory in principle, it is more appropriate to assess aid to social services under the Decision than under the Framework.

To give legal certainty, the Commission has provided an exhaustive list of the social services covered by the Decision regardless of the amount of compensation. This list is extensive, since it includes "*SGEIs meeting social needs as regards health and long term care, childcare, access to reintegration into the labour market, social housing and the care and social inclusion of vulnerable groups*". In particular, the notion of vulnerable groups is quite broad.

Some stakeholders have asked whether nurseries or individual childcare can be covered by the Decision. The Decision does not make any distinction between different types of childcare. However, to be included in the scope of the Decision, childcare needs to be an SGEI. This means that childcare provided without any public service mission cannot receive public service compensation on the basis of Article 106(2) TFEU. However, where a public service mission is defined and where the conditions of the Decision are fulfilled, childcare can receive public service compensation, whether it is a collective or individual service. The same applies to long term care and other social services.

### **3.1.3. The Decision is applicable to aid to air and maritime links to islands as well as to ports and airports below a certain number of passengers**

Land transport is subject to Article 93, which is a *lex specialis* with regard to Article 106(2), so the Decision and Framework do not apply to land transport. However, the Decision and Framework do apply to the maritime and air transport sectors<sup>13</sup>.

The 2011 Decision is applicable to:

- compensation for the provision of SGEIs as regards air or maritime links to islands on which the average annual traffic during the two financial years preceding that in which the SGEI was assigned does not exceed 300 000 passengers<sup>14</sup>;

- compensation for the provision of SGEIs as regards airports and ports for which the average annual traffic during the two financial years preceding that in which the SGEI was assigned does

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13 Certain rules applicable to public service compensation in the air and maritime transport sectors are to be found in Regulation (EC) No 1008/2008 of the European Parliament and of the Council of 24 September 2008 on common rules for the operation of air services in the Community and in Council Regulation (EEC) No 3577/92 of 7 December 1992 applying the principle of freedom to provide services to maritime transport within Member States (maritime cabotage). However, those Regulations do not refer to the compatibility of the possible State aid elements. The SGEI Decision therefore applies to public service compensation in the air and maritime transport sectors provided that, in addition to fulfilling the conditions set out in the Decision, such compensation also complies with the sectoral rules contained in Regulations (EC) No 1008/2008 and (EEC) No 3577/92 where applicable.

14 Article 2(1)(d).

not exceed 200 000 passengers in the case of airports, and 300 000 passengers in the case of ports<sup>15</sup>.

Only the threshold for compensation for SGEI provision as regards airports has been modified compared to 2005, reduced from one million to 200 000 passengers. By doing so, the Commission intends to scrutinise more closely SGEI compensation for regional airports. Since 2005, those airports have developed dramatically, partly due to the rise of low cost airlines. There is more and more competition among these airports, leading to an increased risk of subsidiary races which distort competition and trade between Member States<sup>16</sup>.

Recital (25) was also modified from recital (19) in the 2005 Decision. Recital (25) now clarifies that only the number of passengers is relevant to determine whether the Decision is applicable. Therefore, a Member State cannot invoke the Decision on the basis of the argument that the compensation is below EUR 15 million.

### **3.1.4 The Decision is applicable only to entrustment acts not longer than 10 years except in certain cases**

An important change from 2005 is that it only applies where the period for which the undertaking is entrusted with the operation of the SGEI does not exceed 10 years, unless significant investment is required which needs to be amortised over a longer period. This can be the case for instance in the social housing sector (Decision recital (12)).

No such condition was imposed in the 2005 Decision. However, the extent to which a particular compensation measure affects trade depends not only on the average amount of compensation per year and the sector concerned, but also on the overall duration of the contract. For instance, a fifteen-year entrustment where public service compensation of EUR one million is awarded each year is likely to affect competition and trade more than several consecutive shorter entrustments with annual compensation of EUR one million insofar as the repeated entrustment provides more scope for switching SGEI provider in a context of competing service offerings.

Therefore the necessity and proportionality principles should also apply to the duration of the contract. The duration of the entrustment should be sufficiently long to attract potential providers – especially when investments are needed to provide the SGEI – but not longer than necessary.

### **3.1.5. The Decision is applicable regardless of the beneficiary's turnover**

There are two main reasons why this threshold, exempting company turnover of less than EUR 100 million from the notification obligation, was eliminated:

- first, the turnover threshold was in some cases difficult to apply. This was particularly true for group structures because it was often difficult to identify the appropriate delineation for State aid purposes;

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<sup>15</sup> Article 2(1)(e).

<sup>16</sup> Investment aid and possibly certain operational aid might be allowed for those airports on the basis of Article 107(3)(c). The compatibility conditions will be specified in the airport and aviation guidelines which the Commission intends to adopt in 2012.

- second, this threshold led to different treatment for undertakings of different sizes, even where the impact on competition was the same.

It may be argued that large undertakings are more likely to have commercial activities which could be cross subsidised. This concern should be alleviated by the obligation for undertakings carrying out activities falling both inside and outside the scope of the SGEI to have internal accounts that show separately the costs and receipts associated with the SGEI and those of other services<sup>17</sup>.

### **3.2 Compatibility conditions**

The compatibility conditions remain similar to the compatibility conditions under the 2005 Decision. However there are some novelties, mainly aimed at simplifying the rules or offering more flexibility.

#### **3.2.1 Existence of an SGEI**

The existence of an SGEI is a prerequisite to apply the Decision<sup>18</sup>. On this aspect, there is no new element. It is useful in this context, however, to refer also to the new Communication, which clarifies the concept of SGEI and manifest error.

#### **3.2.2 Entrustment act including a reference to the Decision**

Regarding the existence of an entrustment act, the main change from the 2005 Decision is the requirement that the entrustment act include a reference to the 2011 Decision itself.

One of the main issues raised in the application of the 2005 package was insufficient compliance with the rules. This was shown by the Commission Staff working paper on the application of EU State Aid rules on SGEI since 2005, published on 23 March 2011.. In many cases, public authorities or SGEI providers do not know whether the compensation granted qualifies as aid, and if it does not, whether it complies with the 2005 Decision. By requiring public authorities to include a reference to the Decision in the entrustment (similar to the General Block Exemption Regulation), the Commission intends to remove the "grey" area which currently exists because authorities do not ask themselves whether the compensation involves State aid or not. This should improve transparency and compliance with the rules.

#### **3.2.3 Amount of compensation and control of overcompensation**

As regards the amount of compensation, the fundamental principle remains the same as under the 2005 Decision: the compensation should not exceed what is necessary to cover the net cost incurred in discharging the public service obligations, including a reasonable profit.

**Compensation ≤ net costs + reasonable profit**

Above this limit, the provider receives an "overcompensation" which cannot be justified by the need to provide the SGEI.

There are however a number of novelties:

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<sup>17</sup> Article 5(9) of the 2011 Decision.

<sup>18</sup> Article 2: "This Decision applies to State aid in the form of public service compensation, granted to undertakings entrusted with the operation of SGEI as referred to in article 106(2), ...".

a) The 2011 Decision takes a **multi-annual approach**, rather than an annual approach. This means that a provider can receive overcompensation for a certain year, as long as there is no overcompensation for the whole duration of the contract. It thus increases flexibility. It also better fits the aim of moving towards compensation schemes that provide for efficiency incentives, given that the provision of such incentives typically requires a multi-annual perspective.

However, with a view to avoiding cases where the beneficiary would receive overcompensation for a long time without any scrutiny, the Decision provides that Member States must carry out regular intermediate checks (at least every three years) during the period of entrustment and at the end.<sup>19</sup> Where, under the terms of the entrustment act, the undertaking has received overcompensation, the Member State must require the undertaking concerned to repay it. However, the overcompensation can be carried forward to the next period when it does not exceed 10% of the average annual compensation. A final, comprehensive, check is made at the end of the contract to ensure that there was no overcompensation over the lifetime of the contract.

This new approach enables Member States to carry out fewer checks than under the 2005 decision and reduces the administrative burden.

b) Regarding the **method for calculating the net cost of providing the SGEI**, as under the 2005 Decision, Member States can calculate the net cost as the difference between the costs incurred in providing the SGEI and the revenue earned from it<sup>20</sup>. In particular, when an undertaking carries out SGEI and non SGEI activities, it should separate the accounts between them and count as SGEI costs all direct costs incurred in providing the SGEI, and an appropriate contribution to the costs that are common to both SGEI and non SGEI activities.

However, under the 2011 Decision, Member States can also calculate the net cost of providing the SGEI as the difference between the net cost for the undertaking of operating with the public service obligation and the net cost or profit of the same undertaking operating without the public service obligation<sup>21</sup>. This methodology can be useful (and, in certain cases, simple to use). For instance, for undertakings active in social housing: the cost of the SGEI could be the difference between the price at which the social housing provider has to rent the housing and the market price for that housing.

Thus the 2011 Decision offers more flexibility than the 2005 Decision.

c) Regarding **reasonable profit**, there are two changes compared to 2005:

- The first change relates to the profit indicator. The 2011 Decision provides that the "rate of return on own capital" means the "internal rate of return" (IRR) that the undertaking makes on its invested capital over the duration of the entrustment period<sup>22</sup>. This rate is the standard measure to assess investment profitability over longer periods of time. It also reflects the Commission's aim to switch from an ex post perspective of profit (based on annual accounts) towards a more ex ante perspective (based, at least partially, on financial forecasts over the lifetime of the contract). The ex ante perspective is, in principle, better able to give incentives for

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<sup>19</sup> Article 6(1) of the Decision.

<sup>20</sup> See cost allocation methodology under the Framework.

<sup>21</sup> See net avoided cost methodology under the Framework.

<sup>22</sup> Article 5(5) of the 2011 Decision.



SGEI providers to become more efficient over time (see below under the Framework section for details).

However, when it is not appropriate to use the internal rate of return on capital in specific circumstances, Member States can rely on accounting profit indicators such as the average annual return on equity, return on capital employed, return on assets or return on sales<sup>23</sup>. Here again, the Decision is flexible.

- The second change relates to the level of profit allowed. The rule (based on the necessity and proportionality principles) remains the same as under the 2005 decision: the profit should not exceed the rate of return on capital that would be required by a typical undertaking considering whether or not to provide the SGEI, taking into account the level of risk.

On one hand, the 2011 Decision provides the simple rule that profit below swap rate<sup>24</sup> + 100 basis points<sup>25</sup> is considered to be reasonable in any event. This is a safe harbour.

On the other hand, with a view to discouraging the use of ex post full compensation schemes<sup>26</sup>, the 2011 Decision provides that this safe harbour is a profit cap where the provision of the SGEI is not connected with a substantial commercial or contractual risk, in particular when the net cost incurred in providing the SGEI is essentially compensated ex post in full.

Many of the other rules relating to the amount of compensation and control of overcompensation remain unchanged:

- If an undertaking holds special or exclusive rights linked to activities, other than the SGEI for which the aid is granted, which generate profits in excess of the reasonable profit, or if it benefits from other advantages granted by the State, these have to be included in its revenue, irrespective of their classification for the purposes of Article 107 of the Treaty<sup>27</sup>.

- In determining what constitutes a reasonable profit, Member States may introduce incentive criteria relating, in particular, to the quality of service provided and gains in productive efficiency. Efficiency gains must not reduce the quality of the service provided<sup>28</sup>.

- Where an undertaking carries out activities falling both inside and outside the scope of the SGEI, the internal accounts must show separately the costs and receipts associated with the SGEI and those of other services, as well as the parameters for allocating costs and revenues<sup>29</sup>.

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<sup>23</sup> Article 5(8) of the 2011 Decision.

<sup>24</sup> The swap rate is the longer maturity equivalent to the Inter-Bank Offered Rate (IBOR rate). It is used in the financial markets as a benchmark rate for establishing the funding rate.

<sup>25</sup> The premium of 100 basis points serves, inter alia, to compensate for liquidity risk related to the fact that an SGEI provider that invests capital in an SGEI contract commits that capital for the duration of the entrustment act and will be unable to sell its stake as rapidly and at as low a cost as is the case with a widely held and liquid risk-free asset.

<sup>26</sup> Ex post full compensation schemes are compensation schemes where the providers receive compensation equal to the net cost incurred in providing the SGEI: such a scheme does not provide incentives to undertakings to become more efficient when providing the SGEI.

<sup>27</sup> Article 5(4) of the 2011 Decision.

<sup>28</sup> Article 5(6) of the 2011 Decision.

<sup>29</sup> Article 5(9) of the 2011 Decision.

### 3.2.4 Transparency

The 2011 Decision says that for compensation above EUR 15 million granted to an undertaking which also has activities outside the scope of the SGEI, the Member State concerned must publish the entrustment act or a summary of it and the amounts of aid granted to the undertaking on a yearly basis.

The objective is to reinforce transparency and compliance with the rules for those measures which – although covered by the Decision – involve higher risks of competition distortion. Indeed, although the requirement to separate accounts should alleviate concerns about cross subsidization from SGEI to non SGEI activities, the consultation process has shown that a number of stakeholders have doubts about whether separation of accounts is sufficient.

### 3.3 Transitional provisions<sup>30</sup>

Individual aid which was granted before the revised Decision comes into force and complied with the 2005 Decision is not affected by the revision. Individual aid that was granted before the revised Decision comes into force and was incompatible with the 2005 Decision, but fulfils the conditions of the revised Decision, is compatible aid.

Aid schemes that are put in place before the revised Decision enters into force and are compatible with the 2005 Decision continue to be compatible and exempt from the notification obligation for a period of two years from the entry into force of the revised Decision.

## 4 The Framework

### 4.1 Scope of application<sup>31</sup>

The Framework applies to public service compensation not covered by the Decision. Therefore its scope of application reflects the changes made to the Decision's scope of application.

The Framework does not apply to aid to:

- the land transport sector. Rules concerning aid to the land transport sector rules are based on Article 93;
- public service broadcasting. This sector is covered by a specific Communication<sup>32</sup>;
- SGEI providers in difficulty. Such aid will be assessed under the Community guidelines on State aid for rescuing and restructuring firms in difficulty<sup>33</sup>. Those guidelines are now being reviewed, and the Commission will examine if and how they should take better account of the specificities of aid to public service providers. One consideration could be that the provision of the SGEI should be ensured, but not necessarily the continued existence of the incumbent undertaking providing the service.

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<sup>30</sup> Article 10 of the 2011 Decision.

<sup>31</sup> Part 1 of the Framework, in particular points 7, 8 and 9.

<sup>32</sup> Communication from the Commission on the application of State aid rules to public service broadcasting (OJ C 257, 27.10.2009, p.1).

<sup>33</sup> OJ C 244, 1.10.2004, p.2.

## 4.2 Compatibility conditions<sup>34</sup>

Compatibility conditions have been substantially modified compared to the 2005 Framework. In line with the Communication adopted by the Commission in March 2011, the main objectives of those changes are to take better account of efficiency and competition considerations and to strengthen transparency.

In line with the principle of having a proportionate approach, the Framework presents the principles guiding the standard assessment (4.2.1), but also includes provisions for a simplified assessment of aid normally covered by the Decision (4.2.2) and provisions for in-depth assessment of cases involving serious distortions to competition and trade (4.2.3).

### 4.2.1 Standard assessment

This part has the same structure as part 2 of the Framework, which sets out the conditions governing the compatibility of public service compensation. Please note that part 2.11 of the Framework is relevant for the simplified assessment only and part 2.9 for the in-depth assessment only.

#### 4.2.1.1. General provisions

Public service compensation may be compatible with the internal market only if it is necessary for the provision of the SGEI and does not affect the development of trade to such an extent as would be contrary to Union interests. Those general principles stem directly from Article 106(2). There is no change in this regard from the 2005 Framework.

The principles of necessity and proportionality are deemed to be complied with if the following conditions are fulfilled.

#### 4.2.1.2. Existence of a genuine SGEI

First, the aid must be granted for a genuine SGEI.

Compared to 2005, the main change relates to the requirement that Member States show they have given proper consideration to the public service needs supported by way of a public consultation or other appropriate instrument, to take the interests of users and providers into account. This requirement should enable the Commission better to identify cases where there is a manifest error in the definition of the SGEI.

It is also worth highlighting that the Commission notes here the principle set out in the Communication, that Member States cannot attach specific public service obligations to services that are already provided or can be provided satisfactorily and under conditions consistent with the public interest, as defined by the State, by undertakings operating under normal market conditions.

Therefore, even though Member States have a wide margin of discretion in defining the existence of an SGEI in the absence of specific EU rules, they should consider the following questions:

1. Is the service for citizens or is in the interest of society as a whole?<sup>35</sup>

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<sup>34</sup> Part 2 of the Framework.

<sup>35</sup> Part 3.2 of the Communication from the Commission on the application of the EU State aid rules to compensation granted for the provision of SGEIs.

2. Is there a public need justifying the public service mission?
3. Is this need already fulfilled or could it be fulfilled by undertakings operating under normal market conditions?

For those questions, Commission monitoring is limited to monitoring for manifest error.

#### *4.2.1.3. Entrustment act*

Second, there should be an entrustment act.

Regarding the entrustment act, there is no major difference from 2005.

#### *4.2.1.4. Entrustment period duration*

Third, the duration of the entrustment period should be justified by reference to objective criteria such as the need to amortise non-transferable fixed assets. In principle, the duration of the entrustment period should not exceed the period required for the depreciation of the most significant assets required to provide the SGEI.

This is a new condition compared to 2005. The Commission's objective is to avoid excessively long entrustment periods leading to the risk of competition distortion (possibly even foreclosing the market in case of exclusive rights or extremely low regulated tariff), when such a long period is not necessary to provide the SGEI.

Article 2(2) of the Decision is also about the duration of the entrustment act, but it relates to the Decision's scope of application, not to the compatibility conditions. Based on the conjunction of Article 2(2) of the Decision and part 2.4 of the Framework, duration of entrustment longer than 10 years which is not justified by objective criteria implies that the aid is incompatible.

#### *4.2.1.5. Compliance with the Transparency directive*

Fourth, compliance with the Transparency directive, when applicable, is a condition for compatibility.

This provision is new compared to 2005. The objective is to increase transparency so as to improve monitoring of compliance with the rules. However, the importance of this provision is expected to be limited, considering that the separation of accounts is any event required by the Decision and the Framework for undertakings having activities falling both inside and outside the SGEI.

#### *4.2.1.6. Compliance with Union public procurement rules*

Fifth, compliance with Union public procurement rules, where applicable, is a condition for compatibility. This includes any requirement of transparency, equal treatment and non-discrimination resulting directly from the Treaty and, where applicable, secondary Union law (in particular, public procurement directives). Where Union public procurement rules are not applicable, compliance with them is not a condition for compatibility. Therefore this provision does not impose new obligations on Member States, but only reinforces the current ones. This is however an important new element compared to 2005.

On the basis of the *Matra* jurisprudence<sup>36</sup>, the Commission used to consider that if there was no indissoluble link between the public procurement rules and the State aid rules, the aid could be deemed compatible even if public procurement rules had not been complied with. However, this policy is not always satisfactory and the *Matra* jurisprudence does not prevent the Commission from going beyond the indissoluble link approach.

From a competition perspective, public procurement is preferable because it allows a competitive process and makes for a competitive SGEI market. Therefore, before concluding that aid is compatible, it is appropriate to ensure that public procurement rules have been complied with - or will be complied with before granting the aid. This measure will contribute both to improving compliance with public procurement rules and to fostering competition when designating the public service provider(s), where public procurement rules apply.

#### *4.2.1.7. Absence of discrimination*

Sixth, where an authority assigns the provision of the same SGEI to several undertakings, the compensation should be calculated on the basis of the same method for each undertaking.

This provision is also new compared to 2005.

This is an important provision, as public authorities relatively often entrust the same SGEI to several undertakings and compensate them on the basis of different methods. The Commission has received a number of complaints based on such facts, for instance in the health insurance sector.

However, until now, the Commission had to conclude that such discrimination was not contrary to the compatibility conditions under the 2005 Decision and the 2005 Framework as long as there was no overcompensation and the other provisions of the texts were fulfilled.

It is no longer appropriate to accept such discrimination, considering that the Framework now takes better account of efficiency. The fact that a provider is able to provide the service for lower compensation shows that higher compensation is not necessary for the provision of the service, but rather keeps afloat an inefficient provider.

Of course, this provision could also lead public authorities to increase compensation for the most efficient providers. But considering their limited resources, it appears more likely that this measure will lead to lower compensation in the medium or long term.

The Decision does not include a non-discrimination clause, although it could be particularly relevant for hospitals, for instance. It was felt that under the diversified and proportionate approach, efficiency and competition considerations could be seen as less pressing for compensation covered by the Decision, in particular for hospitals and social services.

#### *4.2.1.8. Amount of compensation*

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<sup>36</sup> Case C-225/91, *Matra* [1993] ECR I-03203. "The procedure under Article 85 et seq. and that under Article 92 et seq. of the Treaty are independent procedures governed by specific rules, with the result that, when the Commission is called upon to take a decision on the compatibility of State aid with the common market, it is not obliged to await the outcome of a parallel procedure initiated under Regulation No 17, once it has reached the conclusion, based on an economic analysis of the situation and without any manifest error in the assessment of the facts, that the recipient of the aid is not in contravention of Articles 85 and 86 of the Treaty."

Seventh, the amount of compensation must not exceed what is necessary to cover the net cost of discharging the public service obligations, including a reasonable profit.

This is the usual principle<sup>37</sup>. However part 2.8 of the Framework shows a number of significant differences in the method of applying this principle. Those changes are mainly explained by the Commission's objective of taking better account of efficiency and competition for large-scale non-social SGEIs.

### *Efficiency incentives*

In line with the Communication adopted by the Commission on 23 March 2011 on the reform of the EU State aid Rules on SGEIs, the Commission considered how to take greater account of efficiency and competition considerations for large-scale commercial services.

Indeed, although the 2005 Decision and Framework brought clarity and legal certainty on the conditions under which public service compensation could be granted, in many cases they may have led to situations where the public service provider had no incentive to improve its efficiency and, in some cases, where more efficient providers were crowded out. The reason for this situation is that the 2005 Decision and Framework, while in principle allowing for efficiency gains to be recognised, also imposed annual checks for overcompensation on the basis of incurred costs and receipts. In doing so, it may have inadvertently prompted public authorities often to opt for compensating the net cost incurred in providing the SGEI on an **ex post** basis and **in full**. If the whole net cost is fully compensated ex post, however, the provider has no incentive to improve its efficiency. If, in addition to such a compensation mechanism, public authorities grant exclusive rights or fix a tariff for the provision of the SGEI which is so low that no competitor is able to offer the service while not receiving compensation, competitors are excluded from the market. This leads to situations where the incumbent can continue to supply the service at an excessive cost (for a given level of quality), this being done at the expense of the public authority and of the users who finance the SGEI. From the perspective of EU interest, this may also lead to fragmentation of the internal market and lack of competitiveness.

To address this concern, the 2011 Framework makes two significant changes:

a) In devising the method of compensation, Member States must introduce incentives for the efficient provision of SGEI of high standard, unless they can justify that it is not feasible or appropriate to do so<sup>38</sup>.

Member States have a large margin of discretion to design the compensation mechanism. The Framework gives two examples of such compensation mechanisms:

- upfront payment: the Member State defines a fixed compensation level which incorporates the efficiency gains that the undertaking can be expected to make over the lifetime of the entrustment act;

- payment dependent upon the extent to which efficiency targets have been met: Member States define productive efficiency targets in the entrustment act whereby the level of compensation is made dependent upon the extent to which the targets have been met. If the undertaking does not meet the objectives, the profit should be reduced. In contrast, if the undertaking exceeds the objectives, the profit should be increased.

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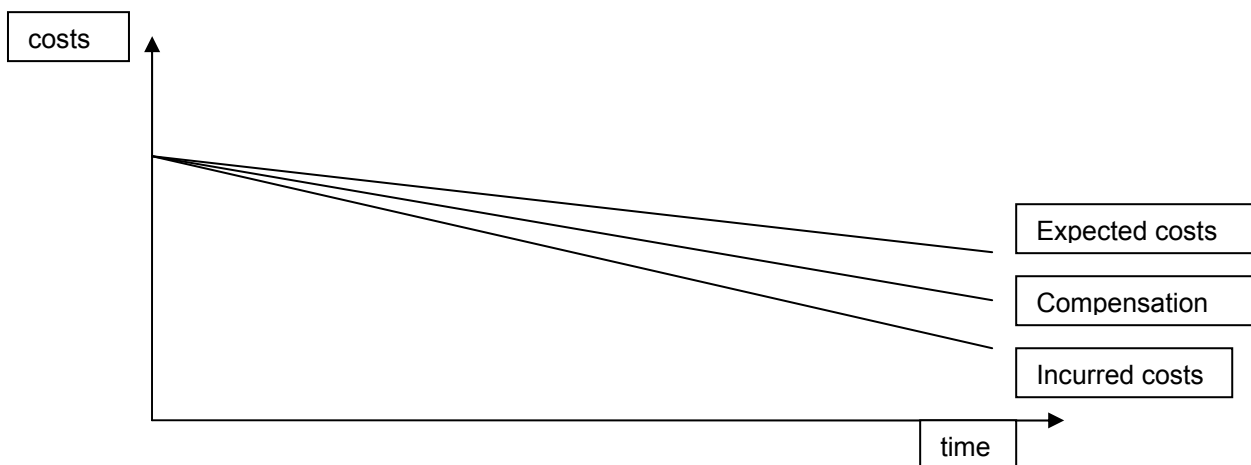
<sup>37</sup> See the 2005 Decision and Framework and the 2011 Decision.

<sup>38</sup> Point 39 of the Framework.

In any event, the compensation should in principle no longer be based on incurred costs only. To preserve the incentive for the provider to become efficient, the compensation should be based on the expected costs (upfront payment) or on a combination of expected and incurred costs (payment depending upon whether the efficiency targets have been met). The compensation mechanism has to be specified in advance in the entrustment act.

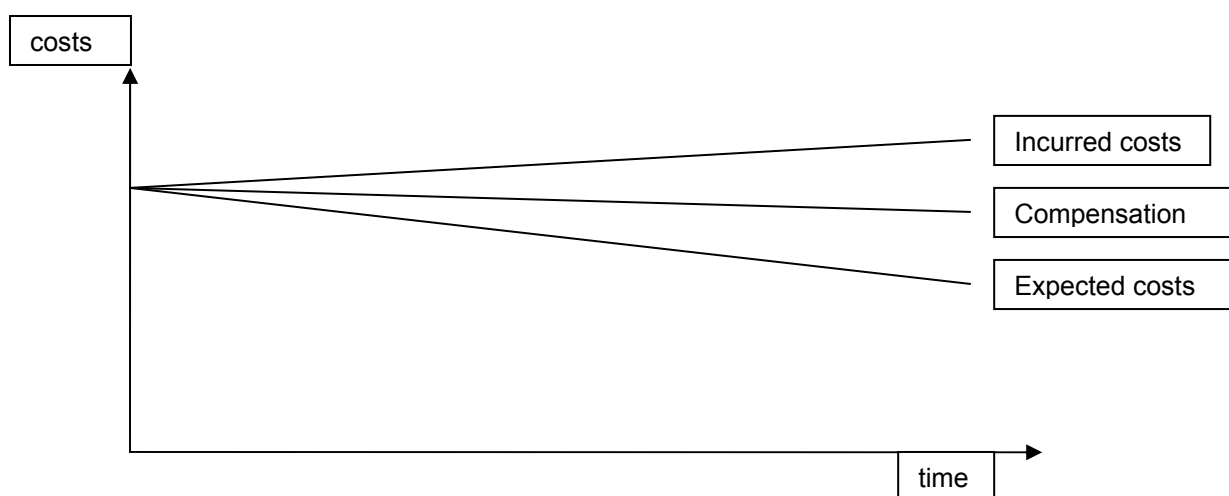
The two following graphics illustrate the case where the compensation is based on a combination of expected and incurred costs:

Case 1: efficiency gains are higher than expected, so incurred costs are below expected costs.



In case incurred costs are below expected costs, the compensation can exceed the incurred costs, thus increasing the profit of the undertaking. The compensation should however in no case exceed the expected costs (plus reasonable profit)<sup>39</sup>.

Case 2: efficiency gains are lower than expected, so incurred costs are above expected costs.



<sup>39</sup> In case the compensation mechanism is an upfront payment, the compensation is equal to the expected costs: the undertaking keeps all the profits linked to the fact that it has been more efficient than expected.

In case incurred costs are above expected costs, the compensation cannot cover the total incurred costs. So the undertaking has to bear part of the loss due to the fact that it was less efficient than expected<sup>40</sup>.

This mechanism should encourage efficiency gains and lead in the medium or long term to lesser amounts of aid (even if in the short term, the compensation may exceed the incurred costs in case efficiency gains are higher than expected).

This has to be distinguished from the efficiency test under *Altmark*. Contrary to the *Altmark* test, there is no requirement for the provider to be efficient; there is only a requirement to introduce efficiency incentives in the compensation mechanism, which should make providers efficient in the medium or long term.

b) Where the Member State is able to justify that it is not feasible or appropriate to take into account productive efficiency and decides to compensate the net cost incurred in providing the SGEI ex post and in full, the Framework provides that the reasonable profit may not exceed the swap rate + 100 basis points<sup>41</sup>.

This provision aims to limit the use of compensation schemes which do not provide incentives for the undertaking to improve efficiency.

#### *Ex ante multi-annual approach*

As explained above, the objective of preserving the efficiency incentives of the public service providers has led the Commission to switch from an ex post approach to an ex ante approach. To be more precise, the Commission is switching from an ex post annual approach, where, on the basis of the annual accounts, the public authorities check the absence of overcompensation every year (with only limited possibilities to carry over the possible overcompensation), to an ex ante multi-annual approach. Here, on the basis of the financial perspectives of the project, the public authorities check the absence of overcompensation over the whole duration of the entrustment<sup>42</sup>.

This gives public authorities more flexibility in the way they grant aid over the duration of the entrustment, as long as there is no overcompensation over its whole duration.

#### *Reasonable profit*

The change to an ex ante approach is reflected in:

- the perspective for assessing the profit: the Framework provides that the "profit will be assessed from an ex ante perspective (based on expected profits rather than on realised profits) in order not to remove the incentives for the undertaking to make efficiency gains"<sup>43</sup>;
- the indicator chosen to reflect the return on capital: the Framework provides that "The rate of return on capital is defined as the Internal Rate of Return (IRR) that the company makes on its invested capital over the lifetime of the project, that is to say the IRR on the cash flows of the

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<sup>40</sup> In case the compensation mechanism is an upfront payment, the compensation is equal to the expected costs: the undertaking bears the total loss due to the fact that it was less efficient than expected.

<sup>41</sup> Point 38 of the Framework.

<sup>42</sup> Point 47 of the Framework.

<sup>43</sup> Footnote (3) (OJ C 8, 11.1.2012, p.18).



contract"<sup>44</sup>. The IRR illustrates that the Commission takes a more contract-based perspective. It allows for compensation schemes that are more ex ante oriented, in that the compensation is based, at least partially, on forecasted costs and revenues over the lifetime of the contract (instead of realised costs and revenues). In doing so, it provides greater incentives for SGEI operators to become more efficient over time. However, where justified, it is also possible to use more ex post oriented accounting measures of the profit like the average return on equity, the return on capital employed, the return on assets or the return on sales.<sup>45</sup>

Whatever indicator is chosen, the Member State must provide the Commission with evidence that the projected profit does not exceed what would be required by a typical company considering whether or not to provide the service, for instance by providing references to returns achieved on similar types of contracts awarded under competitive conditions<sup>46</sup>.

Regarding the level of profit which can be considered reasonable, the provisions in the 2011 Framework are similar to those in the 2011 Decision:

- swap rate + 100 basis points constitutes a safe harbour, under which profit is considered to be reasonable in any event<sup>47</sup>. This is a new provision compared to 2005, and aims to simplify the application of the rules and provide for a safe harbour;
- where the SGEI provision is connected with a substantial risk, for instance because the compensation takes the form of a fixed lump sum payment covering expected net costs and a reasonable profit and the undertaking operates in a competitive environment, the reasonable profit may not exceed the level that corresponds to a rate of return on capital that is commensurate with the level of risk<sup>48</sup>;
- as mentioned earlier, the swap rate + 100 basis points constitutes a limit for the profit when no risk is incurred (in particular when there is full ex post compensation)<sup>49</sup>. This is also a new measure compared to 2005, aimed at discouraging the use of full ex post compensation mechanisms.

*Provisions applicable to undertakings also carrying out activities outside the scope of the SGEI or providing several SGEIs*

The principles to be applied in respect of undertakings also carrying out activities outside the scope of the SGEI or providing several SGEIs<sup>50</sup> remain unchanged from 2005:

- internal accounts must show separately the costs and revenues associated with the SGEI and those of the other services;
- in case the undertaking makes excessive profits from exclusive rights, those excessive profits should be used to finance the SGEI.

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<sup>44</sup> Footnote (4) (OJ C 8, 11.1.2012, p.18).

<sup>45</sup> Point 34 of the Framework.

<sup>46</sup> Point 35 of the Framework.

<sup>47</sup> Point 36 of the Framework.

<sup>48</sup> Point 37 of the Framework.

<sup>49</sup> Point 38 of the Framework.

<sup>50</sup> Points 44-46 of the Framework.

However it is worth noting that following the switch to the ex ante perspective, the 2011 Framework requires that the reasonable profit on the activities for which the undertaking holds special or exclusive rights has to be assessed from an ex ante perspective, in light of the risk, or absence of risk, incurred by the undertaking in question. This preserves the incentive for the undertaking to provide efficiently the services for which it enjoys exclusive rights.

### *Monitoring of overcompensation*

The control of overcompensation should not bring about an ex post approach which would remove efficiency incentives. Therefore, it has to be carried out on the basis of the entrustment act provisions. For instance, where the entrustment act specifies that the provider will receive an upfront payment, monitoring of overcompensation should in principle be limited to checking that the level of profit to which the provider is entitled under the entrustment act is indeed reasonable from an ex ante perspective<sup>51</sup>.

Overcompensation should be monitored at the end of the entrustment act and at intervals of not more than two years for aid granted by means other than public procurement procedure with publication (three years otherwise)<sup>52</sup>.

### *Net avoided cost methodology*

Last, the 2011 Framework includes a novelty aimed at better estimating the economic cost of the public service obligation so as to fix the compensation amount at the optimal level. This new element relates to the method used to calculate the net cost of the SGEI and therefore the compensation which can be granted.

The 2005 Framework was based on the cost allocation methodology, under which costs that are common to the SGEI and other activities of the same provider are allocated based on allocation keys. The 2011 Framework switches to the net avoided cost methodology. Under this methodology, the cost of the SGEI is calculated as the difference between the net cost for the undertaking of operating the SGEI and the net cost for the same undertaking without the SGEI entrustment.

For instance, the costs of a postal sorting centre used both for parcels covered by the SGEI and for parcels outside the SGEI are allocated to the two categories of products in proportion to the number of parcels falling in each category. For instance 70% of the costs of the sorting centre are allocated to the SGEI and 30% to purely commercial services. Under the net avoided cost methodology, to determine the costs of the sorting centre attributable to the SGEI, it is necessary to determine whether the centre would have had to be kept in place if the undertaking no longer had a public service obligation. For instance, if the sorting centre would have been kept with only 40% of its staff, then all fixed costs of the sorting centre + 40% of staffing costs should be attributed to the purely commercial services, and 60% of the staffing costs should be attributed to the SGEI.

The main advantage of switching to the net avoided cost methodology is that it provides a better estimate of the economic burden of the public service obligation, because it takes account of the decisions which would be made in the absence of such an obligation. Pursuant to the

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<sup>51</sup> Point 50 of the Framework.

<sup>52</sup> Point 49 of the Framework.

telecommunication<sup>53</sup> and postal<sup>54</sup> directives, the net avoided cost methodology should be used to calculate the cost of a universal service obligation in these specific areas.

The main disadvantage is that it requires establishing a counterfactual scenario of what the costs would be without public service obligations, which could be complex to do and to monitor. But the new Framework also allows alternative methodologies when the net avoided cost methodology is not feasible or appropriate. The complexity of the net avoided cost methodology is also why it was not considered to be appropriate (at least not as a method to be used in the first instance) under the SGEI Decision.

It is impossible to say whether the net avoided cost methodology leads to lower compensation than methodology based on cost allocation, since it all depends on the counterfactual scenario.

#### **4.2.1.9. Transparency**

The Framework provides that for each SGEI compensation falling within its scope, the Member State concerned must publish a number of information elements, including the amounts of aid granted to the undertaking on a yearly basis<sup>55</sup>.

This measure is aimed at reinforcing transparency and improving compliance with the rules.

#### **4.2.2 Simplified assessment<sup>56</sup>**

The Commission found that it would not be appropriate to apply a number of Framework provisions to public service compensations which would normally be covered by the Decision but which failed to fulfil all the conditions of the Decision.

For instance, public service compensation below EUR 15 million or public compensation for hospitals and social services would not be covered by the Decision because the reference to the Decision would not be in the entrustment act. Such public service compensation would have to be notified and assessed on the basis of the Framework.

However, considering the amount of the aid (below EUR 15 million) and/or the sector concerned (hospitals and social housing), it would not be proportionate to apply certain provisions of the Framework, in particular those aimed at taking better account of efficiency and competition.

This is why the Framework provides that the following do not apply to compensations below EUR 15 million, to compensations for hospitals and social services and to compensations for transport covered by article 2(1) of the Decision: the existence of a public consultation on the public service needs; compliance with Union public procurement rules; the absence of discrimination; use of the net avoided cost methodology; introduction of efficiency incentives in the compensation mechanism; and the additional requirements for particularly distortive cases.

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<sup>53</sup> Directive 2002/22/EC of the European Parliament and of the Council of 7 March 2002 on universal service and users' rights relating to electronic communications networks and services (Universal Service Directive).

<sup>54</sup> Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on common rules for the development of the internal market of Community postal services and the improvement of quality of service, such as amended by Directive 2002/39/EC and Directive 2008/06/EC.

<sup>55</sup> Point 60 of the Framework.

<sup>56</sup> Section 2.11 of the Framework.

#### 4.2.3 Substantive assessment of competition and trade distortions<sup>57</sup>

##### *Overcompensation, necessity and balancing tests*

The compatibility test under the 2011 Decision and Framework can be summarised as checking the existence of an entrustment act and the absence of overcompensation. For certain cases, however, a more far-reaching test was considered appropriate.

Under Article 106(2) TFEU, the granting of State aid needs to be necessary to ensure the provision of the SGEI (i.e. the SGEI cannot be provided without State aid). So the granting of State aid is dependent on whether it would have been possible for the Member State to avoid the granting of State aid. This can be the legal basis for a necessity test, where the Commission would examine if there were alternatives to the granting of the aid to the beneficiary undertaking: for instance aid given directly to users or an SGEI compensation in compliance with the *Altmark* requirements.

A step further would be for the Commission to apply a balancing test on the basis of Article 106(2). The second sentence of Article 106(2) states that the SGEI must not affect the development of trade to an extent as would be contrary to the interest of the Union. This can be interpreted as meaning that even if the aid is necessary for the provision, the Commission could still find that the aid is not compatible because it affects the development of trade to an extent contrary to the interests of the Union.

However, necessity and balancing tests could have far-reaching implications. Under strict necessity logic, the Commission could conclude that the aid is forbidden because, considering that the compensation could have been granted in compliance with the *Altmark* criteria, the aid was not necessary. Only where the Member State could argue that it was not possible to grant compensation complying with the *Altmark* conditions could the aid be authorised. This would probably lead to a drastic reduction of State aid for SGEI (but not necessarily to reduction of the compensations).

Member States may view such far-reaching tests, if applied across the board, as a blow to their discretion in organising and providing SGEI, and as a risk in terms of legal certainty. Member States' discretion is explicitly guaranteed under Protocol 26 to the Treaties.

##### *A competition test limited to the most serious competition distortions.*

The Commission therefore decided that any competition test under Article 106(2)(2) TFEU had to be very closely confined to the most serious competition distortions. This limitation is clearly spelled out in the text to address Member States' concerns about their discretion when defining and organising the SGEI and about legal certainty. This was achieved by clearly defining a series of circumstances in which the SGEI has the potential to generate particularly serious competition distortions in the internal market. This potential could, for example, be the result of:

- bundling a series of tasks which cannot be justified by economies of scale,
- an entrustment leading to the foreclosure of a competitive market (for instance because the tariff set by the public authorities for the SGEI is too low to enable competitors to enter or stay on the market), while no competitive procedure was carried out to select the provider,

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Section 2.9 of the Framework.

- an aid granted on the basis of an entrustment connected with special or exclusive rights, where those exclusive or special rights provide for advantages which cannot properly be apprehended by the methodologies to calculate the net cost of the public service obligations (as highlighted by the postal Directive<sup>58</sup>, public service obligations may not always constitute an "unfair burden" even if they entail a net cost),
- an aid allowing financing the creation or use of a network that is not replicable and enables the public service provider to foreclose the market,
- an aid granted on the basis of an entrustment, which hinders the implementation or enforcement of the Union legislation aimed at safeguarding the functioning of the internal market (for instance, in the energy sector, the Commission could examine whether an aid is necessary to ensure security of supply or whether security of supply could be ensured by implementing the provisions of the sectoral Union legislation<sup>59</sup>).

The main objective of this competition test under Article 106(2)(2) TFEU is not to reject outright Member States' proposals for SGEI compensation in a given field. The test under Article 106(2)(2) will primarily be used to require conditions aimed at mitigating a specific competition concern. It could, for example, result in a decision under which the aid to create a network/infrastructure is only authorised if competitors get access to this network. Only if no other means to address the competition distortion were available would the test lead to the conclusion that the compensation cannot be declared compatible.

#### *4.3 Application and transitional measures*

The temporal scope of the Framework's application is extended: the Framework applies to all notified projects, even if notified before the Framework's entry into force (on 31.01.2012), and to unlawful aid even if granted before the Framework's entry into force, with some exceptions for the main novelties.

Summary of the provisions relating to the application of the Framework:

Type of aid	Application of the Framework	Point
Notified aid	The Commission will apply the principles set out in the Framework to all aid projects notified to it and will take a decision on those projects in accordance with those principles, even if the projects were notified prior to the entry into force of the Framework	68
Lawful individual aid	Individual aid which was granted before the entry into force of the revised Framework and approved under the 2005 Framework is not affected by the revision	

<sup>58</sup> Article 7(3) of the Postal Directive: "Where a Member State determines that the universal service obligations [...] entail a net cost [...] and represent an unfair financial burden on the universal service provider(s), it may introduce (a) a mechanism to compensate the undertaking (s) concerned from public funds;; or (b) a mechanism for the sharing of the net cost of the universal service obligations between providers of services and/or users."

<sup>59</sup> Article 3(2) of the Electricity and Gas Directives state that the public service obligations "shall be clearly defined, transparent, non-discriminatory, verifiable and shall guarantee equality of access for electricity undertakings of the Community to national consumers..."

Unlawful aid	The Commission will apply the principles set out in the Framework to unlawful aid on which it takes a decision after 31 January 2012 even if the aid was granted before this date. However, where the aid was granted before 31 January 2012, certain requirements <sup>60</sup> which would have been difficult to anticipate do not apply.	69
Existing scheme	The Commission proposes as an appropriate measure that Member States publish a list of all existing aid schemes concerning public service compensations that are not in line with the revised Framework by 31 January 2013 and that they bring those schemes in line with the Framework by 31 January 2014.	70

## 5. Conclusion

The following table summarises the main changes in the 2011 Decision and Framework as compared to the 2005 Decision and Framework:

	2005	2011
Decision	<p>Scope of application:</p> <ul style="list-style-type: none"> <li>- Hospitals and social housing</li> <li>- Aid below EUR 30M per year for providers with turnover below EUR 100M per year</li> </ul> <p>Compatibility conditions:</p> <ul style="list-style-type: none"> <li>- Entrustment + overcompensation test</li> <li>- Annual approach with monitoring every year</li> </ul>	<p>Scope of application:</p> <p>Entrustments shorter than 10 years (except if a significant investment is required), in the following cases:</p> <ul style="list-style-type: none"> <li>- Hospitals and social services: "health and long term care, childcare, access to and reintegration in the labour market, social housing and the care and social inclusion of vulnerable groups"</li> <li>- Aid below EUR15M per year</li> </ul> <p>Compatibility conditions:</p> <ul style="list-style-type: none"> <li>- Entrustment + overcompensation test</li> <li>- Multi-annual approach with intermediate monitoring of overcompensation at least every three years</li> <li>- Safe harbour and limit for reasonable profit</li> </ul>
Framework	<p>Compatibility conditions :</p> <ul style="list-style-type: none"> <li>- Genuine SGEI</li> <li>- Entrustment act</li> <li>- Overcompensation test (annual check)</li> </ul>	<p>Compatibility conditions:</p> <ul style="list-style-type: none"> <li>- Genuine SGEI</li> <li>- Entrustment act</li> <li>- Duration of the entrustment period</li> <li>- Compliance with transparency directive</li> <li>- Compliance with EU public procurement rules</li> <li>- Absence of discrimination</li> <li>- Overcompensation test based on ex ante multi-annual approach, efficiency incentives and the net avoided cost methodology</li> <li>- Strengthened transparency</li> <li>- Simplified assessment for aid normally covered by the Decision</li> <li>- Substantive assessment for particularly distortive aid</li> </ul>

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The consultation on the public service needs, compliance with Union public procurement rules, the absence of discrimination, use of the net avoided cost methodology, introduction of efficiency incentives in the compensation mechanism and publication of information including the amounts of aid granted.

In line with the objectives set out by the Communication adopted by the Commission on 23 March 2011 on the reform of the EU State aid Rules on SGEIs, the Decision and Framework now offer a more proportionate response to the different types of SGEIs and make the degree of State aid scrutiny more dependent on the nature and scope of the services provided. This has been done by exempting social services from the notification obligation and taking better account of efficiency and competition for large non-social SGEIs..

The Decision and Framework do not have an expiry date. Nonetheless, the Commission intends to review them by 31 January 2017. This review will be carried out notably on the basis of reports on the application of the Decision and Framework which the Member States have to submit to the Commission every two years<sup>61</sup>.

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Article 9 of the Decision and point 62 of the Framework.