Response by Linklaters LLP to the European Commission's Consultation on the Notice on the recovery of unlawful and incompatible State aid

We welcome the European Commission's ("**Commission**") consultation[1] on the draft Notice on the recovery of unlawful and incompatible State aid[2] ("**Draft Notice**"). Periodic updates of the Commission's notices, to reflect legal developments and to provide clarity regarding recurring questions in practical enforcement situations, are valuable for all stakeholders.

Our comments focus on certain aspects of the Draft Notice that in our view should be further clarified or nuanced. We share the view that expedient recovery is important. However, to safeguard the legitimacy of the State aid regime, increase legal certainty and avoid unnecessary litigation, it is important to involve all interested parties and not to lose sight of their rights. Recovery of State aid is, as the Draft Notice points out, not a penalty. To recover excessive amounts must not therefore be viewed in terms of offering "increased deterrence". Instead, it will lead to unjust enrichment[3], and is liable to distort competition in the same way as granting incompatible aid.

A. General principles (Section 2)

1 The obligation to recover (Section 2.3)

The Draft Notice (paragraph 24) states that since recovery of unlawful and incompatible State aid does not amount to a penalty, it can "***neither be regarded as disproportionate to the objectives of the TFEU with regard to State aid, nor as entailing unjust enrichment for the Member State concerned***".

Although this statement is correct as a matter of principle, we consider that it is nevertheless too absolute. The interpretation of State aid law is informed by other Treaty provisions and general principles of Union law. Whilst it can be rightly considered that the principle of recovery as such, being the consequence of the illegality, should be proportionate and not give rise to unjust enrichment, it does not follow that this will never be the case in practice. The statement also assumes that the amount to be recovered is always calculated in a correct way and does not exceed what is necessary to attain the goals of Union law. The current language suggests that there is an irrebuttable presumption that the recovery is proportionate and not in excess, which is not correct. We suggest adding the qualification ***"in principle"***, or a similar term, to the statement in paragraph 24.

2 Legal certainty and legitimate expectations (Sections 2.4.1.1 and 2.4.1.2)

The Draft Notice (paragraph 39 and footnote 46) suggests that legitimate expectations regarding the lawfulness of a certain measure cannot be based on an earlier decision from the Commission. However, this statement is contradicted by previous Commission decisions. For example, its decisions in SA.21233 - ***Spanish Aid for the acquisition of ships - Spanish Tax Lease*** and C45/2001 - ***Headquarters and logistics centres*** indicate that earlier

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1 Available here.

2 Communication from the Commission – Draft Commission Notice on the recovery of unlawful and incompatible State aid, available here.

3 Avoiding unjust enrichment is a general principle of Union law. See the judgment of the General Court of the European Union of 23 November 2004 in T-166/98, ***Cantina sociale di Dolianova***, EU:T:2004:337, paragraph 160.

findings by the Commission that a certain measure does not amount to State aid may give rise to legitimate expectations, provided that the cases are sufficiently similar.[4]

Indeed, any other interpretation of the principle of legitimate expectations would make it excessively difficult for Member States and interested parties to self-assess whether a certain measure qualifies as State aid. In fact, in the Commission's own no aid decisions adopted under Article 4(4) of the Procedural Regulation, it frequently invokes its own precedents to interpret the scope of Article 107(1) TFEU in analogous situations.[5] We suggest amending paragraph 39 to correctly reflect the role of the Commission's precedents.

3 *Res judicata* (Section 2.4.1.3)

The Draft Notice (paragraph 43) asserts that, while the rules implementing the principle of ***res judicata*** are a matter for the legal system of each Member State, final decisions by national courts regarding unlawful aid cannot render ***"an obstacle to drawing the necessary consequences from the breach of the standstill obligation***".

In support of this statement, the Draft Notice (in footnote 52) refers to the ruling of the Court of Justice of the European Union ("**CJEU**") in ***Klausner Holz Niedersachsen.***[6] However, we submit that the CJEU's position in that case is more nuanced than the Draft Notice suggests. The CJEU would arguably have reached a different conclusion if the national court had examined whether the measure at hand constituted State aid and concluded that it did not. Then the principle of ***res judicata*** would have applied, at national level, to prevent a second court from calling this finding into question. To apply the principle of ***res judicata***, which is common to the legal systems of the Member States, in this manner, is in our view fully compatible with the effectiveness of Union law. We suggest that this is clarified in the Draft Notice.

[4] Commission Decision of 7 July 2013 in SA.21233 — ***Tax regime applicable to certain finance lease agreements (also known as the Spanish Tax Lease System)***, paragraph 250; and Commission Decision of 13 May 2003 in C45/2001 — ***Headquarters and logistic centres***, paragraphs 81 and 82.

[5] See, for two recent examples, Commission decision of 26 October 2018 in SA.43260 – ***Germany - Alleged aid to Frankfurt Hahn Airport and Ryanair***, paragraph 201; and Commission decision of 20 September 2018 in SA.37389 – ***Italy Alleged illegal State aid in the Port of Naples***, paragraph 33.

[6] Judgment of the CJEU of 11 November 2015 in C-505/14, ***Klausner Holz Niedersachsen***, EU:C:2015:742.

B. Roles of the Commission and the Member States (Section 3)

1 Role of national courts

National courts play an important role in State aid recovery. For the sake of completeness, we suggest including in the Draft Notice at least a cross-reference to the Commission's notice on the enforcement of State aid law by national courts.[7]

2 Participation and rights of interested parties

In the 2018 Code of Best Practices for the conduct of State aid control procedures, the Commission recommends the involvement of aid beneficiaries during the formal investigation procedure.[8] This is a welcome clarification. In our experience, the participation of aid beneficiaries is equally important during the recovery phase. However, the Draft Notice does not refer to the participation or the information rights of aid beneficiaries.

The Draft Notice also does not mention the role of the complainant. The complainant has a legitimate interest in knowing whether the distortion of competition has been eliminated.

In this respect, it would be useful to recall that Member States, when implementing Union law, must respect not only the principles of sincere cooperation and primacy (as mentioned in Section 2 of the Draft Notice), but also the procedural rights of interested parties under Union law, such as the right to good administration and the rights of defence.[9] The right to good administration comprises the right to be heard and to have access to the file. Respecting these rights is, in our view, particularly important when the Member State itself shall quantify the amount of the aid to be recovered.

Moreover, the Draft Notice arguably omits to consider that the interests of Member States and aid beneficiaries often diverge. Indeed, Member States may have strong economic motives for interpreting and applying the State aid rules in a manner which enables them to obtain restitution of monies paid in the past. Such motivation may also be political.

This means that there is always a latent risk that Member States seek to use the State aid rules (including recovery proceedings) for a purpose other than that for which they were intended. This cannot be prevented unless proper safeguards are in place. As the Draft Notice correctly recalls (paragraph 59), the aim of recovery is not to maximise the Member States' return. We suggest adding that the rules must be applied so as to avoid any unjust enrichment for the Member States. As mentioned in the introduction, recovery of non-aid or sums in excess of the actual advantage of the aid beneficiary is liable to distort competition in the same way as granting incompatible aid.

More generally, the determination of the exact amounts to be recovered (in cases where the Commission's decision only provides a methodology) and the monitoring of the recovery proceedings take place in bilateral contacts between the Commission and the Member State concerned. There is no transparency on the outcome of such proceedings, except in cases where subsequent court proceedings may reveal issues having occurred. Beyond the legitimate interests of third parties, the general public should be informed about the result of recovery proceedings. They have a legitimate interest in an open and transparent process.

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[7] Commission notice on the enforcement of State aid law by national courts (OJ C 85, 9.4.2009, p. 1) (see Section 2.2.2).

[8] Code of Best Practices for the conduct of State aid control procedures (OJ C 253, 19.7.2018, p.14), paragraph 18.

[9] See Articles 41, 48 and 51 of the Charter of Fundamental Rights of the European Union.

In conclusion, it is submitted that involving the interested parties (aid beneficiaries as well as complainants), ensuring transparency and the respect of procedural rights, will lead to better decisions and avoid unnecessary litigation during the recovery process, and that some form of wider publicity or reporting should be provided.

C. Implementing the recovery decision (Section 4)

1 Identification of the aid beneficiary in a group context (Section 4.3.1)

The Commission has interpreted Article 107(1) TFEU to mean that a group of undertakings can be an aid beneficiary, by applying the "single economic entity" doctrine.

However, a recovery claim can only be enforced under national law against an entity with legal personality. Moreover, in our view there is no support in the case law for holding ***any*** entity within the group liable for recovery. Even if recovery is not a penalty (see above), the recovery claim must still be based on an attribution of responsibility, and this attribution must be personal. The recovery claim is essentially a claim for restitution, and there is no reason for considering the principle of personal responsibility inapplicable to such a claim. Similarly, the removal of the distortion of competition must occur at the level of the actual beneficiary, and the market where it operates, in order to restore competition. We suggest that this is clarified in the final notice or, at least, to remove any language suggesting the contrary.

2 Extension of the recovery order, economic continuity (Section 4.3.2)

We welcome that the Commission has included a section about economic continuity. However, considering the complexity of these issues, it would be helpful to explain in greater detail, in the main text, some of the issues addressed in the footnotes.

3 Quantification of the amount to be recovered and tax effects (Section 4.4)

In our experience, even when the Commission itself quantifies the amount of aid to be recovered, it does not always take into account the taxes paid by the aid beneficiaries on this amount. Indeed, this effect is often extrinsic to the aid measure as such, and is therefore often disregarded or miscalculated.

Moreover, since the aid beneficiary is not a party to the formal investigation procedure, it has no right to be heard and to explain the tax effects to the Commission prior to the adoption of the final decision. The Member State's right to be heard offers no guarantees to the aid beneficiary, since the Member State might not be fully cognisant of the tax impact or, even if it is, might have few incentives to raise this issue with the Commission (since, as previously discussed, it may have an interest in maximising the amount to be recovered).

However, once the Commission has adopted its decision, national authorities and courts will for obvious reasons be reluctant to deviate from the quantification made by the Commission, even if the Commission decision manifestly fails to take into account the tax impact.

While the Commission's decisions can be appealed to the Union courts to rectify errors, it would be helpful, for all stakeholders, to be able to settle the question concerning the necessary tax corrections without recourse to the Union courts. In this regard, one might envisage various alternatives, such as providing for the mandatory involvement of the aid beneficiary during the formal investigation. Another option would be for the Commission's

decisions to fix the gross amount to be recovered, prior to tax effects, and delegate to the Member States to calculate the net amount pursuant to the guidelines in the recovery notice.

Moreover, the Draft Notice (paragraph 101) refers to the "income tax" paid by the aid beneficiary. We suggest referring to "taxes" in general, since the aid beneficiary may have had to pay taxes other than income tax on the amount of aid received.

Lastly, the Draft Notice (paragraph 106) states that: "***if a Member State increases the tax base following a Commission declaration of incompatibility of a tax deduction, other tax deductions which were already available at the time the initial tax was due could in principle still be applied***". The availability of such deductions can have a major impact on the outcome of the case: both to determine whether aid has been granted and to quantify the amount of aid.[10] The Draft Notice (footnote 109) mentions certain conditions that such tax deductions must fulfil: ***"(i) they shall not lead to any (new) State aid; (ii) they should concern all taxpayers in the same way; (iii) they shall apply by way of a rule that existed at the time the incompatible aid was granted; and (iv) the undertakings eligible to the deductions must benefit from them automatically (i.e. the application of the deduction does not require prior authorisation from the Member State nor the activation of an option in due time by the taxpayer)***". These conditions are inspired by the rules governing the finding of a tax measure as State aid or not. Whilst we agree that tax deductions should not amount to new State aid, we submit that the situation regarding the calculation of the "net" amount of aid is different. Indeed, such determination is governed by the national tax provisions as they were actually applied to the amounts of aid received. We consider that the conditions listed in footnote 109 are overly harsh, formalistic, and not supported by case law. Applying them in a literal manner risks leading to unjust enrichment for the Member State in question.

4 Calculation of recovery interest (Section 4.4.2)

The Draft Notice (paragraph 110) mentions the tool used to calculate recovery interest according to the rules established by the Implementing Regulation, but then states (footnote 112): "***Access to the tool is granted following a registration process at both national and Union level. This registration ensures that only the authorised officials of the authorities of the Member State concerned and of the Commission's services can access the tool"***.

We see no valid reason for limiting access to the tool for calculating the recovery interest to the Commission and the Member States. Other stakeholders, in particular the aid beneficiary, also have a legitimate interest in being able to quantify the exact amount of recovery interest. We therefore think that this tool ought to be publicly available.

Further, in relation to calculation of the interest, we suggest recalling that the date when the aid is "made available" to the aid beneficiary is not necessarily the same date as when the aid is "awarded", since the "award" date refers to the date of the promise made vis-à-vis the aid beneficiary. But the aid may be paid and be "made available" at a later date. In our experience, some national authorities confuse these concepts.

5 Provisional implementation and alternative means of recovery (Sections 4.6 and 4.7)

We welcome the added clarity offered by these sections and only have minor comments.

[10] See, for a recent example, the judgment of the General Court of the European Union of 26 February 2019 in T-865/16, ***Fútbol Club Barcelona v Commission***, EU:T:2019:113.

According to the Draft Notice (paragraph 123), "***Provisional implementation of the recovery decision can be achieved, for instance, by way of a payment by the beneficiary of the full recovery amount into an escrow account"***. In our view, it would be helpful to clarify that no interest accrues as from payment of the amount into the escrow account, since the aid is no longer at the disposal of the beneficiary once it has been deposited into this account.

On a separate point, when explaining the basic principles applicable to recovery in kind, the Draft Notice (paragraph 123) states that: "***It must be avoided that economic activities are carried out using the beneficiary's assets for a certain period of time after the decision (at least until full depreciation of those assets according to standard accounting rules). On this point, reference is made to the criteria for evaluating the existence of economic continuity set out in paragraph 91***". We understand that the purpose of this requirement is to prevent the aid from distorting competition through the continued use of the asset. We assume that the reference to paragraph 91 of the Draft Notice means that such continued use is only relevant for this purpose if the asset used for recovery in kind meets the requisites for "economic continuity" (which is normally not the case). We suggest clarifying the drafting.

Linklaters LLP

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