

MONOPOLKOMMISSION

The “More Economic Approach” in European State Aid Control

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The “More Economic Approach” in European State Aid Control^{†*}

1. Introduction

1.1 The Issue

1. The idea of a “more economic approach” is widely discussed in the general public † and in research on European competition policy. The Directorate-General for Competition of the European Commission has for some years been pursuing the aim of gradually redirecting competition law towards a more economic approach. The aims and substance of the new approach are the subject of much controversy amongst economists and legal experts. So far European antitrust law has been the main focus of the general interest¹ (Arts. 81, 82 EC Treaty and the EC Merger Regulation), together with the reforms in this field proposed by the European Commission.² However, the regulations in EU antitrust law, which are intended for companies operating on the European internal market, are not the subject of this chapter. The concern here is the possible application of a more economic approach in the field of EU state aid control (Arts. 87ss. EC Treaty). These articles form the second part of the European rules on competition, and they deal with restraints of competition caused by sovereign states through state aid. The European Commission intends to reform this area fundamentally by applying a more economic approach.³ The present European Commissioner for Competition, Neelie Kroes, attaches considerable importance to reform of the legislation on state aid, indeed she calls it the “flagship project” of her term in office.⁴

2. The new approach in state aid law is not the same as the methods and concepts which the European Commission applies as a more economic approach in EU antitrust law. Certainly, just like EU antitrust law, the legislation on state aid is designed to protect competition in the common market.⁵ Nevertheless, there are decisive differences. In the legislation on state aid the instigators of possible restraints of competition are not companies and market participants but sovereign states. Moreover, other aims beside economic objectives – social and distribution policy and cultural interests – are important in the law on state aid. European state aid

† The German *Monopolkommission* (Monopolies Commission), www.monopolkommission.de, is an independent advisory body to the German Government in the areas of Antitrust and Regulated Industries (a.o. Telecommunications, Energy, Mail and Railways). In its Biennial Reports (this document is a translated version of Chapter VI of the Biennial Report 2006/2007, published 2008) and in its Special Reports, the Monopolkommission scrutinizes systematically for systemic and economic soundness the decisional practice of the *Bundeskartellamt* (German Competition Agency) and of the *Bundesnetzagentur* (German Regulatory Agency for Network Industries) as well as the underlying legal framework, to a lesser but growing extent also the EU Commission's enforcement policy. While without decisional powers, the Monopolkommission's recommendations in the past were regularly followed both by Agencies and the Legislator.

* The Monopolkommission would like to thank Mrs. Eileen Martin for translating the original German text into English.

1 The term “antitrust law” is used very broadly in this chapter, covering all the competition regulations that concern companies, including merger control.

2 Currently in particular aspects of abuse control, Art. 82 EC Treaty.

3 In discussing the desired reform of state aid control the European Commission uses the expression “re-fined” economic approach as well as a “more economic” approach.

4 Neelie Kroes, “European Competition Policy in a changing world and globalised economy: fundamentals, new objectives and challenges ahead”, SPEECH/07/364, GCLC/College of Europe Conference on “50 Years of EC Competition Law”, Brussels, 5 June 2007.

5 This is already evident in the subdivisions in the law. The chapter “Rules on Competition” in Title VI of the EC Treaty is divided into “Section 1 – Rules applying to undertakings” and “Section 2 – Aids granted by States”. While Section 1 contains Arts. 81 to 86 of the Treaty with the antitrust regulations, Section 2 contains the European regulations on state aid (Arts. 87 to 89 EC Treaty).

control is also characterised by a transfer mechanism. The grants are paid out of tax revenue, which in turn causes loss of welfare, or revenue is absorbed that could be used for other purposes (opportunity costs).

1.2 State Aid as a Particular Form of Subsidisation

1.2.1 The Concept of State Aid

3. The concept of state aid is used in European law for subsidies to which the European ban on state aid in Art. 87, Para. 1 EC Treaty applies.⁶ State aid is defined as follows: “Save as otherwise provided in this Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market.”

So five conditions must be met for a measure to be classified as state aid and be subject to European state aid control:

- It must “favour” certain companies or production processes, that is, it must create an economic advantage for the recipient.
- It must be granted to “certain undertakings or the production of certain goods”, so it must have a selective effect.
- It must be granted “by a member state or through state resources”. So only a transfer of a member state’s resources, not aid granted by the EU itself, is state aid.
- It must also “distort or threaten to distort competition”.
- It additionally must “affect trade between member states”.

4. Measures that qualify as state aid are on principle incompatible with the common market under Art. 87, Para. 1 EC Treaty. Under Art. 88, Para. 3, Sentence 1 EC Treaty member states must inform the European Commission of any aid which they intend to introduce or alter early enough for the European Commission to respond (obligatory notification).⁷ The European Commission will examine whether a particular aid may by way of exception be permitted, for the ban in Art. 87, Para. 1 EC Treaty is not absolute. The Treaty lists a number of conditions that will allow an exemption to be made (Art. 87, Paras. 2 and 3, Art. 86, Para. 2), and these are in general terms which allow the European Commission wide scope for judgement in exercising its control. State aid for economic purposes can be approved, for example, if the measure is “to facilitate the development of certain economic activities or of certain economic areas” (Art. 87, Para. 3 c)). Secondly, the EC Treaty also allows aids with a social or distribution policy background – especially aids to promote disadvantaged regions⁸ or aid for cultural objectives⁹ – to be exempt.

6 In practice the term “state aid” is used in a very different ways. In the national accounts drawn up by the German Federal Statistical Office, and consequently in fiscal policy economics, a narrow concept is used, meaning only positive financial grants (monetary transfers) to companies. Cf. Federal Statistical Office, Statistisches Jahrbuch 2007, p. 439; Brümmerhoff, D., Finanzwissenschaft, Munich 2007, pp. 17ss. But the Kiel Institut für Weltwirtschaft, for example, holds the view that all the advantages that are distorted by the allocation of macroeconomic resources should be designated state aid. Cf. Boss, A., Rosenschon, A., Beihilfen in Deutschland: Eine Bestandaufnahme, Kieler Arbeitspapiere, No. 1267, Kiel 2006, pp. 4ss.

7 The obligatory notification only applies to “new aids”, cf. Art. 1, c) of Procedural Regulation No. 659/1999. For “existing aid” (cf. definition in Art. 1, b) of the Procedural Regulation), the procedure laid down in Art. 88, Paras. 1 and 2 EC Treaty applies.

8 Art. 87, Para. 3 a) and c), EC Treaty.

9 Art. 87, Para. 3 d) EC Treaty.

5. It will already be clear that European supervision of state aid – unlike the application of the antitrust regulations (Arts. 81 and 82 EC Treaty, merger control regulations) – is a political part of European competition law. Beside aspects of competition policy social and distribution policy aspects also play an important part. In judging an aid the European Commission must weigh these aspects against each other as well as considering the effects on competition.

1.2.2 *The Macroeconomic Importance*

6. The aids given by member states that fall under European control of state aid are of great macroeconomic importance. The level of all the aids granted in the EU has fallen, from an average of EUR 104 billion in the years 1993 to 1995, but according to information from the European Commission it was still EUR 67 billion in 2006.¹⁰ That is a ratio of about 0.6% of the EU gross domestic product (GDP).

7. The level of aid granted varies between member states, in some cases considerably. In absolute figures Germany was in the lead in 2006, with EUR 20 billion, or 30% of the entire volume of aid given in the EU. It was followed by France with EUR 10 billion, Italy with EUR 5.5 billion and Spain with EUR 5 billion. Measured by GDP other member states are relatively higher on the list. But Germany gave 0.87% of its GDP in financial aids and so was above the EU average of 0.58%.¹¹

8. EU statistics on the distribution of state aid by economic sector in percent of total state aid show that the greater part, 66%, of the state aid granted in Germany flows into manufacturing (EU average 58%), with 20% going to agriculture (EU average 24%) and 11% to hard coal mining (EU average 5%). Of the aid granted for horizontal effect, that is, not intended right from the start for specific sectors but to serve objectives in every sector, the aid given for environmental protection measures and energy saving in Germany tops the list.¹² The above-average aid granted for environmental protection and hard coal mining in Germany is the main reason for the high level of state aid in this country compared with the other EU member states.¹³

10 CF. Commission Report, State Aid Scoreboard, Autumn 2007, COM(2007) 791 final, p. 3, fn.1 The figure quoted includes aids for the manufacturing industry, the services sector, coal mining, agriculture, fisheries and parts of the transport sector. But it does not include aids for rail transport or compensation payments for services of general economic interest (for more detail see 5.4.3), as according to the Commission comparable data was not available. The nominal level of EU aid shown is relatively low compared with the volume of subsidies, namely EUR 45.8 billion, shown in the 21st Subsidisation Report of the Federal Government, just for Germany in the same period, 2006. The figure consists of the financial aids and tax concessions granted by the Federal Government, the Länder and the municipalities without the expenditure by the EU on market regulation and without the ERP financial aids. Cf. Bericht der Bundesregierung über die Entwicklung der Finanzhilfen des Bundes und der Steuervergünstigungen für die Jahre 2005-2008 (21st Subsidisation Report), p. 22. http://www.bundesfinanzministerium.de/nn_53848/DE/BMF_Startseite/Service/Broschueren_Besteller-service/Finanz_und_Wirtschaftspolitik/40200.property=publicationFine/pdf. However, it must be remembered in this context that the EU statistics, unlike the Federal Government's Subsidisation Report, only include pure grants, that is, in exchange contracts only the subsidisation equivalent is calculated and shown compared with the assumed behaviour of a private investor.

11 Malta was in the lead with 2.29% of GDP, followed by Latvia with 1.8%, Finland with 1.53%, and Sweden with 1.15%. Great Britain (0.22%), Greece (0.26%) and Luxemburg (0.32%) all had particularly low levels,

12 This is probably due particularly to the selective exceptions created for German energy-intensive firms, for measures that affect all companies equally are not aid: the criterion of selectivity required under Art. 87, Para. 1 EC Treaty is not met. If all the companies producing in Germany were to be equally affected the measure would be a general economic policy measure and it would not appear in the statistics on state aid.

13 Cf. 21st Subsidisation Report of the Federal Government, loc. cit., p. 43.

1.3 Effects on Competition

9. Granting state aid involves various costs and has various repercussions. On the cost side, first the financing or opportunity costs must be taken into account, as must the welfare losses incurred by the need to raise taxes in other areas (the “shadow cost” of taxation). In addition, state aid can lead to inefficient use of public funds through free riding and erroneous prognoses.

10. In addition to the economic costs there is the danger of disadvantageous effects on competition. The considerable distortion to competition that state aid can cause on the product and services markets affected can be of immense importance for competition policy. Restraints of competition thus induced create misguided incentives in allocative, productive and dynamic respects.

11. In regard to allocation it should be borne in mind that existing resources can be drawn into less productive use through state aid. If competition is workable the market will send clear signals to suppliers on which products and services consumers want. If a state aid induces the companies favoured to lower their prices, these signals may be distorted, and so more resources are used for the subsidised activity. If an entire sector is favoured this can have disadvantageous effects on other sectors. Moreover, finance is withdrawn from market participants in other branches in their function as taxpayers. Such allocative misguidance is evident, for example, in coal mining.

12. State aid can also mean that less efficient companies are artificially maintained, thus making it more difficult for new and efficient companies to enter the market. The productive efficiency of companies can also be impaired if they use their resources for rent-seeking activities, whereas if the market forces were free to operate they could use them productively. And companies have less incentive to produce efficiently and invest if they can assume that the state will come to their aid (to save jobs) if they are in financial difficulties (reducing cost pressure).

13. If state aid changes the profitability of an investment companies may be induced to change the level, nature and timing of their investment. In this way distorting investment decisions may be made and dynamic efficiency impaired.

14. State aid that helps to increase the market power of a single company is particularly problematic. Granting state aid to established companies can result in a barrier to market entry for newcomers, help to seal off the domestic market and facilitate displacement practices. If the company can also transfer market power thus acquired to adjoining markets through cross-subsidisation the competition problem is further intensified.

2. Possible Purposes in Granting State Aid

2.1 Types of State Aid

15. State aid can be found in many forms; the differences are:

- the form in which it is granted¹⁴,
- if it is tied to specific projects¹⁵,

¹⁴ For instance, a loan or tax concession.

¹⁵ The aid can be tied to a specific activity or given as operational aid which the company is free to use as it will.

- the absolute amount and size relative to the costs of the activity subsidised,
- the method of giving the aid¹⁶,
- the duration¹⁷,
- the breadth of the effect¹⁸, and
- the purpose for which the aid is given.

16. The purposes for which state aid is given will now be examined in more detail, in order to assess the suitability of aid as an economic policy instrument. These purposes play a big part in the legality of state aid. State aid can serve to cure market failure. Removing market failure is the classical economic justification for granting state aid and other forms of subsidisation. The classical features of market failure are discussed in 2.2. But there are also aims outside economics which state aid is intended to achieve. These non-economic aims are the subject of 2.3.

2.2 Compensating for Market Failure as a Reason for Granting State Aid

17. On principle state aid can help to reduce market or competition failure. The causes of market or competition failure given in the economic literature are serious external effects, public goods, natural monopolies, asymmetrical information and adjustment shortfalls. It must always be remembered that intervention by the state often itself leads to inefficiencies that in turn can lead to state or policy failure. The main factors that lead to state or policy failure when state aid is granted can be lack of information, erroneous analyses and prognoses, delay in decision-making and in the effects of the use of the funds and misincentives within politics and the public administration. In view of this, before aid is granted an examination should be made using a comparative institutional economic approach, in which the possible market failure is weighed against the threat of state failure. Finally, market failure does not in itself justify state aid, the aid is only justified when it is particularly suited to correct this market failure.¹⁹

2.2.1 External Effects

18. Positive and negative external effects will occur if the activity of one economic subject (e.g. production or consumption) has effects on the benefit to other economic subjects (increasing or decreasing it), without these effects being taken into account in the market pricing system or without any other compensation.²⁰ External effects are the direct result of property rights that are inadequately defined or definable, or that cannot be adequately implemented.

19. Negative external effects are familiar from environmental policy. If those affected by environmental pollution have no enforceable property rights in the commodity environment, they will typically not succeed in preventing the pollution or in charging the (external) costs to the polluter. The failure to include these external costs in the market pricing mechanism (lack of internalisation) results in excessive environmental pollution. For instance, CO₂ emis-

16 For instance using a transparent tender.

17 The aid can be given as a single payment or in instalments.

18 State aid can be individual in nature and only benefit a specific company; but some state aid measures benefit all the companies in a certain sector; finally there is aid with a horizontal objective that is not limited right from the start to a specific economic sector.

19 Cf. Coase, R.H., *The Problem of Social Cost*, *Journal of Law and Economics* 3, 1960, pp. 1-44 and Demsetz, H., *Information and Efficiency, Another Viewpoint*, *Journal of Law and Economics* 12, 1969, pp. 1-22.

20 These effects are called external effects because they occur outside the voluntary market relations.

sion, such as occurs through electricity generation (especially from coal-fired power stations), has negative external effects, unless these costs can be internalised through appropriate political means (e.g. taxes or emission trading certificates).

20. The occurrence of positive external effects is for instance assumed in basic research. Basic research is characterised by the fact that third parties can hardly be excluded from benefiting from the knowledge gained, as the lack of possibilities for patenting mean that there are no enforceable property rights. As they cannot be excluded, third parties also profit from basic research without having to pay for this.

21. As property rights cannot be assigned, the price mechanism alone cannot ensure efficient market results in the case of either negative or positive external effects. In a pure market solution more than the economically efficient quantity of CO₂ would be emitted and less would be spent on basic research than economically efficient. In the case of serious external effects state intervention must aim to ensure that the divergence between costs and yields that are individually taken into account and actually incurred for society as a whole is eliminated by measures to internalise the external effects.

22. On principle state aid, e.g. in the form of an investment bonus for reducing pollution, can help to internalise negative external effects. State aid can have a similar effect on basic research. However, one must heed that the external effect must first be identified as serious and quantified in the form of external costs.²¹ Furthermore must be kept in mind that the assessment of the external effect is influenced by the decision-maker's subjective sensation and the level of his information. In addition, the period for observing the extent of the external effect or the level of the external costs is also relevant. Finally, state aid as an economic policy instrument must be examined for its particular suitability to internalise the external effects. As with taxes, the socially optimal quantity of a good can only be achieved approximately or in a lengthy process of trial and error. Moreover, in view of this granting state aid to the originator of a negative external effect seems dubious, because he is being rewarded for reducing or avoiding the external effect whereas in fact, the originator of the external effect should be obliged to bear the external costs thus incurred.

2.2.2 Public Goods

23. A good that creates no rivalry in consumption and thus can be used by many without marginal costs, and from the use of which no one can be excluded at justifiable expenditure and with justifiable means, is a pure public good.

24. In some economic literature the lack of rivalry in consumption is itself regarded as sufficient to identify a public good, the private provision of which without state intervention would lead to market failure.²² The lack of rivalry for an existing commodity means that additional demand for the same commodity does not require additional costs to provide it, that is, the marginal costs of an additional user are zero. In the ideal case, therefore, no-one should be

21 Strictly speaking, it is hard to imagine an economic activity that does not give rise to any positive or negative externalities (external effects are ubiquitous). If the state attempted to internalise all externalities this would be tantamount to comprehensive interventionism, which would paralyse much private economic activity.

22 Typical goods that are characterised by lack of rivalry in consumption are virtual goods like software and the contents of television and radio programmes and the Internet.

excluded from use of the good. However, at a zero price such good would never be produced in the private sector without subsidisation.²³

25. However, the lack of rivalry is not in itself sufficient to identify market failure. For if it is possible to exclude potential demand from use of the good a supplier can take the one-off provision costs into account in his pricing (e.g. with multi-part tariffs). In a comparative perspective this need not necessarily be inefficient supply.²⁴

26. Hence economists usually only speak of a public good and of market failure induced by it if potential users who are not willing to pay cannot be excluded with justifiable means, as property rights are not adequately defined or definable. Examples of a pure public good are the internal and external security of a country, or ensuring competition on markets. No consumer can be excluded from the advantages of competition with justifiable means, and no citizen can be excluded from his country's internal and external security.

27. Non-exclusivity leads to free riding. As no-one can be excluded from a public good no-one has a strong incentive to participate in financing it (unless forced to do so). As a result a pure public good can generally not be provided efficiently without state intervention.

28. Nonetheless, a public good need not necessarily be provided by the public authorities. It can be provided by private companies, if they can cover their costs with a public grant.²⁵ Such a grant can constitute state aid in the meaning of Art. 87, Para. 1 EC Treaty. However, if a proper tender has been held for the private provision of the public commodity, and the company that puts in the best bid in price and performance is awarded the contract, the public grant given in this context is not regarded as state aid by the European courts.²⁶

2.2.3 Size Advantages in Relevant Demand

29. Size advantages on the supply or demand side of the relevant market can give rise to a natural monopoly. In this case a single supplier will provide the quantity in demand on the market at the most favourable cost. Supply-side size advantages are to be found on electricity grids, for example, where they are caused mainly by installing dense electricity distribution networks.

23 This applies particularly in view of the fact that a supplier generally has fixed costs for providing a commodity. The provision of software, for example, which is also characterised by lack of rivalry in consumption, requires one-off research and development costs, while the costs of reproducing it are negligible.

24 This is evident on various markets for virtual goods, the provision of which is not characterised by general market failure. Moreover, the skimming pricing system is often used by innovators in early marketing phases, in order to ensure rapid amortisation of their research and development costs. It is a frequent strategy on the market for PC processor chips, for example, where it can be observed that the supplier who has developed the next generation of chips initially charges high prices, which come down markedly as soon as competitors put a chip of the same performance on to the market.

25 In Germany, for instance, some prisons have been part-privatised.

26 For more detail see 5.3.4.

30. Demand-side size advantages are created when major positive network effects occur. A positive network effect is the phenomenon that new demand for the same good increases the benefit to current users. A new user for an application software, for example, will increase the benefit to other users because he is an additional potential exchange partner (e.g. for text processing documents or information). The resultant desire to join as big a network as possible can in the extreme case lead to monopolisation of the entire market by one supplier.²⁷ A well known example of a demand-side induced (quasi-) monopoly is the application software Microsoft Office.

31. Often the marginal costs of a natural monopoly are below the average costs, so that a marginal cost price would cause a deficit for the operator of the monopoly. Deviating from the marginal cost price, on the other hand, leads to a loss of allocative efficiency, in contrast to the theoretical ideal case. In theory, state aid could be justified economically. In practice, however, natural monopolies do not generally require state aid. The loss of allocative efficiency is more of a theoretical nature and without practical relevance. In many cases natural monopolies actually require state price supervision, in order to protect users from exploitation by too high prices. These cases occur when the monopoly supplier is protected from potential competitors by high barriers to market entry and so can keep his price above competitors' levels.

2.2.4 Asymmetrical Information

32. There is asymmetrical information if one side of the market participants concerned is better informed than the other. The undesirable effects this causes can be moral hazard²⁸ and adverse selection.

33. There is asymmetrical information on credit markets, for example. The suppliers of loans are not fully informed of the exact risk of default posed by each borrower. Consequently they will set the interest rate for their loan (the price for the loan) by the estimated average default risk. Would-be borrowers with low individual risk of default (good risk customers) will regard this price as too high and may possibly decide against taking up the loan. Would-be borrowers that are an above-average risk, on the other hand (bad risk customers) benefit from the price, which is relatively favourable for them. The systematic displacement of the good risks by the bad (adverse selection) can in extreme cases lead to market failure, as beneficial transactions are not undertaken.²⁹

34. Particularly in regard to raising capital for small and midsize companies it is suspected that there are major information asymmetries that could cause market failure. It is assumed for both venture capital markets and for lending by banks in the private sector that the suppliers of capital systematically overestimate the risk of default on loans to this group of companies

²⁷ This will occur if one of a number of incompatible proprietary technologies has achieved a critical mass of demand. Owing to the positive back-coupling effect that then starts this technology, after achieving the critical mass, will attract the entire market demand (winner takes all / winner takes most). This form of demand-side induced competition for the dominant market position is particularly evident on markets for virtual network goods, as there are no supply-side restrictions here. A supplier of software, for example, can adapt his supply to changes in demand at almost any speed (instant scalability).

²⁸ There is moral hazard when one market side has the possibility of changing key items that are relevant to the transaction secretly and at the expense of the other side (owing to the asymmetrical information) after the contract is signed (ex post).

²⁹ The classical example of negative selection caused by information asymmetries at the expense of the demand side is the market for used cars. Cf. Akerlof, G., The Market for 'Lemons': Quality Uncertainty and the Market Mechanism, Quarterly Journal of Economics 84, 1970, pp. 488-500.

and so set the price too high.³⁰ As a result raising capital is made more difficult for smaller and midsize companies than for larger firms, so that they can suffer considerable competitive disadvantages.

35. Public authorities often grant small and midsize companies loans at favourable conditions with the aim of compensating for these competitive disadvantages. As the award is selective these loans take on the character of state aid. Hence before state interventions, as by granting a soft loan, it should always be examined whether protective mechanisms are not forming on the market itself that could prevent market failure. Possible protective mechanisms are effective screening or signalling, which reduce the danger of moral hazard and adverse selection. An exact examination is also indicated in view of the fact that information asymmetries on capital markets do not necessarily lead to less lending, as inefficiently high lending can also be shown to be the result of underestimating risks. In this case state lending would lead to further loss of efficiency.

2.2.5 Shortcomings in Adjustment

36. Adjustment shortcomings are, firstly, a situation in which a market equilibrium does not exist, owing to unfavourable supply and demand constellations, or a new equilibrium does not evolve, or not at the desired speed, especially owing to lack of flexibility by market actors. One example of lack of flexibility is the ruinous competition that is caused by the “wrong” order in which suppliers leave a market (e.g. in inland waterways and agriculture).

37. State aid is often used as an instrument of sectoral structural policy in the EU and by member states. The aim here is to cushion the problems caused by structural change from the agricultural (primary) and manufacturing (secondary) sectors to the services sector (tertiary sector) and make them socially bearable. The need for a sectoral structural policy is seen in the lack of flexibility outlined above.

38. Economically, adjustment aids (or restructuring aids in EU law) can at most be justified as an economic policy instrument for sectoral structural policy under certain conditions. Adjustment aids are given to companies with the aim of simplifying the process of adjustment to the given economic conditions. After German reunification, for example, adjustment aids were given particularly to agricultural production cooperatives in the new Federal Länder. The grants, which were given e.g. for purchases of modern agricultural equipment, were to enable the farmers to move to market economy conditions more quickly.

39. On principle adjustment aid is intended to be help to self-help. It should only be paid until the necessary adjustment to changing structural conditions has been made. However, it has frequently been evident in the past that under political pressure a grant that was originally intended to be a short-term measure became a permanent subsidy to a particular sector or certain enterprises. This maintained the old structures and counteracted the original intention to accelerate the adjustment process. Permanent subsidisation is not an appropriate way to remove market failure caused by shortcomings in adjustment. On the contrary, permanent aid that assumes the character of maintenance grants serves other economic policy aims.

³⁰ One reason for this is that potential investors are faced with relatively greater problems in obtaining reliable information on the business prospects for small and midsize companies than for large firms. Cf. European Commission, Community Guidelines on state aid to promote capital investments in small and medium-sized enterprises, OJ EU C 194 of 18 August 2006, p. 2.

2.3 The Non-Economic Aims of State Aid

2.3.1 Regional, Distributional, Employment and Industrial Policy Aims

40. Maintenance subsidies, also called rescue aid in European law, are used as a structural policy instrument to maintain economic, cultural and regional cultural structures. They are given in the form of a compensation grant, for example, in agriculture and mining. Maintenance aids are intended to keep the incomes of those employed in the sector affected by structural change (e.g. hard coal mining) on a certain, socially desirable level (distribution policy aim), and avoid excessive unemployment in the regions concerned (employment policy aim).³¹ Purchases to support prices have also been a well known form of maintenance subsidy in the EU.³²

41. In general a critical attitude should be taken to the use of state aid as a structural policy instrument, in the form of both an adjustment aid and as a maintenance aid, because it is not precise enough and can have negative side effects. Maintenance aids in particular set the wrong price signals on product markets, and so cause considerable distortion to competition to the benefit of the subsidised industry. Moreover, the resulting wrong income signals cause workers to remain in jobs that have no future prospects. This hinders the necessary structural adjustment process, which causes more loss of economic efficiency. Other instruments, like individual financial support for the workers, are better suited to achieve employment and distribution policy aims. Targeted promotion of the workers in old industries, e.g. in the form of further training and retraining courses, will achieve these aims more efficiently and more permanently without the negative side effects.

42. The focus of regional policy is on the distribution of the production potential and the development of the infrastructure in areas within an economy. The aim of regional policy measures is to create equal living standards in a region. Against this background, i.a. financial incentives are offered to companies in branches with good future prospects to induce them to move into structurally weak areas that have high unemployment, and so increase the demand for labour. The political decision-makers also hope that the arrival of these companies will have other positive effects as well, like agglomeration advantages.³³ But state aid motivated by regional policy bears a considerable prognosis risk and so can fail to have the intended effect.

43. On national level targeted promotion of large companies, i.a. through selective tax concessions, has been evident in recent years. The intention of the state decision-makers was partly to strengthen their international competitiveness by promoting these national champions. Ac-

31 Besides employment policy and distribution policy aims, the argument put forward for subsidies in hard coal mining and agriculture, which have assumed outstanding importance in Germany in the past, was particularly the need to secure supplies nationally. This national argument loses significance in the European context.

32 This practice has been particularly frequent on the agricultural market, where a minimum price was set to guarantee a specific income level in the sector. The minimum price was set above the market equilibrium price, and the surplus production that resulted, and which the farmers could not sell on the market at the fixed minimum price, was bought up by the state decision-makers at the previously fixed intervention price and – as far as possible – stored. This led to the well know butter and meat mountains. Alternatively, price support can also be achieved by paying a grant tied to capacity limitation (e.g. closure premiums).

33 State aid given as part of regional policy can lead to competition between different jurisdictions “to attract private investment”, which in regard to dynamic can lead to gains in efficiency. It is conceivable that of several incentive packages on offer the most efficient will become established – and with it the region that attaches the greatest value to attracting companies. This is discussed separately in Section 3.

According to the theory of strategic foreign trade policy, if considerable advantages of scale and scope exist, an active industrial policy can result in the domestic company achieving gains abroad in the medium to long term, which then benefit the domestic economy.³⁴

44. The Monopolkommission has explained in the past that for several reasons it takes a very critical view of the promotion of national champions, as is currently being practised in Germany in the railway and postal services sectors, for example.³⁵ It doubts that subsidising domestic industry benefits the state that is giving the aid; it also doubts that the benefit from the gains that may (possibly) be achieved abroad through the promotion exceed the costs of disabling the markets at home.³⁶ Even those who support the theory of strategic foreign trade policy assume that in constellations where all the states are granting aid they will all in the final result be worse off (the prisoners' dilemma),³⁷ and an inefficient aid race (a rat race) will ensue.³⁸

2.3.2 Merit Goods and Basic Security

45. In many cases aid is also granted to ensure the provision of a socially desirable quantity of goods. For goods that on principle are provided through the market mechanism, but are not regarded as provided in sufficient quantity, the term “merit goods” has been coined in the literature on fiscal policy.³⁹ Those who advocate this concept see the reason for the inadequate provision of merit goods as errors in estimating the benefit to themselves of these goods by private users, which in turn were caused by distorted preferences, lack of information or false information, and irrational decisions by members of the general public. This causes inadequate willingness to pay and consequently insufficient demand for merit goods. To avoid the economic inefficiencies that this undesirable development involves the political decision-makers must promote the provision of merit goods, e.g. with state grants (aid), to such an extent that the price people have to pay for the socially desirable quantity of consumption corresponds to their “inadequate willingness to pay”. The advocates of this theory name education, culture, health care and provision for old age as typical merit goods.

46. As an economic concept the principle of merit goods plays hardly any role in economic theory today, as it is problematic even in its basic approach. Firstly, there is the problem of which good should be classified as deserving promotion (identification problem). This generally results in state intervention in individual people's preferences, when state decision-makers also have to fix the degree of intervention (the quantity to be consumed) as a norm. This contains considerable potential for error and conflict, as the decision by a collective – or the decision-makers authorised by a collective – is set above that of the individual.⁴⁰ Moreover the state elite do not have sufficient knowledge of how demand will react to a change in price.

34 Cf. Brander, J., Spencer, B., Export Subsidies and International Market Share Rivalry, *Journal of International Economics* 18, 1985, pp. 83-100.

35 Cf. Monopolkommission, Wettbewerbspolitik im Schatten “Nationaler Champions”, Hauptgutachten 2002/2003, Baden-Baden 2005, Items 1ss.

36 Loc. cit., Item 16.

37 The prisoners' dilemma is a situation where individually rational behaviour by single members of the group leads to a bad result for the group as a whole.

38 Rat races are competition processes where growing expenditure is not matched by expectation of higher earnings overall; consequently a rat race is a waste of resources.

39 Cf. Musgrave, R.A., A Multiple Theory of Budget Determination, *Finanzarchiv N.F.* 17, 1956/1957, pp. 333-343.

40 The argument is only uncontested in a few exceptional cases, where the decision-making competence of an individual cannot be regarded as given (e.g. children up to a certain age).

It is also unclear where the state decision-makers are to obtain information on the optimal quantity of a merit good, if the people themselves do not know their preferences. Where this greater insight is to come from remains in the dark. So the politically desirable quantity of the merit good can only be achieved, even in the best case, through an elaborate process of trial and error. In view of this it seems more than questionable to justify huge areas of state policy, like health care and pension provision, with the merit argument. Ultimately, this is always a value judgement, which is unavoidable in weighing between individual preferences and preferences set collectively.

47. In some cases alternative reasons could be found for state aid given on the questionable grounds of merit. Assuming that the modern social state will support an individual even when he is in a desperate situation he has caused himself, certain insurance obligations can also be seen as means of preventing free riding.⁴¹ Workers might make no provision for their old age if they could assume that after leaving working life they will receive state transfer payments. In this case the possible free riding could be prevented by making provision for old age obligatory. Similar arguments can be put forward for health and care insurance. Some state funding of culture and education can also be justified on the grounds of positive external effects.

48. The concept of services of general interest that is used in administrative law (*Daseinsvorsorge*) is also used to justify state aid in connection with some goods that are provided or subsidised by the state (like local transport, health care and broadcasting).⁴² Under the term “services of general interest” are subsumed all state measures intended to secure the 'essential supply' (“Grundversorgung”) of the population. Unlike merit goods, such supply is not justified with the argument that owing to erroneous estimates of individual needs the provision of these goods has become insufficient : it is rather argued that the market does not provide such services of general interest to the politically desired extent. The politically desired extent need not be the same as the economically efficient quantity. The loss of economic efficiency which this entails is generally accepted for the sake of other political aims. The Monopolkommission regards the pursuit of these other aims as an entirely legitimate procedure in a democracy. However, in providing the politically desired amount of funding to cover people’s basic needs care should be taken to ensure that this is done at the least possible economic cost, to avoid unnecessary distortion to competition and the resultant inefficiencies.

49. An efficient provision of goods to cover people’s basic needs can be achieved through competitive tender procedures. The tenders must be held so that the company that can provide the good in the desired quality and quantity at the lowest cost is awarded the contract. The part of the costs that is not covered by the market process can be compensated by state grants. As outlined above in regard to the private provision of public goods these grants do not qualify as state aid in EU law in the meaning of Art. 87, Para. 1 EC Treaty, if they are given as part of a proper temporary tender procedure. The provision of the politically desired quantity of services of general interest in conformity with competition can thus actually help to increase the public and political acceptance of reforms to the general order.

41 There will be free riding if persons in need are not to be excluded from the state transfer system. This would be tantamount to a negative external effect.

42 On existential support see 5.3.4 below as well.

2.3.3 Politico-Economic Grounds

50. The above remarks make it clear that state aid is intervention in the market mechanism, and so can result in considerable distortions to competition. In this context state aid can cause considerable economic costs. As it is paid out of tax revenue, it first constitutes diminution of income, which is then disbursed in selective form to privileged branches of industry or enterprises. Granting state aid also involves bureaucracy costs and transaction costs for the enterprises (e.g. for consultancy on the aid, to make the application and for the obligatory reporting). Particularly protecting a stagnating branch with maintenance aid withdraws further funds from an economy. In addition, state aid has undesirable side effects, e.g. in the form of price distortions, which can result in further state maintenance payments.

51. Despite these well known disadvantages of state aid, it is evident in political practice that the aids are given even when other instruments would be better suited to achieve certain competitive or non-competitive purposes. One-off direct subject-related transfer payments (e.g. single payments to persons employed in mining), for example, have a better economic cost-benefit ratio. Inefficient granting of state aid is also due to the fact that it is given as part of the political process, and those responsible for political decisions are also pursuing their own interests. The danger of self-centred behaviour by political decision-makers, who are concerned with their own re-election chances, or those of their party, is particularly high. Short-term populist measures can give the (wrong) impression that the state aid will permanently secure jobs or create jobs in a region. State aid given in large and very noticeable amounts to a small group (like one company) has a very marked effect. The big group of taxpayers are financing it, on the other hand, with relatively small amounts that are individually hardly noticeable. While the fact that the taxpayers hardly notice the amount means that they do not take any action, the entrepreneurs and workers affected generally act in a way that the general public does notice, and so their response can help to secure an election victory for a politician or a party.

3. Possible Alternative Concepts to European Control of State Aid

3.1 Full Harmonisation of the Economic Policy Conditions?

52. Distortion to competition within the Community can be caused not only by state aid with selective effect but also by general economic policy measures by member states. There are proposals to remove these distortions to competition within the EU through full harmonisation of the economic policy rules, namely the national regulations (in labour market policy, environmental and product standards, company law), company taxation and public expenditure.⁴³ Banning state aid on European level is not enough, the need is to go further and aim for a level playing field throughout the EU. This can help to remove artificial distortions to competition caused by national states, enable companies to make the best use of the cost advantages of production and maximise welfare on the European internal market.

53. Harmonisation of legal requirements can be a meaningful instrument in some areas, for instance if it considerably reduces the transaction costs where cross-frontier movements are involved. But full harmonisation throughout the EU is not to be recommended, in the view of the Monopolkommission, as it would exclude all systems competition between member states

⁴³ For more detail see Ehlermann, C.-D., *Ökonomische Aspekte des Subsidiaritätsprinzips: Harmonisierung vs. Wettbewerb der Systeme*, Integration 19, 1995, pp. 11-21.

and regions in the EU. Moreover, it would ignore the fact that member states have different customs and preferences in regard to their economic policy conditions.⁴⁴ In systems competition institutions are competing for efficient and mobile factors that will be strong in value creation, like companies, financial capital and mobile workers.⁴⁵ The economic policy parameters that are available to states and regions to attract mobile factors or prevent their departure consist on the one side of public assets like infrastructure, the wages level, the level of training and technology and product regulation, and the taxes and charges raised to finance these on the other. Systems competition can help to reveal the true preferences of potential users, that is, the decision-makers on mobile factors, in regard to the state offer of taxation and performance.

54. In addition, systems competition – independently of the mobility of the factors – also opens up the possibility of trying out and comparing various concepts to solve socio-political problems through a competition for ideas. The political actors in systems competition have the incentive to develop attractive institutional regulations, and reduce superfluous regulations and bureaucratic obstacles, leading to a discovery procedure. In view of this the Monopolkommission speaks out against full harmonisation of the economic policy framework conditions within the EU. It would eliminate systems competition.

3.2 Location Competition by Granting (Relocation) State Aid?

55. In view of the positive effects of systems competition some writers argue that the supervision of state aid assigned to the European Commission should be abolished – at least for businesses relocating to an area – while member states and regions within the EU should be allowed to use (relocation) state aid as a competition parameter.⁴⁶ An appropriate offer of state aid can help to ensure that companies or investors make efficient location decisions, they say. In politico-economic regard it can be assumed that political decision-makers are extremely keen to attract companies into their area of jurisdiction, to create jobs and increase their tax basis. On the other side mobile companies want the best possible conditions in a location to allow them to produce and meet demand at the lowest possible cost. State aid can be an effective instrument to incorporate and internalise the positive effects that attracting companies into a particular region will have, especially in the form of agglomeration advantages to the authority granting the aid. As the positive effect could vary in intensity, depending on the characteristics of the company willing to relocate and of the region, it is efficient for sovereign authorities to create price differentiation with state aid in the form of discounts on tax payments. In location competition that region will win through that offers the greatest advantages to companies willing to locate there.

56. It is also argued that many companies would necessarily have to make long-term investment specific to that location if they settled there. That would be the case for suppliers of infrastructure facilities like energy, transport or telecommunications. In these cases there is a

⁴⁴ Systems competition, which is also referred to as institutional, inter-jurisdictional or location competition, means that not only companies but economic systems or locations as well are competing with each other.

⁴⁵ Cf. Monopolkommission, Systemwettbewerb, Sondergutachten 27, Baden-Baden 1998, Item 9.

⁴⁶ For more detail see Gröteke, F., Europäische Beihilfenkontrolle und Standortwettbewerb – eine ökonomische Analyse, Stuttgart 2007, pp. 182ss. Opponents of this extreme approach to systems competition, by contrast, see granting state aid as a potential cause of inefficient allocation of enterprises between the various locations; they regard European supervision of state aid as a necessary institutional framework condition. For example cf. Koenig, C., Kühling, J., Reform des EG Beihilfenrechts aus der Perspektive des mitgliedstaatlichen Systemwettbewerbs – Zeit für eine Neuausrichtung?, Europäische Zeitschrift für Wirtschaftsrecht 10, 1999, pp. 517-523.

risk that the sovereign authority could subsequently change the framework conditions to the company's disadvantage, for instance through subsequent tax increases or other regulations.⁴⁷ Location aid can be a means to secure specific investment against later deterioration and exploitation by the authority (the hold-up problem). Moreover, granting state aid in location competition between authorities is one possible competition parameter among many. So the question arises why specifically that parameter must be regulated. EU supervision of state aid merely shifts location competition on to other parameters, like improving the physical infrastructure, free or subsidised training for workers, building regulations, etc.

57. In the view of the Monopolkommission the proposal to abolish supervision of state aid for newly locating companies to encourage competition between locations is an interesting concept in theory. However, this extreme form of systems competition, in which (location) aid would be a permissible competition parameter for local authorities and not subject to prior control would in practice only be fully functional if the principle of fiscal equivalence were realised.⁴⁸ Fiscal equivalence means that the aid would be financed entirely by the region granting it and be subject to strict budget restrictions, so that a region in financial difficulties could not expect assistance from another sovereign authority. Otherwise there would be a risk that the costs involved in a corporate location would be shifted to other authorities. This externalisation of costs could mean that a region would offer excessively high aid and consequently inefficient location decisions would be made. However, the principle of fiscal equivalence can scarcely be realised. Indeed, it is unclear on which level it should be realised – in the individual municipality, in parts of a Federal Land, throughout one Federal Land, in several Länder (e.g. North Germany) or throughout Germany. The problem would not be solved if one Federal Land were the reference unit. That would imply that cross-subsidisation was accepted within one Federal Land while subsidisation across the borders between the Länder had to be stopped. Each Federal Land would then have to fix its tax rates and decide on grants to investors in location competition. This premise of free competition in aid between the Länder would be clearly contrary to the fiscal constitution in the Basic Law. In so far as tax revenue is joint revenue and also accrues to the Länder under Art. 106 of the Basic Law – and this applies to the greater part of the revenue from income, corporation and turnover tax – the Federal Government still has (competing) legislative powers, and the consequence is uniform taxation that does not depend on the domicile of the taxpayer. The obligatory financial equalization for the Länder under Art. 107, Para. 2 Basic Law also prevents the realisation of fiscal equivalence. Furthermore, there is a political obligation to redistribution between regions within the EU as well. Under Arts. 158ss. of the EC Treaty the most disadvantaged regions are to be promoted in the interests of economic and social cohesion within the Union. This results in payment flows of considerable size, motivated by distribution policy (and frequently in the form of EU subsidies).

58. There is also the risk that a state granting aid may err in its estimates, with the result that the hoped-for positive effects for the region concerned do not materialise in the long term. This prognosis risk can theoretically be reduced if the aid is repaid if the expected positive effects for the region do not materialise. However, it is only possible to concretise and implement a repayment obligation of this nature if it has involved guarantees for which the recipient of the aid is responsible, like the commitment to create a certain number of jobs. It cannot

47 Cf. Haucap, J., Hartwich, T., *Fördert oder behindert die Beihilfenkontrolle der Europäischen Union den (System-)Wettbewerb*, in: Schäfer, W. (ed.), *Wirtschaftspolitik im Systemwettbewerb*, Schriften des Vereins für Sozialpolitik, N.F., Vol. 309, Berlin 2006, pp. 93ss.

48 This view is shared by those who support this approach. For more detail see Gröteke, F., loc. cit., pp. 206ss.

include the actual external effects which the new location could create in the region as a whole, as these are difficult to measure and cannot be exactly forecast. Moreover, the aid can prove to be inefficient if the political decision-makers are acting in self-interest in granting it (mindful of a coming election) and thus take short-term popular measures or are promoting particular interests. The danger of a hold-up described in Item 941 can also occur for the converse reasons. Conceivably, a company that has received aid could build up a potential to exert pressure that will grow with the increasing size of the company, and threaten to move elsewhere, with the loss of jobs for the region this would entail. However, to what extent companies or authorities have such potential power does depend on the specific nature of the investment made and in how far it is reversible. A company that has invested considerable amounts in facilities specific to a location (e.g. in the infrastructure) cannot issue very credible threats to leave.

59. A further consideration to support supranational aid control is that aid granted by one member state can cause negative effects in another member state in the form of distortion to competition on product and services markets. That applies particularly in cases where large companies domiciled in that member state, or the companies in a specific branch, are built up and promoted to strengthen their international competitiveness. European supervision of state aid can help to reduce cross-frontier distortion to competition on the EU single market.

60. The Monopolkommission is not in favour of abolishing European control of state aid. This is because the principle of fiscal equivalence cannot be sufficiently realised, moreover granting state aid involves prognosis problems and can cause cross-frontier distortion of competition on product and services markets. It must also be borne in mind that the ban on state aid in Art. 87, Para. 1 EC Treaty is normed and does not apply absolutely, indeed numerous exceptions are envisaged. Member states are not prevented right from the start from granting location aid under the present system, but the European Commission should take greater account than hitherto of the positive effects that competition between locations to attract companies can have.

4. The Tasks for the European Commission in State Aid Supervision under Arts. 87ss. EC Treaty

4.1 Possible Economic Grounds for Shifting State Aid Control to a Supranational Body

61. In the economic view there are two possible reasons for transferring supervision of the award of state aid to a supranational body like the EU. Such powers can be created with the aim of avoiding the negative effects which state aid can cause in other states through distortion of competition. Another possible reason may be to have the efficient use of public resources appraised externally and avoid commitment problem with this form of budget control.⁴⁹ Owing to political pressure sovereign powers sometimes find it difficult to refuse to give aid. They are not willing to tie themselves in advance to a long-term ban on aid and a fixed budget. If giving state aid is likely to increase support in the short term, and win more votes in a coming election, politicians may be inclined to grant it even if the aid is not economically efficient and ultimately constitutes a waste of public resources. Delegating control of state aid to a higher authority that is politically independent can help to avoid such commitment problems.

⁴⁹ Cf. Friederiszick, H.W., Röller, L.-H., Verouden, V., *European State Aid Control: an Economic Framework*, in Buccirosi, P. (ed.), *Handbook of Antitrust Economics*, Cambridge, Mass. 2008, pp. 625-669.

4.2 Protection of Competition in the EU Internal Market as Sole Objective – No Budget Policy Powers

62. Both the systematic position of Arts. 87ss. EC Treaty in the legislation and the wording of Art. 87, Para.1 EC Treaty suggest that aid control is exclusively intended to protect competition on the internal market. The regulations on state aid (Arts. 87ss. EC Treaty) are contained in Chapter 1 of Title VI to the EC Treaty, that is headed “Rules on Competition”. So just like the antitrust regulations in Arts. 81, 82 EC Treaty, which are in the same chapter, they relate to the aim named in Art. 3, Para. 1 g) EC Treaty, namely to set up a system that will protect competition within the internal market from distortion. Art. 87, Para. 1 EC Treaty expressly names distortion of competition and restriction of trade between states as the main criteria. Preventing negative spill-over effects in the form of distortion to competition in the EU internal market is consequently the protective purpose of European state aid control. It was introduced with the aim of promoting the establishment of a single internal market and preventing member states from using state aid to counteract the lowering of trade barriers and the realisation of the basic freedoms named in the EC Treaty. State aid to national companies can have an effect similar to protective customs barriers in sealing off a market.⁵⁰ In recent years attempts by member states have been evident to compensate for the loss of state control through the former state monopolies or network industries by making greater use of state aid and by permitting major national mergers, and to this extent to hamper the EU internal market. The Monopolkommission rejects this protectionist industry policy, which is directed to promoting domestic industries and sealing off national markets.

63. However, the Community has no powers to control member states’ budgets. The EU has so far only been granted power of budget control to supervise adherence to the Maastricht criteria (Art. 121 EC Treaty). It is not one of the European Commission’s tasks in state aid control under Arts. 87ss. EC Treaty to supervise the right use of member states’ resources as such.⁵¹ As long as there are no such powers the member states are responsible for setting up effective control mechanisms and a stringent system within their borders to prevent an economically harmful waste of state funds through the inefficient award of state aid. In accordance with the aim formulated in Art. 3, Para. 1 g) EC Treaty the sole protective purpose of the European regulations on state aid is to avoid distortion to competition on the product and services markets on the European internal market.

64. This aim has been taken out of the final version of the Lisbon Treaty, the future EU reform treaty.⁵² Owing to the negative signal effects it will have for European competition policy the Monopolkommission regards this with concern. In legal terms, however, no direct changes will result for the implementation of the competition regulations in EU antitrust law and state aid law.⁵³ Under Art. 3, Para. 3 of the Lisbon Treaty the realisation of the internal market is one of the primary aims of the Community, and a protocol annexed to it states that the internal market also includes a system that will protect competition from distortion.⁵⁴ Pro-

50 Cf. Mestmäcker, E.-H., Schweitzer, H., *Europäisches Wettbewerbsrecht*, 2nd edition, Munich 2004, § 42, No. 20.

51 Cf. Bartosch, A., *Der More Economic Approach in Beihilfesachen*, *Recht der Internationalen Wirtschaft* 53, 2007, pp. 681-690.

52 Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community, signed at Lisbon, 13 December 2007, OJ EU C 306, 17 December 2007, p. 1.

53 Arts. 81, 82 and 87ss. of the EC Treaty were retained with only a few modifications, cf. Art. 2, Fig. 75ss. of the Lisbon Treaty.

54 Protocol on the internal market and competition, OJ EU C 306, 17 December 2007, p. 156.

tools that are added to the primary law Community treaties have binding legal force and the same primary law ranking.

4.3 Improving the National Means of Control

65. It is essential for the public authority granting state aid to know the foreseeable effects of this on the general welfare (macro welfare oriented cost-benefit comparison). However, as explained above, in its control of state aid the European Commission is only obliged to assess those costs that can be incurred through state aid in the form of restraints of competition in the internal market, and weigh them against the desired benefit.

66. On national level, on the other hand, the other economic costs induced by granting state aid must be taken into account beside the expected distortion to competition. Member states must calculate the cost of financing the state aid, and the opportunity costs and loss of net welfare (the shadow costs of taxation), and ensure that the aid is given efficiently, avoiding any waste of public funds.

67. Germany has a large number of promotional programmes with some overlapping objectives, initiated by various public authorities and sovereign bodies (the EU, the Federal Government, the Länder and the municipalities). Owing to the resultant intransparency it is difficult for companies (especially small and midsize companies) to gain an overview of whether and to what level they could obtain promotional funds. In some cases they have to spend considerable resources on clarifying the question. Owing to the lack of coordination there is also a risk that aid in pursuit of specific objectives will be given in inefficiently high amounts or that contrary aims will be pursued. The coordination could be improved if state aid and state aid programmes had to be published by all the donors in advance on a central website on the Internet, with a description of their objective, their volume and the qualities expected of their actual or potential recipients. For practical reasons this obligation should only apply to state aid that exceeds a certain volume still to be determined. A central website of this nature could help to lower the transaction costs for the acquisition of information by potential applicants for state aid. Another possible way of lowering transaction costs – especially for smaller and midsize companies – could be to allow companies to apply for state aid on their tax declaration forms, with the factors that qualify them for the aid clearly formulated. The aid should then be given in the form of tax reductions.

68. The Monopolkommission recommends subjecting the national state aid programmes to regular success control, in which an independent body would examine whether the objectives, that should be clearly formulated in advance, had been achieved, and which disadvantageous effects had occurred as a result of the state aid. To avoid the creation of a subsidisation mentality and ensure efficient appraisal a time limit should be set for state aid right from the start (sunset regulation). Degressive state aid for longer term promotion is also to be recommended.

69. Beside ex post success control there is also the possibility of prescribing ex ante control for particularly serious cases, where the aid programme, or the intended individual grant, is for a volume still to be determined. In the ex ante control the entire economic effects of an aid, including the consequences for competition, should be forecast. The examining body would not be empowered to make a political decision instead of the public authority granting the aid, but it should check whether the donor has taken all the foreseeable economic costs into account in its decision. It should also consider whether the aid is on principle a suitable

and necessary means of achieving the desired effect, and whether the expected costs are not out of proportion to the expected benefit. The powers to undertake this form of macro national aid control and assessment could be given to the national audit courts, for example, as they already have the task of checking the budgets and economic management of the public administration. Alternatively, an independent national body of experts (a subsidisation control council) could be considered.⁵⁵ The competent body could be given powers to hold hearings, make statements and report as part of its ex ante control, and it could make recommendations. But it could also be given right of objection, similar to the powers the European Commission has in European state aid control.

70. In addition, state aid should on principle be given in an open and transparent procedure, as is prescribed for the award of public contracts (§ § 97ss. Act Against Restraints of Competition – GWB). For a general, abstract aid programme the funds should be available to all companies that meet certain criteria. In the case of individual aids there should be competition in a transparent tender. This would avoid inefficiently high and discriminatory aid and unnecessary additional distortion to competition.

71. Finally, subjective rights and an efficient system of legal protection should be created for potential recipients of the aid, competitors affected and their associations. Permitting private lawsuits would, in the view of the Monopolkommission, increase the efficiency of macroeconomic national state aid control. The regulations on checking the award of public contracts (§ § 104ss. GWB) could serve as a model. Under these regulations companies that have failed to obtain a public contract can obtain legal protection under §§ 107ss. GWB before independent awarding chambers in a formal ex post appraisal procedure, if certain thresholds have been reached or exceeded. Immediate objection to the decision by the awarding chamber is permitted. An award senate of the Intermediate Court of Appeal in whose jurisdiction the awarding chamber is located (§ 116 GWB) decides on the appeal. This procedure also raises the question of the protection of confidential business data. To prevent the beneficiary's operating and business secrets having to be revealed to the competitor who has brought the case the awarding chambers and senates are to be allowed to refuse the right to access files containing the relevant data.⁵⁶ In addition, regulations could be introduced to accelerate the procedure, analogous to the legislation on the award of contracts, to avoid delays and legal uncertainties.⁵⁷

72. State aid that is designed right from the start for individual companies and so for which no tender is held, and state aid for the benefit of specific, already established branches, should on principle be forbidden on national level and at most permitted in exceptional cases. Aid of this kind regularly proves particularly problematic in the macroeconomic regard. This applies, for instance, to rescue aid designed to maintain a specific company. As well as the risk that the aid will fail to have the desired effect (securing jobs), may be given to an excessive level or be the result of self-interest on the part of politicians, this kind of state aid can cause considerable distortion of competition because inefficient companies are promoted, and access to the market is made more difficult for efficient newcomers.

55 Cf. Monopolkommission, Wettbewerbspolitik in Zeiten des Umbruchs, Hauptgutachten 1994/1995, Baden-Baden 1996, Item 154.

56 Cf. § 111 GWB. § 120, Para. 2 GWB states that this is applicable to the immediate appeal to the awarding senates.

57 § 113 GWB provides for acceleration of the ex post appraisal procedure before the awarding chambers.

73. In regard to the politico-economic context explained in 2.2.3 above, the introduction of effective control of state aid on national level is not very likely. The political interest in maintaining the financial scope to serve the politicians' own clientele is too strong, and it is presumably for these reasons that the European authorities have extended their area of application of state aid control fairly widely, with a broad interpretation of Art. 87, Para. 1 EC Treaty.⁵⁸ This fills a gap, so to speak, in the institutional structure of member states. Because they do not effectively control their own subsidisation practice, but on the other hand acknowledge the budget policy need to limit this, member states generally do not protest much if the European Commission also examines the award of state aid where noticeable restraint of competition and restriction of trade between states is not seriously evident, so ultimately where the issue is budget policy discipline. The Monopolkommission sees its proposals to reduce European state aid control onto aid relevant to competition, and to create a national aid control system, as a package of complementary measures that can only be realised as a whole.⁵⁹

5. The Legal Framework Conditions and their Traditional Interpretation by the European Institutions

5.1 Subsidies given by the EU and Third Countries: Art. 87 EC Treaty does not apply

74. The EU itself grants subsidies to a considerable extent. The figure given in the 2007 budget plan was EUR 126.5 billion.⁶⁰ The 25 EU member states, by contrast, gave state aid totalling "only" EUR 66.5 billion in 2006.⁶¹ EU distribution and agricultural policy measures have so far predominated. The regional structural measures that are intended to improve cohesion between the various regions and member states accounted for 35.9% of the EU budget in 2007. EUR 45.5 billion was earmarked for these in the budget plan, with EUR 35.3 billion intended for the economically weakest regions in the EU. The share of aid for agriculture and rural development in the EU budget was set at 44.4% (EUR 56.3 billion) in the same period.⁶²

75. Despite its importance aid from the EU does not come under the ban in Art. 87, Para. 1 EC Treaty. The definition "aid granted by a Member State or through State resources" only covers measures by member states and aid given by them. Aid given by the Community, a considerable share of which is not in pursuit of horizontal aims but flows to specific sectors (agriculture) and should be classified as particularly problematic in regard to competition policy, is therefore not subject to the strict control of state aid by the EU under Arts. 87ss. EC Treaty. EU aid is only subject to the regulations in WTO legislation. These are in both the General Agreement on Tariffs and Trade of 1994 (GATT 1994) and the Agreement on Subsidies and Countervailing Measures (SCM Agreement).⁶³ As well as the member states the EC itself is party to these international agreements under Art. 133 EC Treaty, making them binding for the institutions of the Community as well as for its member states (Art. 300, Para. 7 EC Treaty). The European legislation on state aid is a much more differentiated set of regula-

⁵⁸ For more detail see 5.2.4 and 5.3.5 below.

⁵⁹ See 5.2 and 7.1 below.

⁶⁰ European Commission: Survey of the 2007 EU Budget, http://ec.europa.eu/budget/publications/budget_in_fig_de.htm.

⁶¹ Cf. Commission Report, State Aid Scoreboard, Autumn 2007, loc. cit., p. 10.

⁶² The direct payments to farmers and measures to sustain an orderly market account for EUR 45.8 billion of this.

⁶³ Cf. OJ EU L 336 of 23 December 1994, p. 3, here pp. 156-183 (Annex 1A, Agreements and Countervailing Measures).

tions than the WTO legislation, and its application is comprehensively designed to realise the Common Market and remove distortion to competition.⁶⁴

76. The present system of EU aid is characterised by the coexistence of a number of funds, whose tasks are not always clearly delimited. Institutionally, Community aid is given by the European Guidance and Guarantee Fund for Agriculture (Art. 34, Para. 3 EC Treaty), the European Social Fund (Art. 146 EC Treaty), the Structural Fund to Achieve Cohesion and Convergence (Arts. 158ss. EC Treaty), the European Investment Bank (Arts. 266f. EC Treaty), as well as in research and development (Arts. 163ss. EC Treaty).⁶⁵ In many cases the level of financing for the individual funds provided by member states is the result of political compromise.

77. As potential beneficiaries find the criteria for EU aid complex and difficult to understand current EU promotion runs the risk of excessive bureaucracy costs and lack of efficiency. The supervision of EU aid also has shortcomings, entailing the risk of free riding and fraud.⁶⁶ Due to the lack of transparency in the system and the amount of funds being awarded EU aid can, in the view of the Monopolkommission, give rise to considerable distortion of competition in the European internal market. The present WTO regulations, which are not very differentiated and mainly of significance in relations with third countries outside the EU, offer only rudimentary protection.

78. There are proposals to extend the control regime laid down in Arts. 87ss. EC Treaty to EU aid.⁶⁷ In the view of the Monopolkommission this would involve difficulties, not least because

64 The SCM Agreement distinguishes between three categories of state aid (traffic lights approach):
 RED: banned aid (Part II SCM Agreement). This is aid tied to the export of goods or the use of domestic goods, which is banned per se. If the “special group” of the Dispute Settlement Body (DSB, a WTO organ) is involved and concludes that the measure is a banned form of aid it will “recommend” the state concerned to withdraw the aid without delay; if that is not done the state is restricted and may not take any countervailing measures.

YELLOW (disputable) aid (Part III SCM Agreement): Aid can be disputed if it will have disadvantageous effects on the interests of other members (Art. 5, SCM Agreement). In this case the WTO member granting the aid can withdraw it or remove the disadvantageous effects; if it does not do so countermeasures (countervailing duties) may be imposed as protection against subsidised imports (Arts. 10ss. SCM Agreement).

GREEN (non-disputable) aid (Part IV SCM Agreement). Certain research grants, aid for disadvantaged regions and environmental aid come into this category.

65 The European Commission is also aiming to reform EU aid. For 2008, for example, a debate is planned on the principles of reorienting the EU Common Agricultural Policy, which will be implemented in 2013 at the earliest. In 1992 the EU began on the first of now three reforms to withdraw gradually from market and price support. In the last agricultural reform, in 2003, the member states decided to uncouple aid from production and replace it with a system of direct income support. The level of the lump sum payments, which farmers are now receiving, is oriented to the level of the operational aids granted in former years. The European Commission suggests limiting the aid to large agricultural enterprises and cutting back the direct EU payments to farmers in favour of a policy to promote rural regions. For more detail see Maas, S., Schmidt, P., *Gemeinsame Agrarpolitik der EU*, Wirtschaftsdienst 87, 2007, pp. 94-100 and Anon, *EU-Kommission stellt Basis für Agrarhilfen in Frage*, Frankfurter Allgemeine Zeitung, 31 October 2007, p. 15.

66 In its annual report on the implementation of the budget plan for the financial year 2006 (OJ C 273 of 15 November 2007, pp. 1, 132, Col. 1, Item 6.39) the European Community Audit Court reaches the conclusion that in 2006, in structural policy for instance, at least 12% of the promotional funds should never have been granted. The reasons for the high error ratio are firstly carelessness and insufficient knowledge on the part of the offices disbursing the funds, and secondly specific attempts at fraud, facilitated by the lack of quality and the number of controls. In Germany fraud with promotional funds can be prosecuted under § 264 of the Criminal Code.

67 For example Schwintowski, H.-P., *Staatlich veranlasste Wettbewerbsbeschränkungen auf europäischen und internationalen Märkten*, *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 58, 1994, pp. 232-291, 245.

the EU would be controlling itself, through the same institution. For the European Commission has not only been entrusted with carrying out aid control, it is also responsible for the administration of European promotional finance and the European funds. A transfer of the control function to the European courts would be conceivable. However, traditionally they leave the European Commission wide scope for judgement in decisions of a political nature. So it appears questionable whether efficient control of EU aid could be achieved in this way. It would be preferable to transfer control to a new independent European supervisory authority, that could act free of political influence. Beside EU-related measures greater engagement on international level for the introduction of a better control regime within the WTO framework should also be considered.

79. European aid control fulfils an important and essential function in protecting cross-frontier competition on the EU internal market. Corresponding protective mechanisms are lacking in many states outside Europe, so that granting aid by the political decision-makers is not subject to strict control, as it is in the EU. Consequently, when there is international competition for major projects third countries may be able to hold out a prospect of higher grants (subsidies) to companies than EU member states can, as they are bound by Arts. 87ss. EC Treaty. In the view of the Monopolkommission the regulations on EU aid should not be reduced or relaxed even in such circumstances. The aim should rather be to establish better standards of protection on the international level and work for the introduction of more stringent rules on subsidisation (especially in the WTO), in relations with third countries as well.

5.2 The Factual Level (Art. 87, Para. 1 EC Treaty)

5.2.1 Granting Aid

80. Although Art. 87, Para. 1 EC Treaty contains a definition of aid, the criteria are given in indeterminate legal terms that are open to differing interpretations and need to be concretised. To make clear under which conditions a measure has so far been classified as aid and subject to European control the individual criteria named in Art. 87, Para. 1 EC Treaty and their traditional interpretation by the EU institutions will now be discussed.

81. A measure is only aid if it involves “favouring” in the meaning of Art. 87, Para. 1 EC Treaty. This can result from positive state payments. Hence a broad spectrum of forms of assistance are subsumed as aid. In contrast to the report on aid by the Federal Government, therefore, this also includes state guarantees. Measures are also classified as aid if they reduce the burden a company normally has to bear. Thus loans at preferential conditions and easier terms of payment for taxes and social insurance contributions also fall under European state aid control.

82. The ban on aid in Art. 87, Para. 1 EC Treaty covers not only one-way state measures, it also covers advantages which the state grants a company as part of an exchange. Member states can certainly take part in economic activity as investors aiming to make a profit (Art. 295 EC Treaty), but to prevent evasion of the regulations favourable treatment in the meaning of Art. 87, Para. 1 EC Treaty is assumed if the state payments are not matched by appropriate reciprocity (partial gratuitous transfer, e.g. the sale of land below market price). To what extent an injection of capital, compensation for loss or renunciation of profit constitutes aid or can be regarded as market behaviour is examined more closely by the European Commission

in individual cases. According to long-standing jurisprudence, the “private investor test” is to be used to distinguish between favourable treatment and market action by the state.⁶⁸

83. This is the only condition in Art. 87, Para. 1 EC Treaty that has been subject to extensive economic analysis over an extensive period. It is usual in practice for economic reports to be compiled and used in establishing whether there is favourable treatment, at least in difficult cases and especially as part of the private investor test. This contrasts with the approach to the other aid criteria.

5.2.2 Favouring “Certain Undertakings or the Production of Certain Goods”

5.2.2.1 Possible Beneficiaries

84. For a measure to constitute aid a company or branch of production must benefit from it. The concept of an “undertaking” in Art. 87, Para. 1 EC Treaty corresponds with that in the other EU competition rules. Just as in Art. 81, Para. 1 EC Treaty, for example, an undertaking is a unit that performs any economic activity independently of its legal form and the way it is financed (the function concept of an undertaking).⁶⁹ Grants that primarily benefit private households are not covered by the term. Under Arts. 87ss. EC Treaty aid supervision must cover not only aid to private enterprises but also aid to public enterprises (Art. 86, Para. 1 EC Treaty). Public enterprises are economically active units of any legal form, on whose business planning or activity public sovereign authorities can exercise a determinant influence, directly or indirectly (through ownership, shareholdings, voting rights or in any other way). Deutsche Bahn (the German Railway company) is one example.⁷⁰ If the beneficiary exclusively performs social tasks assigned to him by law, it is not an undertaking in the meaning of Art. 87, Para. 1 EC Treaty, according to jurisprudence by the European Court of Justice, as long as it performs its legal tasks independently of the level of contributions and entirely in accordance with the idea of solidarity (e.g. the statutory health insurance institutes).⁷¹ The ban on aid applies not only to financial benefits to companies, it also applies to whole branches of production. This concept is interpreted broadly, as meaning branch or sector, and it also covers the services sector.

5.2.2.2 Selective Advantage

85. The measure must benefit specific companies or specific branches of production. So only state measures of a selective nature constitute aid. The selectivity makes the difference between the competence of member states to regulate general economic policy measures and the competence of the Community to protect competition from individual acts of intervention. State payments that benefit all the companies in the member state, without distinction (e.g.

⁶⁸ In this context the European Court of Justice has stated that member states are interested less in short term than in longer term profitability for their investments. Their behaviour as public investors must therefore be compared with that of holding companies or groups of private companies, whose profitability thinking is more long term.

⁶⁹ ECJ, Judgement of 17 February 1993, Conn. Cases 159/91 and 160/91, Poucet/AGF and Camulrac and Pistre/Cancava, Rec. 1993, 1-637, No. 17.

⁷⁰ Cf. Art. 2 b) of 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 (the Transparency Directive), OJ EU L 318 of 17 November 2006, p. 17.

⁷¹ ECJ, Judgement of 16 March 2004, Conn. Cases C-264/01, C-354/01, C-355/01, AOK-Bundesverband et al., Rec. 2004, 1-2493, No. 48ss.

general labour market policy measures, general tax rules or infrastructure measures that will benefit all the corporate sector) are not aid in the meaning of Art. 87, Para. EC Treaty.

86. Differences in the initial conditions, and distortions to competition that result from member states making use of their powers to instigate appropriate general economic policy measures, can only be removed through legal harmonisation (Arts. 94ss. EC Treaty). If a measure introduces different treatment between companies, according to jurisprudence the decisive fact is whether this difference is due to the nature of the current system or its structure. If the difference is due to other than the objectives of the general system it is on principle assumed that the measure in question is to be classified as selective in the meaning of Art. 87, Para. 1 EC Treaty.

87. In general the fact of selectivity (“favouring certain undertakings or the production of certain goods”) is interpreted very widely by the EU organs.⁷² Accordingly, not only those advantages that a member state grants a certain company individually, or a certain branch, are subject to aid control. Rather, a measure is already regarded as selective if it covers

- only companies of a certain size, independent of their branch, e.g. only large firms or small and midsize firms
- only companies producing physical goods or
- only new companies making investment of a certain level and creating a certain number of jobs.

Measures to benefit companies of neighbouring branches are also included. Moreover, measures that will benefit all the companies and branches in a certain region are generally classified as selective.⁷³ So if, for example, a German Federal Land allowed all the companies that settled or were established in its territory a low rate of tax, this measure would be covered by the ban on aid, and it would be subject to control by the European Commission, even if the degree of selective effect were relatively slight.⁷⁴

72 Cf. ECJ, Judgement of 13 September 2006, Case T-210/02, British Aggregates Association/Commission, Rec. 2006, II-2789, Nos. 104ss.

73 In its Azores judgement of 6 September 2006, Case C-88/03, Portugal/Commission the ECJ considered the question of the range covered by the concept of regional selectivity in aid law in more depth. It drew a distinction between the following groups of cases:

Lack of devolution (that is, no transfer of sovereign powers to regional bodies): The central government sets a rate of tax for a certain region (to be paid by all the economically active) that is lower than the rate charged on national level. In the view of the Court such a measure is always selective, as it only applies to part of the geographical area for which the tax legislature is responsible.

Symmetrical devolution: The model of divided taxation powers, in which all the territorial authorities of a certain level are free, within the limits of the competences assigned to them, to choose the rate of tax for their area of responsibility. In the view of the Court the criterion of selectivity is not fulfilled in such a constellation. The determinant frame of reference is the unit that is regionally responsible, not the member state as a whole.

Asymmetrical devolution: In the exercise of its powers a regional or local body sets a rate of tax that is lower than the national rate and which applies only to the companies in its territory. In the view of the Court a tax measure in such a constellation is not selective in the meaning of Art. 87, Para. 1 EC Treaty only when the body is sufficiently autonomous in institutional, procedural and economic regard. Accordingly, the lower tax rate may not be cross-subsidised and the economic consequences of lowering this rate of tax must be borne by the region itself.

In detail on the judgement see Arhold, C., *Steuerhoheit auf regionaler oder lokaler Ebene und der europäische Beihilfenbegriff – wie weit reicht das Konzept von der regionalen Selektivität*, *Europäische Zeitschrift für Wirtschaftsrecht* 17, 2006, pp. 717-721.

74 Measures of this nature by the German Federal Länder would not be exempt from the ban on aid, according to the jurisprudence by the European Court of Justice on regional selectivity (the Azores judgement) outlined in the previous footnote, because the Länder are not sufficiently autonomous, especially as a result of

5.2.3 State Grants or Grants using State Funds

88. The ban in Art. 87, Para. 1 EC Treaty only covers “aid granted by a Member State or through State resources”. Aid is state aid if the donor is a sovereign authority. So the ban applies not only to the member states as such but also to all their sovereign authorities (the Länder, municipalities, other bodies and institutes incorporated under public law). According to jurisprudence by the European Court of Justice, only those advantages that involve a transfer of state funds, or are paid out of the state budget are covered by the ban (the *PreussenElektra* jurisprudence).⁷⁵ So the criterion is not met if the state action only achieves a desired beneficial effect, while the cost is borne entirely by the private sector. Consequently the promotion under the German Renewable Energies Law, which includes an obligation to pay non-competitive prices, does not come under the European aid regime.⁷⁶

89. In the economic view financial advantages to the private sector accruing from state regulation, the costs of which are to be borne by other members of the private sector, will have distorting effects on competition similar to the benefits that accrue directly or indirectly from state budgets. Consequently there is a risk that member states can evade the European regime on aid with skilful steering of the flows of funds. In the view of the Monopolkommission the concept should nevertheless not apply to all the measures that arrange for transfer payments between different market participants. Such an interpretation would mean that many regulations in member states’ legislation that cover the relation between different members of the private sector (e.g. obligatory liability or regulations in labour law) would be subject to European aid supervision. This would make all the legislation that places obligations on the private sector subject to aid supervision, which is unsuited for these purposes. In the view of the Monopolkommission, in cases where the legislature is obliged (under constitutional law) to ensure that certain facilities can function and are financed, ordering a transfer of resources between these enterprises and their private users can, by contrast, be seen as saving expenditure which the state would otherwise have to make, and so these measures can be classified as aid in the meaning of Art. 87, Para. 1 EC Treaty (e.g. financing the public radio corporations).⁷⁷

90. The alternative “or through State resources” is intended to prevent evasion and also extend aid control to the indirect assignment of public funds through facilities that are not sovereign powers (e.g. a public enterprise like a state-owned bank). The criterion is met if the economic advantage ultimately comes from state funds and the aid is also assignable to the state.⁷⁸

the Länder financial compensation arrangements. This also applies to cases where the tax in question is not charged uniformly throughout Germany. Cf. also Arhold, C., loc. cit.

75 In its judgement on the *PreussenElektra* case of 13 March 2001, Case C-379/98, Rec. 2001, I-2099, No. 59, the ECJ decided that a law that obliges electricity supply companies to buy the electricity produced in their distribution area from renewable energies (obligatory purchasing) and to pay a minimum rate for this electricity that is higher than its actual commercial value (the minimum remuneration regulation) is not state aid because there is no charge on the state budget.

76 Act to Give Priority to Renewable Energies of 1 July 2004, BGBl. I, p. 1918; for more detail on the Renewable Energies Law see Monopolkommission, *Strom und Gas 2007: Wettbewerbsdefizite und zögerliche Regulierung*, Sondergutachten 49, Baden-Baden 2008, Items 79ss.

77 Cf. Monopolkommission, *Mehr Wettbewerb auch im Dienstleistungssektor! Hauptgutachten 2004/2005*, Baden-Baden 2006, Item 788.

78 If the advantage is granted by a public enterprise the mere fact that the state can exercise a dominant influence is not enough, according to jurisprudence by the ECJ. For financial support given by this enterprise to a third party to be classified as state aid the European Court deems it necessary for state offices to be involved in some way in issuing the specific measure. ECJ, Judgement of 16 May 2002, Case C-482/99, *Star dust Marine*, Rec. 2002, L-4397, No. 52.

5.2.4 Restriction of Trade between Member States

91. Under Art. 87, Para. 1 EC Treaty measures are only subject to aid control if they “affect trade between Member States”. This criterion is intended to exclude effects on purely national trade from the area of application of Art. 87, Para. 1 EC Treaty, and it serves to delimit the areas of competence of the Community and member states in the control of state aid. In many cases the European Court of Justice examines the criteria of “distortion of competition relevant to the Community” and “restriction of trade between Member States” as a single issue.

92. According to long-standing jurisprudence the European Commission is not obliged to prove the actual effects of state aid on trade within the Community,⁷⁹ it regards as sufficient a tendency to restrict trade. In so far the requirements are very slight. According to the jurisprudence, neither a relatively small amount of aid nor a relatively small company as beneficiary exclude the possibility of restriction of trade between member states.⁸⁰ So in contrast to the antitrust regulations in Arts. 81 and 82 EC Treaty noticeable restriction of trade has not so far been required as an unwritten rule. In the view of the Monopolkommission that is not appropriate. In aid control as well, it should be an unwritten rule that noticeable restriction of trade between states is an essential condition, to prevent matters of purely local significance coming under the European aid regime.

93. In aid supervision, unlike under EU antitrust legislation, the European Commission does not have the power to decide whether it should deploy a procedure. It is obliged to intervene in any measure that could be unlawful state aid. The De minimis regulation provides for some relief.⁸¹ It states that certain cases of state aid that do not exceed a specific amount do not give rise to any restriction in the meaning of Art. 87, Para. 1 EC Treaty and consequently do not have to be notified to the European Commission under Art. 88, Para. 3 EC Treaty.⁸² In addition, certain forms of aid are exempt from obligatory notification under block exemption regulations.

5.2.5 Distortion of Competition

94. Art. 87, Para. 1 EC Treaty prohibits aid granted by member states only if it “distorts or threatens to distort competition”. According to the jurisprudence by the European Court of Justice the criterion of distortion to competition in Art. 87, Para. EC Treaty is met if aid strengthens the position of the beneficiary over (current or potential) competitors.⁸³ Initially the European Commission held the view that it did not need to detail the circumstances which, in its view, constituted (the threat of) distortion to competition in a specific case. Aid would always distort competition.⁸⁴ In 1985 the European Court of Justice decided that the Commission must at least name these circumstances in the justification of its decision, al-

79 ECJ, Judgement of 15 June 1999, Case T-288/97, Friuli Venezia Giulia/Commission, Rec. 1999, II-1871, No. 47f; Judgement of 15 June 2000, Case T-298/97, Alzetta Mauro/Commission, Rec. 2000, II-2319, Nos. 76ss.

80 ECJ, Judgement of 3 March 2005, Case C-172/03, Heiser/Innsburck Tax Office, Rec. 2005, I-1627, No. 25.

81 Commission Regulation (EC) 1998/2006 of 15 December 2006 on the application of Arts. 87 and 88 EC Treaty to “De minimis” aid”, OJ EU L 379 of 28 December 2006, p. 5.

82 The upper threshold has now been raised. Formerly financial aid that did not exceed a total amount of EUR 100,000 within three years was not state aid. In the new De minimis regulation that amount has been raised to EUR 200,000. Loan securities are permitted up to EUR 1.5 million.

83 ECJ, Judgement of 13 June 2000, Case T-204/97, EPAC/Commission, Rec. 2000, II-2267, Nos. 87ss.

84 Commission of the European Communities, Eleventh Competition Report 1981, Brussels, Luxemburg 1982, No. 176.

though in certain cases it could be clear from the circumstances in which aid was granted that it would distort or threaten to distort trade between member states.⁸⁵ However, the Court does not require a very detailed account. A summary of the circumstances relevant to competition and plausible explanation of the actual or threatened distortion to competition are regarded as sufficient “proof” that there is at least a risk of distortion to competition.⁸⁶ The European Commission only has to show which sectors are potentially affected by the aid, that there is competition in these sectors, that competitors are affected in different ways by the aid in question and that the favourable treatment is likely to affect competition.⁸⁷ A quantitative analysis of the possible effects of the aid on competition and an exact delimitation of the market are not required by the Court.⁸⁸

95. The jurisprudence in connection with Art. 87, Para. 1 EC Treaty thus traditionally allows the European Commission a wide margin of appreciation. In contrast to Arts. 81 and 82 EC Treaty the European Court of Justice does not require a specific intensity or evidence of distortion to competition as an unwritten rule.⁸⁹ As a result cross-frontier distortion to competition is generally assumed as soon as it is clear that there is a selective benefit to certain companies or production branches in the meaning of the above jurisprudence. Nor is this assumption prescribed in the wording of the norm. The use of the phrase “threaten to distort” in Art. 87, Para. 1 EC Treaty does show that simply the possibility of distortion to competition is sufficient, it need not actually materialise for the ban to be applied. But it cannot be deduced from this that a concrete account of the competition situation and the facts that give rise to the danger of adverse effects on competition could be dispensed with.

96. The formulation of the competition criterion in Art. 87, Para. 1 EC Treaty differs from that in the antitrust norm in Art. 81, Para. 1 EC Treaty, where the phrase “which distorts or threatens to distort competition” is not used; instead the reference is to certain practices “which have as their object or effect the prevention, restriction or distortion of competition within the common market”. Nevertheless, in Art. 81, Para. 1 EC Treaty the various practices that restrict competition are interpreted as inadmissible in order to protect competition.⁹⁰ Moreover, both Art. 87, Para. 1 EC Treaty and Art. 81, Para. 1 EC Treaty refer to the objective named in Art. 3, Para. 1 C) EC Treaty, namely to protect competition on the internal market from distortion. Therefore, it does not necessarily follow from the different formulations of the criterion of competition in Art. 81, Para. 1 EC Treaty on the one side and Art. 87, Para. 1 EC Treaty on the other that competition is to be interpreted differently in the legislation on state aid from the antitrust legislation.

85 ECJ, Judgement of 13 March 1985, Verb. Cases 296 and 318/82, Netherlands and Leeuwarder Papierwarenfabriek, Rec. 1985, No. 24.

86 ECJ, Judgement of 15 June 1999, Case T-288/97, Friuli Venezia Giulia/Commission, Rec. 1999, II-1871, No. 48/50; judgement of 15 June 2000, Case T-298/97, Alzetta Mauro/Commission, Rec. 2000, II-2319, No. 95; judgement of 13 June 2000, Case T-204/97, EPAC/Commission, Rec. 2000, II-2267, Nos. 35/47s.; judgement of 29 September 2000, Case T-55/99, CETM/Commission, Rec. 2000, II-3207, Nos. 102ss.

87 ECJ, Judgement of 13 June 2000, Case T-204/97, EPAC/Commission, Rec. 2000, II-2267, Nos. 87ss.

88 ECJ, Judgement of 17 September 1980, Case 730/79, Philip Morris/Commission, Rec. 1980, 2671, Nos. 9 and 11s.

89 ECJ, Judgement of 19 September 2000, Case C-156/98, Germany/Commission, Rec. 2000, I-6857, No. 32/29.

90 An examination of the actual effects of Art. 81, Para. 1 EC Treaty is not necessary, according to the jurisprudence of the European courts, if the agreement in question is objectively likely to cause distortion of competition. For the purpose in question, therefore, it is sufficient for disadvantageous effects on competition typically to occur, without proof being required that this was actually intended by the parties involved. For more detail see Bechtold, R., et al., EG Kartellrecht, Kommentar, Munich 2005, Art. 81 EC Treaty, Nos. 70ss.

97. The Monopolkommission regards the fact that the legislation on state aid does not require a detailed examination of the competition situation as dubious for several reasons. Firstly, because the criterion of trade between member states is interpreted very widely and extended to cover cases that are largely local, and secondly, because to meet the criterion of selective advantage (“favouring certain undertakings or the production of certain goods”) a very low degree of selectivity is regarded as sufficient and is held to be evident even with measures that benefit all the companies in a region or all those of a certain size, and thirdly, because the level of state aid granted can be very low.⁹¹

5.2.6 Conclusion

98. In the past the criterion of distortion to competition has not been the subject of detailed economic study by the European Commission. The economic proof required by the European courts to establish distortion of competition has so far been minimal – unlike the requirements in the field of merger control and the antitrust regulations in Arts. 81 and 82 EC Treaty. Accordingly, the European Commission has usually limited its consideration of the criterion of distortion of competition to a general sector-specific examination. If, in its view, there is selectivity and favouring, distortion of competition and restriction of trade are generally assumed, although owing to the broad interpretation of selectivity, a large number of measures with horizontal objectives and very broad effect come into the area of application of Art. 87, Para. 1 EC Treaty. In the case of restriction of trade between member states and distortion to competition it is not an unwritten rule that the threat of restriction should at least be “noticeable” – unlike under the antitrust regulations in Arts. 81 and 82 EC Treaty. Consequently, Art. 87, Para. 1 EC Treaty also applies to cases that are largely local. The Monopolkommission, by contrast, believes that – as with Art. 81, Para. 1 EC Treaty – the objective likelihood that an aid measure will noticeably distort competition and cause noticeable restriction of trade between member states should be examined in the state aid control procedure.

99. The broad interpretation of the concept of state aid and the low level of proof required mean that the European Commission must also follow up cases that are hardly relevant. Under Art. 10, Para. 1 of Procedural Regulation 659/1999⁹² it must examine without delay all information of whatever origin on state aid that may be unlawful. Generally the European Commission is informed when competitors of the favoured company lodge a complaint of unlawful state aid that has not been notified. The European Commission’s obligation under Art. 10, Para. 1 of the Procedural Regulation to examine such cases is very far-reaching. As soon as its examination of the information confirms that there may possibly be unlawful state aid the European Commission must continue the procedure, as for notified aid, and reach a decision.⁹³

5.3 Justification – Examination of Compatibility (Art. 87, Paras. 2 and 3 EC Treaty, Art. 86, Para. 2 EC Treaty)

100. Measures to which the ban on state aid in Art. 87, Para. 1 EC Treaty applies can be granted exemption. The grounds for exemption are given in the EC Treaty, in particular in Art. 87, Paras. 2 and 3 and Art. 86, Para. 2.⁹⁴ The European Commission will decide whether

⁹¹ Under the revised De minimis Regulation only state aid of a promotional level up to EUR 200,000 is exempt.

⁹² Council (EC) Regulation 659/1999 of 22 March 1999 on laying down detailed rules for the application of Article 93 of the EC Treaty

⁹³ See Art. 13, Para. 1 together with Art. 4 Procedural Regulation.

⁹⁴ There are also special rules on state aid for agriculture (Art. 36 EC Treaty) and transport (Arts. 73, 76 EC Treaty).

a measure may be permitted by way of exemption either in an individual procedure or generally under a block exemption regulation. In the compatibility examination which it has been authorised to conduct the European Commission must weigh the intended and expected positive effects of the aid measure against the risk of negative consequences to competition.

5.3.1 Legal Exemptions in Art. 87, Para. 2 EC Treaty

101. Art. 87, Para. 2 EC Treaty contains the following grounds for exemption:

- exempts aid of a social character, if it is granted to individual consumers without discrimination related to the origin of the products.⁹⁵
- exempts aid granted to remedy damage caused by natural catastrophes or other extraordinary events (e.g. the economic consequences of the Gulf War).
- finally, states that aid given to compensate for the economic disadvantages caused by the division of Germany is compatible with the Common Market.⁹⁶

102. 987. If, after examining the results, the European Commission concludes that one of these three criteria for exemption is present it must declare the aid in question compatible with the Common Market. It has no scope for discretion in applying Art. 87, Para. 2 EC Treaty. However, the legal exemptions in Art. 87, Para. 2 EC Treaty are of little practical importance.⁹⁷

5.3.2 Grounds for Exemption in Art. 87, Para. 3 EC Treaty

103. Unlike under Art. 87, Para. 2 EC Treaty the European Commission does have wide powers of discretion in applying Art. 87, Para. 3 EC Treaty. This disposition, frequently applied in practice, contains five, very generally formulated grounds for exemption, letters a) to e):

- a) covers regional aid to promote the economic development of areas where the standard of living is extraordinarily low, or where there is serious underemployment. Under this condition only areas that are particularly weak economically, measured by the EU average, are eligible. Disadvantage compared with the national average of the member state in question is not sufficient. This condition is to enable regional cohesion between member states to develop.
- b) covers aid to promote important projects of common European interest or to remedy a serious disturbance in the economy of a member state. Projects of common European interest (the first alternative) can be aid for research and development projects, if the projects are important qualitatively and quantitatively, if the Community has a direct interest in them and if a number of member states are involved. A serious disturbance in the economy of a member state (the second alternative) is only assumed by the European Commission extremely rarely and only under very strict conditions.⁹⁸

⁹⁵ This is firstly on condition that the measure is aid as defined in Art. 87, Para. 1 EC Treaty. This can only be assumed for advantages granted to consumers if certain companies or branches of production benefit indirectly. One example is tax exemptions granted by a member state to owners of private cars with catalytic converters, independent of the make of the car.

⁹⁶ The European courts interpret this exception, which was included in the Treaty long before German reunification, very narrowly. Only aid granted to compensate for disadvantages directly resulting from the physical construction and maintenance of the inner-German border is included. The exemption covers disadvantages caused by the break in the transport routes, for example.

⁹⁷ Cf. Jestaedt, T., Schweda, E. in Heidenhain, M. (ed.), *Handbuch des Europäischen Beihilfenrechts*, Munich 2003, § 14, No. 2.

⁹⁸ Since the start of the 1980s the European Commission has only applied this in the case of Greece; the consequences of German reunification were not regarded as sufficient economic disturbance.

- c) covers aid to promote the development of certain economic branches or economic areas. The first alternative (branches) covers a large number of different measures. As well as rescue packages and restructuring aid, measures with horizontal objectives (aid for research and development, environmental protection and exports) can be justified, as can sectoral aid (e.g. for the transport sector or the automotive industry). The second alternative, economic areas, again covers regional aid. Unlike the conditions in a) it is not necessary here for the region benefiting to be particularly disadvantaged by the EU average, regions with general development problems (compared with other regions within the member state concerned) can also benefit. In contrast to the areas regarded as particularly in need of promotion under a), promotion is only possible here if it “does not adversely affect trading conditions to an extent contrary to the common interest”.
- d) refers to aid to promote culture and for heritage conservation.
- e) permits the Council to agree to other kinds of aid at the proposal of the European Commission if they are compatible with the Common Market.⁹⁹

104. The criteria in Art. 87, Para. 3 EC Treaty which allow exemptions from the ban on aid not only for economic policy reasons but more particularly for non-economic considerations (regional policy, social, cultural reasons) are indeterminate legal concepts that allow the European Commission a wide margin of discretion. Consequently, despite supranational aid control the danger of intransparent decision-making and (industrial) policy influence is not excluded. This applies particularly in view of the fact that the European Commission is not designed as an independent competition authority, but as a political body with far-reaching legislative and executive powers, and consisting of a large number of Directorates-General. They are naturally pursuing contradictory aims in some cases (e.g. the DG Environment and the DG Trade and Industry). The member states also frequently pursue national interests on European level and attempt to exert influence to that effect. In practice most of the exemptions which the European Commission grants individually or under block exemption regulations are granted on the basis of Art. 87, Para. 3 a) or c) EC Treaty.

5.3.3 Publications to Date Concretising the European Commission’s Approvals Practice

105. The European Commission has issued a large number of guidelines and Community frameworks in the past¹⁰⁰ to concretise the approvals conditions and typify the assessment procedure. The aim is ensure transparency and legal certainty in the application of Art. 87, Para. 3, EC Treaty and the justification given there, especially in a) and c). Hence a complex system of regulations has been created, most of which refer to the objective of the aid and differentiate between the categories below (see Table VI.1).

⁹⁹ The Council has used these powers to regulate aid to the shipbuilding industry and hard coal mining. Beside the option named in Art. 87, Para. 3 e) EC Treaty to extend the general list of aid that can be approved, the member states also have the possibility of taking a (political) decision in individual cases under Art. 88, Para. 2, Sentence 3 EC Treaty. If aid has not been approved by the European Commission under Art. 87, Para. 1 EC Treaty, under this regulation the Council, upon application by a member state, can decide unanimously and in deviation from the grounds for exemption in the EC Treaty, that a measure granted or planned by this state is compatible with the Common Market, if “exceptional circumstances” justify the decision. This political caveat has parallels with the ministerial approvals procedure provided for mergers in German antitrust law (§ 42, Act Against Restraints of Competition).

¹⁰⁰ In some cases with the participation of the European Council.

106. It is characteristic of these past publications (Community frameworks, communications, guidelines)¹⁰¹ that several conditions are set that are relatively easy to establish and can be fulfilled cumulatively; moreover they automatically involve certain legal consequences (like the compatibility of aid with Art. 87, Para. 3 EC Treaty). Accordingly, the legal consequences do not depend on the economic effects of the measure, the right categorisation (for instance as horizontal environmental protection aid or regional aid) plays a decisive part. That is why the approach used so far is known as the “form-based approach”.¹⁰²

Table VI.1:

Categories of State Aid

Guidelines and Community Framework Documents interpreting Art. 87, Para. 3 EC Treaty refer to:		
<p>1) Horizontal Aid</p> <p>(= aid with horizontal objective not limited right from the start to individual companies or branches for</p> <ul style="list-style-type: none"> • research and development • small and midsize firms • risk capital • employment and training • environmental protection <p>Aid with horizontal objectives is generally regarded by the European Commission as relatively less distortive of competition¹</p>	<p>2) Regional Aid</p> <p>(= aid to support regional development and cohesion, Art. 87, Para. 3 a) and c) EC Treaty</p> <p>Regional aid plays a big part in member states’ promotional activities.</p> <p>There are also a number of Community regional promotion instruments (structural funds), with which member states’ regional promotion policy is increasingly to be coordinated.</p>	<p>3) Other Aid</p> <p>a) Sectoral aid</p> <p>Branch-specific, Community framework under Art. 87, Para. 3 EC Treaty for the following areas:</p> <ul style="list-style-type: none"> • Iron and steel • Artificial fibres • Motor vehicles • Shipbuilding • Agriculture (Art. 36 EC Treaty) • Fishing (Art. 36 EC Treaty) • Air and sea transport • Electricity <p>There are also special rules for rail, road and inland waterways transport (Arts. 73, 76 and 78 EC Treaty)</p> <p>b) Special rescue and restructuring aid</p> <p>(for companies and branches in difficulties)</p> <p>The European Commission regards this type of aid as particularly problematic.</p>

¹ Report by the European Commission, State Aid Scoreboard, Autumn edition 2006, COM(2006)761, final, p. 18.

Source: Monopolkommission

101 Only the Community frameworks are general acts of legislation, not the guidelines and communications from the European Commission. These instruments, by which the European Commission undertakes a self-binding obligation, are comparable to the “administration regulations” familiar in German law.

102 Cf. Lowe, P., Some Reflections on the European Commission’s State Aid Policy, Competition Policy International 2, 2006, pp. 77ss.

107. Beside these measures (the justification level), which involve the examination of compatibility under Art. 87, Para. 3 EC Treaty, the European Commission has published communications and regulations on the following areas:¹⁰³

- The interpretation of the ban in Art. 87, Para. 1 EC Treaty (example: De Minimis Regulation)¹⁰⁴
- Obligatory notification under Art. 88, Para. 3 EC Treaty (especially block exemption regulations)¹⁰⁵
- Certain forms of aid (e.g. obligatory liabilities and guarantees)
- Financial transfers to public enterprises and companies providing services of general economic interest and
- The procedure to be carried out (preliminary examination and formal investigation procedure by the European Commission, injunction to recover unwarranted aid by member states)¹⁰⁶

108. The above acts of secondary legislation and measures are mutually complementary and some of the objectives overlap. Regional aid for structurally weak areas with horizontal objectives, for example, is privileged. There are also several regulations that contain privileges for small and midsize companies (SMEs).¹⁰⁷ In the State Aid Action Plan (SAAP), in which the European Commission presents its new reform concept, it states aptly itself that over time the documents have grown in number and become increasingly complex, so that streamlining is now necessary¹⁰⁸.

5.3.4 The Special Area of Services of General Interest (Art. 86, Para. 2 EC Treaty)

109. The justification given in Art. 86, Para. EC Treaty is relevant in the field of what is known as “services of general interest”, a term which is used for state measures to ensure the basic welfare of the population.¹⁰⁹ Which areas are actually covered by such “essential supply” has not been finally clarified, and the range can be defined in various ways.¹¹⁰ The term used in Art. 86, Para. 2 EC Treaty is not essential supply but “services of general economic interest”. While services to provide basic welfare include both market related and non-market related activities, services of general economic interest are solely market related.¹¹¹

¹⁰³ In some cases with the participation of the EU Council.

¹⁰⁴ This states that certain aid that does not exceed a fixed amount does not cause distortion in the meaning of Art. 87, Para. 1 EC Treaty and so does not need to be reported to the European Commission under Art. 88, Para. 3, Sentence 1 EC Treaty.

¹⁰⁵ In Regulation 994/98, OJ EC L142 of 14 May 1998, which is based on Art. 89 EC Treaty, the European Council has empowered the European Commission to issue block exemption regulations for certain groups of horizontal aid. Accordingly in certain horizontal areas of promotion the Commission may determine which aid projects are per se compatible with the Common Market.

¹⁰⁶ Cf. Procedural Regulation 659/1999.

¹⁰⁷ E.g. the Guidelines on State Aid to Promote Risk Capital Investment in Small and Midsize Enterprises (OJ EU C 194, of 18 August 2006, p. 2), the Guidelines for State Aid with Regional Objectives 2007-2013 (OJ EU C 54 of 4 March 2006, p. 13), which i.a. provide for business aid for small companies in promotional areas to assist their development in the start-up and early phases.

¹⁰⁸ SAAP, Item 17.

¹⁰⁹ Cf. Haucap, J., Daseinsvorsorge zwischen Beihilfenkontrolle und globalem Wettbewerb, Wirtschaftsdienst 87, 2007, pp. 712-716.

¹¹⁰ See 2.3.2 above.

¹¹¹ Cf. European Commission, Report for the European Council in Laeken, Brussels, 17 October 2001, COM (2001), 598, final version p. 24; Kallmayer, A., Jung, C., in: Callies, C., Ruffert, M. (eds.), EUV/EGV, 3rd ed., Munich 2007, Art. 16 EGV No. 2.

These services differ from normal services in that in the view of the state they must also be provided if the market does not offer incentives for their provision to the politically desirable extent.¹¹² According to the jurisprudence of the European courts member states have a wide margin of appreciation over which type of services they regard as being of general economic interest. Labour placement, postal operations, telecommunications, transport, energy supply and public broadcasting are all recognised as services of general economic interest. In the view of the Monopolkommission, as an exception Art. 86, Para. 2 EC Treaty should be interpreted narrowly. Otherwise there is a risk that the efforts to liberalise the network industries could be counteracted with greater use of state aid and national markets could be sealed off.¹¹³

110. In November 2005 the European Commission published its decision that certain types of aid for essential supply are exempt from obligatory notification.¹¹⁴ So this decision fulfils the same function as a block exemption regulation. It exempts compensation payments to enterprises whose annual turnover on all activities before tax did not exceed EUR 100 million in the two accounting years preceding the assumption of a service of general economic interest, and that receive a compensation payment of less than EUR 30 million per year for the service provided. The maximum limit of EUR 30 million for the aid is clearly above the general upper limit of EUR 200,000 in the De Minimis Regulation. Certain areas (social housing construction, hospitals, airports and seaports) are further privileged under this decision, because these upper limits for turnover and aid received do not apply to them.

111. Under Art. 86, Para. 2 EC Treaty the ban on state aid in Art. 87, Para. 1 EC Treaty only applies to (public or private) enterprises that are entrusted with the provision of services of general economic interest as long as “the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them”. However, the justification in Art. 86, Para. 2 EC Treaty will only apply if the measure in question can in fact be classified as aid in the meaning of Art. 87, Para. 1 EC Treaty, and is not simply a compensation payment for services required by the public authorities.¹¹⁵

112. The relation between the ban in Art. 87, Para. 1 EC Treaty – to be more exact, the criterion of “favouring certain undertakings or the production of certain goods” (selectivity) – and the justification in Art. 86, Para. 2 EC Treaty is controversial. The following basic positions are taken. In the 'aid interpretation' state funds granted to an enterprise for the provision of services of general benefit are always state aid in the meaning of Art. 87, Para. EC Treaty, although it can be justified under Art. 86, Para. 2 EC Treaty.¹¹⁶ In the 'compensation approach' state funding of services of general economic interest is only aid in the meaning of Art. 87, Para. 1 EC Treaty if and in so far as the economic advantage granted goes beyond adequate compensation for the provision of these services, or beyond the additional costs which this provision entails.¹¹⁷ The difference is that in the compensation approach state financing of this

112 Cf. also Art. 16 EC Treaty, which was introduced in the Amsterdam Treaty and is intended to underline the special importance of Community services.

113 In the field of antitrust legislation there could be state distortion of competition in the form of allowing major national mergers or preventing cross-frontier mergers.

114 Decision by the European Commission of 28 November 2005 on the application of Article 86, Para. 2 EC Treaty to state aid granted to certain enterprises that are entrusted with providing services of general economic interest, OJ EU L312, of 29 November 2005, p. 67.

115 The European Court of Justice has given the conditions for this in more detail in the judgement on Altmark Trans; Judgement of 24 July 2003, Case C-280/00, Rec. 2003, I-7747.

116 Cf. Koenig, C., Kühling, J., in: Streinz, R. (ed.), EUV/EGV, Munich 2003, Art. 87 EGV, No. 35.

117 European Court of Justice, Judgement of 22 January 2001, Case C-53/00, Ferring, Rec. 2001, I-907, Nos. 32s.

kind is not subject to the notification requirement in Art. 88, Para. 3, Sentence 1 EC Treaty. Independent of the legal classification, however, there is agreement that overcompensation of the costs to enterprises of providing such services is generally impermissible, that is, the condition in Art. 87, Para. 1 EC Treaty is met and the aid is not justified under Art. 86, Para. 2 EC Treaty, either. However, the Monopolkommission believes it will be difficult in practice to calculate the additional costs of providing essential supply services.

113. In its more recent decision-making practice the European Commission has been pragmatic and used both the aid approach and the compensation approach. It has applied the same criterion, appropriate compensation, on both the factual level and the justification level. If the compensation can be identified as appropriate without difficulty, this in itself shows that the circumstances described in Art. 87, Para. 1 EC Treaty do not exist. If it cannot, the European Commission undertakes a detailed examination of the matter on the justification level (Art. 86, Para. 2 EC Treaty). The principles established by the European Court of Justice in the *Altmark Trans* judgement serve as the standard.¹¹⁸ According to these, in the field of public welfare state aid in the meaning of Art. 87, Para. EC Treaty is not being given if the finance is clearly, transparently and directly a consideration for clearly defined obligations in the public interest and the beneficiary is not fixed right from the start. If these conditions are met in an individual case the European Commission assumes that the compensation paid for the provision of services of general economic interest is not favourable treatment in the meaning of Art. 87, Para. EC Treaty. If aid that requires to be notified is being given this may be justified under Art. 86, Para. 2 EC Treaty, and here the decisive factor is whether the financing in question is necessary as compensation for the performance of public tasks and is appropriate to this purpose.

114. In the Community Framework of November 2005 the principles for the application of Art. 86, Para. 2 EC Treaty are concretised.¹¹⁹ According to this framework, the level of compensation may not go beyond what is necessary to cover the costs incurred in fulfilling the

¹¹⁸ ECJ, Judgement of 24 July 2003, Case C-280/00, *Altmark Trans*, Rec. 2003, I-7747, Nos. 89-93. The European Court names the following conditions under which financial compensation for services of general benefit is not to be classified as state aid:

First, the recipient enterprise must actually be required to discharge public service obligations, and those obligations have to be clearly defined. So the court had to examine whether the services of public interest which *Altmark Trans* was obliged to perform were clear from the national legal requirements and/or the approvals in dispute in the initial proceeding.

Secondly, the parameters on the basis of which the compensation is calculated must have been established beforehand, clearly and objectively. This is to prevent the compensation creating an economic advantage that would favour the enterprise to which it is granted over its competitors.

So if a member state compensates the losses suffered by an enterprise before the parameters are established, because it subsequently becomes clear that these public obligations could not have been performed commercially, this constitutes financial intervention and is regarded as state aid in the meaning of Art. 92, Para. EC Treaty.

Thirdly, the compensation must not exceed the amount necessary to cover all or part of the costs of performing these public obligations, taking into account the relevant receipts and a reasonable profit for discharging these obligations. Only if this condition is met can it be ensured that the enterprise is not being given an advantage that will strengthen its competitive position and so distort or restrict competition.

Fourthly, if in a specific case the enterprise that is to perform public obligations has not been selected in a procedure for the award of public contracts which would enable that applicant to be chosen who can perform these services at the lowest cost for the general public, the level of compensation required must be determined on the basis of an analysis of the costs of performing these services to an average enterprise that is well managed, has the appropriate means of transport and can meet the public requirements. The income thereby earned and an appropriate profit are to be taken into account.

¹¹⁹ Community framework for state aid given as compensation for the provision of public services, OJ EU C 297 of 29 November 2005, p. 4.

public obligation, taking into account the income thereby earned and an appropriate return on the performance of these obligations.¹²⁰ Moreover, the compensation may only be used to ensure that the service of general economic interest functions. Financial compensation used to operate on other markets is not justified and is classified as state aid that is incompatible with the Common Market. Under European competition law cross-subsidisation of this kind can come under both the legislation on state aid and the antitrust legislation. Under Art. 82 EC Treaty the European Commission or the national competition authorities can proceed against cross-subsidisation if the enterprise concerned has a dominant market position and attempts to extend this market power to a neighbouring competitive market by transferring profits. If the funds used are state grants the European Commission can intervene with reference to the legislation on state aid. The problem of cross-subsidisation through state payments for basic security arises particularly in the liberalised economic sectors like postal services, telecommunications and the energy sector.¹²¹ In practice it is frequently extremely difficult to prove cross-subsidisation.

5.4 The Procedural Aspects

5.4.1 Proceedings before the European Commission

5.4.1.1 Aid Duly Notified

115. Unless an exception is stipulated under a block exemption regulation member states are obliged to notify the European Commission of any new aid they intend to give (Art. 88, Para. 3, Sentence 1 EC Treaty).¹²² As long as the aid has not been notified to and approved by the European Commission, the member state may not grant it (Art. 88, Para. 3, Sentence 3 EC Treaty). Infringements of this ban on execution can be brought directly before the national courts by competitors of the benefiting enterprise.¹²³

120 According to No. 16 of Community framework 2005 the costs comprise:

- The variable costs incurred for the provision of services of general economic interest
- An appropriate contribution to the fixed costs, both those related to the public service provided and those incurred elsewhere.
- An appropriate return on the enterprise's equity capital that can be assigned to the services of general economic interest.

The appropriate return is to be calculated by a comparison of profits in accordance with the principles in No. 18 of the framework:

- An appropriate return is an appropriate yield on capital, taking into account the risk, if any, entered into by the enterprise from the state intervention. This applies particularly if the state grants exclusive or special rights.
- The appropriate return should correspond to the profitability shown for that sector and as a rule it may not exceed the average return obtained in that sector in the immediately preceding years.
- In sectors where there are no enterprises that can serve as standard of comparison for the enterprise entrusted with the provision of services of general economic interest enterprises in other member states, or if necessary in other sectors, may be used for comparison, on condition that the special characteristics of the sector in question are taken into account.

On the problem of Cost Standards cf. Monopolkommission, Preiskontrollen in Energiewirtschaft und Handel? Zur Novellierung des GWB, Sondergutachten 47, Baden-Baden 2007, No. 20.

121 Cf. Mestmäcker, E.-J., Schweitzer, H., loc. cit., § 43, Nos. 35s.

122 While Art. 88, Para. 3 EC Treaty applies to new aid, Art. 88, Paras. 1 and 2 EC Treaty cover current aid, which, unlike new aid, does not have to be reported to the European Commission. The European Commission constantly appraises the current rules on state aid (Art. 88, Paras. 1 and 2 EC Treaty). Essentially, aid being given before the EC Treaty came into force on 1 January 1958 or before a member state joined the EU is classified as current aid, as is aid previously approved by the European Commission or the Council in some way.

123 Cf. 5.4.3 for more detail.

116. The European Commission's procedure in state aid control, like its merger control, is divided into two phases, the preliminary examination and the formal investigation procedure, which follows if necessary. In the preliminary examination the European Commission examines whether the project notified gives cause for concern. After a full notification has been received the European Commission must decide within two months whether it will approve the aid or whether it wishes to make a detailed examination and initiate the formal investigation procedure. If it fails to give a decision by that deadline fictive approval can be assumed.¹²⁴ In this first phase of the supervisory procedure only the European Commission and the member state are involved, while the enterprise receiving the aid and its competitors are not admitted. Nor can the latter learn of the notification and the deployment of a preliminary examination, as these facts are not published. By far the greater majority of cases are concluded in this preliminary examination stage.¹²⁵

117. If the European Commission was not able to clarify the question of the legality of the aid in the preliminary procedure it initiates the formal investigation procedure. The decision to do so is published in the Official Journal (Art. 26, Para. 2 together with Art. 4, Para. 4, Procedural Regulation). In the formal investigation procedure beside the member state concerned in accordance with Art. 20, Para. 1 Procedural Regulation, other "interested parties" may give a written statement. "Interested parties" here means "any Member State and any person, undertaking or association of undertakings whose interests might be affected by the granting of aid, in particular the beneficiary of the aid, competing undertakings and trade associations" (Art. 1 lit. h) Procedural Reg.). This possibility for participation is intended not only to take account of the interests of parties that may be affected but also to open up a source of information for the European Commission. Under Art. 7, Para. 6, Sentence 2 Procedural Regulation the formal investigation procedure should if possible be concluded within 18 months. However, failure to keep to this deadline – which may be extended by mutual agreement – only enables the member state to demand a decision from the European Commission within two months on the basis of the information available to it (Art. 7, Para. 7 Procedural Regulation). The law does not lay down any conditions should the European Commission also fail to meet this deadline. In particular, unlike the preliminary procedure, a direct sanction in the form of fictive approval will not be imposed. In such a case the member state could therefore only lodge a complaint of excessive delay with the European Court, under Art. 232, Para. 1 EC Treaty.

118. If under Art. 7, Paras. 2 to 5 Procedural Regulation the European Commission concludes the formal investigation procedure by deciding that state aid is not involved, the aid can be approved without objection (positive decision). The European Commission can also issue a positive decision with conditions attached or declare the aid incompatible with the Common Market (negative decision). In practice negative decisions are the exception. The European Commission only decides not to allow aid for about 2% of the duly notified measures.¹²⁶

¹²⁴ The aid is regarded as approved if the European Commission has not issued a decision within two months of receipt of a full notification. The member state may carry out the measure if it informs the European Commission of such intention and the European Commission has still not given a decision within a further 15 working days (Art. 4, Para. 6 Procedural Regulation).

¹²⁵ Between 2000 and 2006 the European Commission did not initiate a formal investigation procedure at all in around 95% of the cases duly notified, but gave a final decision in the preliminary procedure. Cf. Commission Report, State Aid Scoreboard, Spring 2007, COM(2007) 347, final, p. 15.

¹²⁶ Commission Report, State Aid Scoreboard, Spring 2007, loc. cit., p. 7.

5.4.1.2 *Aid that is Formally Unlawful*

119. In practice it often happens that member states grant aid with breach of the obligation to notify the European Commission under Art. 88, Para. 3 EC Treaty and the ban on execution which it contains. Between 2000 and 2006 the European Commission carried out more than 600 procedures on aid that was formally unlawful in this way.¹²⁷ Around 24% of the procedures carried out concerned the Federal Republic of Germany.¹²⁸ The number of cases of formally unlawful aid is probably even higher, as the European Commission will not learn of every case of infringement. Under Art. 10, Para. 1 Procedural Regulation the European Commission must examine without delay all the information it receives on apparently unlawful aid, regardless of its origin. Generally the European Commission is informed that there may have been infringement by third parties who have right of communication under Art. 20, Para. 2 of the Procedural Regulation.

120. The procedure for formally unlawful aid is the same as the procedure already described that is applied for duly notified aid (Arts. 10ss. Procedural Regulation). However, there is a crucial difference in that no deadlines are provided for in the procedure for formally unlawful aid.

121. The European Commission cannot order aid that has been given prematurely in breach of Art. 88, Para. 3, Sentence 3 EC Treaty to be recovered, solely on the grounds of formal illegality. The European Courts also require the aid to be materially incompatible with the Common Market with no possibility of exemption – as under Art. 87, Para. 3 EC Treaty. In the past the European Commission came to the conclusion that formally unlawful aid was also materially inadmissible in about 25% of the cases.¹²⁹ The decision that the aid must be recovered, regularly issued in these cases, is addressed to the member state, who under Art. 14, Para. 3 of the Procedural Regulation must demand repayment of the aid “without delay”, in accordance with its national law.¹³⁰ Objections to repayment are rarely successful.¹³¹

122. In the past, contrary to Art. 14, Para. 3 Procedural Regulation, recovery of aid was frequently not implemented speedily by member states, the payments were stretched, if they were made at all, over several years.¹³² It may be difficult for a member state to obtain return of the aid, for instance if the company has meantime registered insolvency, if the ownership has changed or if a large number of companies have profited from the aid and the benefit consisted of reducing their expenses (for instance through selective tax concessions). In such cases the parties who are obliged to repay and the amount that should be demanded of them can only be determined with considerable expenditure. In only a few member states is the responsibility for implementing the demand for recovery entrusted to a central state authority. In Denmark and Great Britain the national competition authorities are responsible for making the demand. In Germany and most of the other member states, on the other hand, the office

¹²⁷ Loc. cit., p. 4.

¹²⁸ The large member states grant formally unlawful aid relatively frequently. Beside Germany with 24%, Italy accounted for 17%, Spain 12%, France 10% and the United Kingdom 9% of the procedures. Cf. Commission Report, State Aid Scoreboard, Spring 2007, loc. cit., pp. 15ss.

¹²⁹ Commission Report, State Aid Scoreboard, Spring 2007, loc. cit., p. 5.

¹³⁰ Repayment may not be demanded (Art. 14, Para. 1, Sentence 2 Procedural Reg.) if this would infringe a general principle of Community law. Under Art. 14, Para. 2 Procedural Reg. the obligation to repay includes the obligation to pay interest from the date the unlawful aid was made available to the recipient and until it is actually repaid.

¹³¹ For more detail see Sinnavee, A., in: Heidenhain, M. (ed.), loc. cit., § 34, Nos. 16ss.

¹³² Cf. Commission Report, State Aid Scoreboard, Spring 2007, loc. cit., pp. 17ss.

that originally granted the aid is responsible for recovery, but it generally does not have the appropriate specialised knowledge. In Germany this problem is lessened as the central department for aid is in the Federal Ministry of Economics and Technology. Beside making the initial notification of individual grants and regulations on aid to the European Commission it has the task of mediating between the European Commission and the various national donors when carrying out aid measures, including any recovery procedures.

123. Another reason why the recovery procedures can take so long is that in most member states – as in Germany – there are no specific regulations on recovery, general procedural law is applied. A recovery procedure will be very protracted if the recipient of the aid appeals to the national courts against the demand for repayment. These legal proceedings can have the effect of postponing the repayment, a possibility which the state authorities cannot prevent.

124. Under German law, for instance, this will be the case if the aid was granted as part of a contract under civil law. According to general principles a repayment demand must also go through the civil courts in such cases, and it cannot be ordered by sovereign administrative act. However, with reference to the effectivity requirement in Community law,¹³³ the appellate administrative court in Berlin-Brandenburg expressly permitted repayment demands by act of administration for unlawful aid in a decision of 7 November 2005.¹³⁴ This decision raises legal doubts, as a measure by a public authority that involves an obligation – like the issue of an administrative act that must be implemented without delay – may under the principle of the rule of law only be imposed with legal authorisation (the doctrine of legal reservation). A basis in national law is not evident here, and the direct applicability of the regulation in Community law, Art. 14, Para. 3 Procedural Regulation, seems questionable in view of the wording of the regulation.¹³⁵ The effectivity requirement in Community law can mean that a national regulation is not applied, but it cannot of itself provide a basis for authorising intervention to impose an obligation. However, the national legislature should create a legal basis for authorisation that will make immediate recovery possible and generally exclude delay through legal proceedings on national level. Otherwise the distortion to competition caused by granting the aid could possibly persist for years. Exclusion of the delaying effect would not be disproportionate, as a decision by the European Commission to obtain recovery must be implemented by member states. Due account should be taken of the concern for legal protection on the part of the recipients of the aid by enabling them to appeal against the European Commission's decision to demand repayment on EU level, before the Community courts.¹³⁶

133 Under the effectivity requirement (effet-utile principle) national legal protection regulations may not make it practically impossible to implement claims under Community law or hinder these excessively.

134 Appellate Administrative Court of Berlin-Brandenburg, Decision of 7 November 2005, OVG 8 S 93.05, NvwZ 2006, 104-106. In this case the state authority responsible (Bundesanstalt für vereinigungsbedingte Sonderaufgaben – Federal Institute for Special Expenditure related to Reunification) ordered the immediate recovery by act of administration, although the aid had been granted to the beneficiary enterprise (Aker Warnow Werft GmbH) under a contract in civil law. The Berlin-Brandenburg court held the view that owing to the efficiency requirement in Community law a sovereign order was permissible, as only in this way could the obligation imposed by the Commission's decision and in Art. 14, Para. 3 Procedural Reg. be fulfilled and repayment be demanded immediately.

135 Art. 14, Para. 3 Procedural Reg. states: "Without prejudice to any order of the Court of Justice of the European Communities pursuant to Article 185 of the Treaty recovery shall be effected without delay and in accordance with the procedures under the national law of the Member State concerned, provided that they allow the immediate and effective execution of the Commission's decision. To this effect and in the event of a procedure before national courts, the Member States concerned shall take all necessary steps which are available in their respective legal systems, including provisional measures, without prejudice to Community law."

136 Cf. 5.4.3.

125. In keeping with its announcement in the SAAP, the European Commission has now issued a Notice to accelerate the implementation of decisions to recover aid. In it the Commission draws attention to the principles elaborated by the Community courts and aims to explain the Commission's practice in demanding repayment.¹³⁷ The Notice can be a useful guide for the offices in member states that are responsible for dealing with demands for repayment, but it cannot create a binding set of uniform rules for this. In the view of the Monopolkommission, an EU directive to create uniform minimum standards of legal protection in aid cases before national courts would be helpful, as it would i.a. include rules on the possibilities of legal protection against recovery demands.¹³⁸

5.4.1.3 Comparison with the Antitrust Procedure

126. The procedure in aid control differs in several respects from the procedure used in EU antitrust cases. Private parties – especially the enterprises benefiting from the aid and their competitors – have fewer rights and are subject to considerable restrictions. Only the European Commission and the member state granting the aid are parties to the procedure. Private parties can only participate – apart from the permission to send a communication at any time under Art. 20, Para. 2 Procedural Regulation – when the European Commission has initiated the formal investigation procedure, and here they are limited to handing in written statements.

127. The reverse side of the bilateral structure of the aid procedure is that the European Commission does not have the scope for examination which it has in antitrust law. It cannot oblige enterprises and their associations to give information or carry out a sector-specific study (Arts. 17, 18 of the Antitrust Regulation).¹³⁹ As the European Commission has no direct powers to investigate the private market participants affected in an individual case, and who are best informed of conditions in the sectors concerned, it cannot examine the current competition situation to the extent possible under antitrust law. The information problem is made worse because the European Commission must communicate only with the central government of the member state, even if the aid has been planned or given on regional and local level.

128. The law on state aid does contain specific deadlines for Commission procedures on duly notified aid. These deadlines are, however, noticeably longer than those in merger control. While periods of two and 18 months are set for the preliminary and the formal aid control procedures respectively, in merger cases the preliminary procedure may take at most 15 working days, and the main investigation procedure generally at most 105 working days (Art. 10, Paras.1 and 3 Merger Control Regulation).¹⁴⁰ Unlike in merger control (Art. 10, Para. 6 Merger Control Regulation), failure to meet the deadline in the formal procedure in aid control does not involve sanctions on the European Commission, as no fictive approval is generated.¹⁴¹

137 Notice from the Commission – Towards an effective implementation of Commission decisions ordering Member States to recover unlawful and incompatible State aid, OJ EU C 272 of 15 November 2007, p. 4.

138 This is also recommended in the Study on the Enforcement of State Aid Law at National Level, March 2006, Jones Day, Lovells, Allen & Overy, http://ec.europa.eu/comm/competition/state_aid/studies_reports/studies_reports.cfm. The study was commissioned by the General-Directorate for Competition.

139 Council Regulation (EC) 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty.

140 Council Regulation (EC) 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation), OJ EU L 24 of 29 January 2004, p. 1.

141 Aid control procedures that are concluded in the preliminary phase last on average 5.2 months, according to information from the General-Directorate on Competition. The cases for which the European Commission initiates a formal investigation procedure, last on average 21.4 months.

129. A further difference from antitrust law is that owing to the low level of proof required by the European courts to establish most of the facts under Art. 87, Para. 1 EC Treaty, the European Commission is obliged to investigate cases of little relevance. In aid control, unlike antitrust law, the opportunity principle does not apply, as it does for infringements of Arts. 81 and 82 EC Treaty (Art. 11, Para. 1 Reg. 1/2003) nor are there high thresholds for taking up a case, as in merger control (Art. 1, Paras. 2 and 3 Merger Control Regulation). As soon as the examination of the information shows that unlawful aid may have been given the European Commission must continue the procedure, as for notified aid, and reach a decision (cf. Art. 13 in connection with Art. 4 Procedural Regulation). These requirements are only eased by the De Minimis Regulation, which sets a very low threshold (EUR 200,000 within three years), and by the block exemption regulations issued for state aid. Reform of the Procedural Regulation is not planned under the present Commissioner for Competition, Neelie Kroes.

130. In the view of the Monopolkommission the state aid control procedure needs to be reformed, and in certain points brought into line with the antitrust procedures. Instead of the legality principle applied so far (Art. 10, Para. 1 Procedural Regulation) the European Commission could be allowed to judge whether to take up a case, as it can under antitrust law. However, the opportunity principle should only be introduced below a certain volume of promotion. This is still to be determined, but it could be set at EUR 1 million for individual aids. That would enable the European Commission to react flexibly and set priorities by concentrating on important cases. Any distortion to competition caused by low amounts of aid is generally less than that caused by larger amounts. However, that may not be the case for small, highly concentrated markets, or markets that are just developing, and intervention by the European Commission may well be needed here. Effective control and assessment could be made possible if EU member states had to send a brief communication and a description of the aid granted and its recipient to the European Commission for aid that does not exceed a certain fixed threshold. If the European Commission did not express any doubts within a period still to be settled (e.g. two months) the aid could be regarded as approved. If the member state fails to fulfil this obligation *ex post* intervention by the European Commission should still be possible.

131. The discretion allowed to the European Commission over whether to take up a case could be flanked by the introduction of a private action for a declaratory judgement by competitors affected or their associations. The competitors of the recipient of the aid could be given the right to bring an action before the Community courts if the European Commission decides not to carry out a procedure on opportunity grounds. To prevent the European Commission's scope for decision being counteracted and avoid a flood of legal actions the possibility should be considered of allowing the private action only if the competitor's position on the market in question is considerably restricted by the state aid.

132. In addition, the procedural rights in the aid control procedure of the recipients of the aid, their competitors and their associations should be strengthened. The procedure should not remain purely bilateral between the European Commission and the member state concerned, the recipients of the aid should be admitted in the preliminary procedure as a party and the competitors affected (or their associations) as participants. The European Commission should also be allowed direct powers to investigate private parties. That could give it better access to the information it needs to make an economically well-founded estimate of the competitive situation. The efficiency of the Commission's procedure could be increased by introducing both binding and shorter deadlines, with fictive approval to come into force if the deadlines are

missed and no decision is taken. However, this would only appear to be appropriate if the member states have duly notified the European Commission of the aid and did not grant it prematurely by infringing the ban on execution in Art. 88, Para. 3, Sentence 3 EC Treaty. The decision not to set deadlines in the procedures for formally unlawful aid – which is already intended – sets an incentive to observe the obligation to report the aid.

5.4.2 Proceedings before the European Courts

133. If the European Commission has taken a decision classifying aid as incompatible with the Common Market (a negative decision) the member state in question can appeal against the decision in the European Court of Justice on grounds of invalidity under Art. 230, Para. EC Treaty.

134. An authority within a member state can also appeal against a negative decision by the European Commission on grounds of invalidity. That could happen if a German Federal state, for example, or a municipality wished to grant aid entirely or partly out of its own funds and were prevented by a negative decision by the European Commission. Unlike the member states themselves, their regional subdivisions are not, however, entitled per se to appeal. They must prove that they are directly and individually affected by the negative decision (Art. 230, Para. 4, EC Treaty).

135. The criterion of direct effect is met, according to jurisprudence, if the act of Community law affects the interests or the legal position of the plaintiff, without further executory act, or if the national authorities have no discretionary powers at all in the implementation. That is the case in negative decisions by the European Commission, since, although these are addressed exclusively to the member state, they allow no scope for judgement and must be observed by the regional authorities as well.

136. Persons (natural or legal) who are not the addressees of the act of Community legislation are only individually affected, according to the Plaumann verdict by the European Court of Justice,¹⁴² if the act of legislation affects them owing to certain personal qualities or particular circumstances that mark them out of the group of all other persons, and so individualise them in a similar way as addressee. This condition is regarded as met for a regional authority if it is involved financially in the aid or has autonomous powers in granting or demanding repayment of the aid.¹⁴³ Insofar, unlike for cases brought by member states it is not the European Court of Justice that is first competent but the Court of the First Instance (the European Court).¹⁴⁴

137. The potential recipient of the aid can also have an interest in appealing against a negative decision by the European Commission on grounds of invalidity. He, too, is only empowered to bring the suit if he can show that he is directly and individually affected by the negative decision (Art. 230, Para. 4 EC Treaty). The criterion of individual effect is interpreted narrowly by the Community courts following the Plaumann formula. In this context it is important whether the negative decision was on an individual grant or a general aid scheme.

142 ECJ, Judgement of 15 July 1963, Case. 25/62, Plaumann/Commission, Rec. 1963, 213.

143 Cf. ECJ, Judgement of 15 December 1999, Verb. Cases T-132/96 and T-143/96, The Free State of Saxony et al./Commission, Rec. 1999, II-3663, No. 91.

144 Cf. Art. 225, Para. 1 EC Treaty together with Art. 51 of the Protocol on the Statute of the Court, OJ EC C 80 of 10 March 2001, p. 63.

138. Individual aids are characterised by the fact that they are tied to a specific project or are individualised for the recipient.¹⁴⁵ If the European Commission forbids an individual aid, and the enterprise bringing the lawsuit would have profited from it, the individual effect required by the European courts is regarded as present without further examination.

139. The situation is different in cases where the negative decision is on a general aid scheme. In these cases those entitled to receive aid and the projects promoted are not specified in concrete but defined in general and abstract terms (e.g. a statutory tax concession for the application of certain environmental standards).¹⁴⁶ Aid schemes are “self-executing”, that is, they can be implemented in themselves and they justify direct claims. The individual assignment of the favourable treatment follows later, when concrete aid is granted on the basis of the aid scheme. This aid – if it is covered by the decision to allow the aid – does not have to be reported separately to the European Commission under Art. 88, Para. 3, Sentence 1 EC Treaty. In the case of general aid schemes enterprises that can show that they would have profited from the scheme had the European Commission not taken a negative decision are only regarded as authorised to appeal in exceptional cases.¹⁴⁷ If the aid scheme provides for benefits to enterprises in a specific sector, according to jurisprudence it is not sufficient for the enterprise bringing the suit to belong to the sector in question and to have been directly eligible for benefit. In the view of the European Court of Justice the aid scheme is only a general legal norm, from the standpoint of the enterprise bringing the suit. Consequently, the conditions in the Plaumann formula outlined above, namely that the plaintiff must be individualised by the decision owing to personal qualities or special circumstances, are not met. This restrictive line is a fortiori applied in cases where the ban by the European Commission is on a horizontal aid scheme, that is intended to benefit enterprises in various sectors.

140. By contrast, in cases where a member state has already implemented an aid scheme in breach of the ban in Art. 88, Para. 3 EC Treaty before the European Commission has issued its final decision, the enterprises benefiting are regarded as individually affected.¹⁴⁸ These enterprises can then appeal against the decision by the European Commission in which the general aid scheme is classified as incompatible with the Common Market, pleading invalidity under Art. 230, Para. 4 EC Treaty. This leads to contradictory assessments.¹⁴⁹ As a result of this jurisprudence, enterprises that have already received aid in breach of Art. 88, Para. 3 EC Treaty are ultimately privileged over enterprises that would be directly entitled to appeal if the European Commission had not raised objection to the duly notified aid scheme.

141. Nor does the Lisbon Treaty provide for improvement in the legal protection against general aid schemes.¹⁵⁰ Art. 265 of the reform treaty, that is intended to replace Art. 230 EC Treaty, does provide for extension of the right to appeal. In future natural and legal persons

145 In Art. 1 c) Procedural Regulation “individual aid” is defined as aid “that is not awarded on the basis of an aid scheme and notifiable awards of aid on the basis of an aid scheme.”

146 In Art. 1 d) Procedural Regulation the term an “aid scheme” is defined as any act “on the basis of which, without further implementing measures being required, individual aid awards may be made to undertakings defined within the act in a general and abstract manner and any act on the basis of which aid which is not linked to a specific project may be awarded to one or several undertakings for an indefinite period of time and/or for an indefinite amount.”

147 Cf. ECJ, Judgement of 2 February 1988, Cases 67, 68 and 70/85, Van der Kooy/Commission, Rec. 1988, 219, No. 5.

148 Cf. ECJ, Judgement of 29 September 2000, Case T-55/99, CETM/Commission, Rec. 2000, II-3207, Nos. 23ss.

149 Cf. Soltesz, U., in: Heidenhain, M. (ed.), loc. cit., § 43, No. 16.

150 Lisbon Treaty to Amend the Treaty on the European Union and the Treaty to establish the European Union, signed in Lisbon on 13 December 2007, OJ EU C 306 of 17 December 2007, p. 1.

will be able to appeal against acts of EU legislation that have the character of regulations if they are directly affected and if no implementation measures are required. They do not have to provide separate proof that they are individually affected. However, this condition is not met if the European Commission approves a general aid scheme, as it is issued by the member states themselves and not the EU organs, and further concretising measures are generally needed to execute it, like establishing the entitlement. So even after the Lisbon Treaty comes into force proof of direct effect will be needed for general aid schemes as well, to which ECJ applies the restrictive requirements of the Plaumann formula outlined above.

142. Competitors of the enterprise benefiting from the aid can also appeal on European level if at the end of the preliminary or the formal investigation procedure the European Commission finds that the measure in question is not aid, or if it approves an aid. The decisive hurdle for admission of the competitor's suit is again whether he is individually affected under Art. 230, Para. 4 EC Treaty. The jurisprudence of the European courts on the criterion of individual effect on third parties who can be disadvantaged if aid is granted is not stringent. The requirements vary depending on the phase of the procedure (preliminary or formal investigation) and the form of the aid (individual or general).

143. If the decision by the European Commission is not on an individual aid but on a general aid scheme individual effect on competitors is on principle abnegated, as for appeals by the recipient of the aid with reference to the Plaumann formula. The situation is only different if individual aids have already been granted to competing enterprises on the basis of the aid scheme.¹⁵¹

144. If an aid is approved, and if only a preliminary examination has been made, it must be taken into account that the competitor lodging the appeal has had no possibility to participate, as third parties are not admitted at this stage of the procedure. As already shown, parties other than the member state only have the opportunity to exercise their procedural rights, guaranteed also under Art. 88, Para. 2 EC Treaty, by giving a written statement in the formal investigation procedure. At least according to earlier jurisprudence, to prove that a private third party was affected it was sufficient to point out that this party has had no opportunity to exercise its rights as a party involved in procedures by the European Commission as the formal procedure was not opened.¹⁵² To justify involvement in the formal procedure it is sufficient if enterprises' "interests might be affected" (Art. 1 lit. h) Procedural Regulation). Simply potential affection is therefore sufficient, without the necessity to prove actual affection. The jurisprudence outlined here has not so far been expressly abandoned, but in more recent decisions, in addition to the restriction of individual interests, proof has been required from the competitor that his competitive position on the market is negatively affected by the aid.¹⁵³ So implicitly the requirements to lodge an appeal are greater than would have been necessary to justify the position of the plaintiff as participant in a formal investigation procedure – a procedure which the European Commission did not instigate. However, no specific degree of restriction (noticeable or considerable) is required for Commission decisions completed in the preliminary procedure.

151 Cf. ECJ, Judgement of 5 June 1996, Case T-398/94, Kahn Scheepart/Commission, Rec. 1996, II-477, Nos. 41 and 49.

152 Cf. ECJ, Judgement of 19 May 1993, Case C198/91, Cook/Commission, Rec. 1993, I-2487, Nos. 20ss.; ECJ, Judgement of 15 June 1993, Case C-225/91, Matra/Commission, Rec. 1993, I-3203, Nos. 14ss.

153 Cf. ECJ, Judgement of 21 March 2001, C-69/96, Hamburger Hafen- und Lagerhaus/Commission, Rec. 2001, II-1037, Nos. 41ss.

145. If an individual aid is approved after a formal investigation procedure a competitor of the recipient is to be regarded as individually affected, according to the Cofaz judgement, if he played an active part in the aid procedure, and if his market position will be noticeably restricted by the aid.¹⁵⁴ As the European Court of Justice explained in its Sniace decision of 22 November 2007, the criterion on active participation is not to be regarded as an essential condition.¹⁵⁵ Unlike situations where the decision by the European Commission that is being contested was taken during the preliminary examination, here the restriction must be shown to be “noticeable” or “considerable”. Under which conditions that can be confirmed is not entirely palpable from the jurisprudence. It is clear however that on the one side it is not enough for the enterprise to compete in some way with the recipient of the aid,¹⁵⁶ while on the other side it is enough if the aid in question would have enabled the competing recipient to survive on a market that is characterised by a very limited number of producers, fierce competition and big excess capacities.¹⁵⁷ In the Sniace judgement mentioned above the European Court of Justice agrees with the preceding instance, namely that the existence of direct competition between the enterprises is not sufficient to prove noticeable or considerable restriction of a market position, and so there is no right of appeal.¹⁵⁸

146. Legal proceedings before the Community courts brought by associations are on principle admitted to a much more liberal extent than in general German case law. Business associations can act in aid cases for the recipient and for his competitors. The scope for associations to bring an action on the grounds that their own interests are restricted is very limited.¹⁵⁹ However, according to the jurisprudence by the European courts, an association is not only empowered to bring an action if it can show that it has an interest in the case, but also if the individual enterprises in the association (or some of them) are in turn authorised to appeal and the association is acting as administrator of the individual interests of its members.¹⁶⁰ An action by an association on behalf of the recipient would appear to be a meaningful and efficient instrument, particularly if the European Commission has not forbidden an individual aid but a general aid scheme from which several members of the association would have profited. Conversely, actions by associations for competitors will mainly be brought if many of the members are affected by aid approved by the European Commission. As already shown, an association that wishes to represent the interests of its members can only bring an action if at least some of the members are themselves authorised to appeal under Art. 230, Para. 4 EC Treaty. As the jurisprudence takes a very restrictive line on actions by private plaintiffs on general aid schemes, actions by associations are also prevented by the hurdle in Art. 230, Para. 2 EC Treaty.

154 Cf. ECJ, Judgement of 28 January 1986, Case 169/84, Cofaz/Commission, Rec. 1986, 391, Nos. 24f.

155 Cf. ECJ, Judgement of 22 November 2007, Case 260/05, Sniace/Commission, No. 57, <http://curia.europa.eu/juris/cgi-bin/form.pl?lang=de>.

156 Cf. ECJ, Judgement of 22 October 1996, Case T-266/94, Skibsvaerftsforeningen/Commission, Rec. 1996, II-1399, Nos. 45ss.

157 Cf. ECJ, Judgement of 21 October 2004, Case T-36/99, Lenzing/Commission, Rec. 2004

158 Cf. ECJ, Judgement of 22 November 2007.

159 According to the jurisprudence it may be assumed that the association is affected if its position as partner in negotiations is negatively affected by the Commission decision that is contested. That is if the association has considerable rights of co-determination in the national or EU regulations on aid in question. Cf. ECJ, Judgement of 2 February 1988, Cases 67, 68 and 70/85, van der Kooy/Commission, Rec. 1988, 219, No. 15.

160 Cf. ECJ, Judgement of 10 July 1986, Case 282/85, DEFI/Commission, Rec. 1986, 2469, Note 16; cf. also Soltész, U., in: Heidenhain (ed.), loc. cit., § 45, Nos. 4ss.

147. The Monopolkommission on principle takes a positive view of the admission of actions by associations, as they can help the efficient implementation of the legislation on aid. In contrast to the jurisprudence by the European Court of Justice, actions against decisions on general aid schemes by the European Commission brought by recipients of aid, their competitors and their associations should be admitted, and in so far the restrictive Plaumann formula should not be applied. This corresponds to the standpoint put forward by the Advocate General Jacobs in his summing up in the *Aktionsgemeinschaft* case.¹⁶¹ The only proof required that a potential recipient of the aid is individually affected should be that he would have been directly entitled to benefit had the aid been approved.

148. The same applies to actions brought by competitors against a decision by the European Commission to approve aid, if it can be shown that individual aid will be granted in future on the basis of the scheme and will negatively affect the competitive position of the enterprise. In addition, the criterion of individual restriction should not be made dependent on procedural aspects but – independent of the procedural stage in which the decision by the European Commission was taken – on material restriction.¹⁶² To prove that they are individually affected in the meaning of Art. 230, Para. 4 EC Treaty competitors should not be required to show that their competitive position has actually been restricted as a result of the aid. Such proof of causality will only be possible in very few cases, and it will prevent many from bringing an action. It should be sufficient for a competitor to show substantively that he can be negatively affected by the aid. To simplify the procedure and for legal certainty individual affection should be presumed if the plaintiff can show that he is a direct competitor of the enterprise benefiting from the aid, and if the aid exceeds a certain amount to be specified, e.g. for individual aids EUR 1 million. The existence of concrete and direct competition should generally – in contrast to the view of the European Court of Justice – be regarded as sufficient.

5.4.3 Proceedings before National Courts

149. The legislation on aid envisages not only cases before Community courts, but proceedings before the national courts as well. Beside cases for recovery of the aid,¹⁶³ actions brought by competitors are particularly important. To provide legal protection for competitors on national level it must be remembered that the ban on aid in Art. 87, Para. 1 EC Treaty does not have direct effect, according to the jurisprudence by the European courts, that is, it cannot serve as grounds for appeal before national courts or be applied by them. As the grounds for exemption to this ban given in Art. 87, Para. 3 EC Treaty are very broad, the concretisation and unconditionality required to establish direct effect are lacking. The examination of whether aid is compatible with the Common Market is therefore exclusively the responsibility of the European Commission, which is in so far controlled by the European courts. However, under European jurisprudence the national courts have the task of ensuring effective legal protection against infringement of the directly applicable disposition of Art. 88, Para. 3 EC Treaty. This is intended to secure the system of preventive aid control by the European Commission and avoid competitive advantages which the beneficiary could derive from aid not granted in the envisaged way.

¹⁶¹ Cf. ECJ, Judgement of 13 December 2005, Case C-78/03 P, *Commission/Aktionsgemeinschaft*, Rec. 2005, I-10737, Nos. 138ss. (summing-up by Advocate General Jacobs).

¹⁶² Cf. Advocate General Jacobs, loc. cit. However, only the procedural aspects should be considered if the European Commission has not opened the formal investigation procedure, and the request to appeal by a third party who has not been able to claim its rights as a party involved under Art. 20, Para. 2 Procedural Reg. should be limited to obliging the European Commission to open the formal investigation procedure.

¹⁶³ See above 5.4.1.2.

150. It is generally accepted that a competitor who is affected can appeal for an injunction or for removal of the aid if there is infringement of the obligation to notify in Art. 88, Para. 3 EC Treaty and of the ban on granting aid, by bringing an action against the public donor authority (action by a competitor). He also has the alternative of sending a communication to the European Commission under Art. 20, Para. 2 Procedural Regulation, or he can combine these two methods. Should he bring an action the national courts must examine whether the aid is formally unlawful. Should that be the case the national court to which appeal has been made must, according to jurisprudence by the European Court of Justice, generally order the aid to be repaid, independently of whether it was materially legal and is later approved by the European Commission. If the aid was granted as part of an exchange agreement under civil law, according to jurisprudence by the German Federal Supreme Court the agreement as a whole must be regarded as invalid, as the ban in Art. 88, Para. 3, Sentence 3 EC Treaty has been breached.¹⁶⁴

151. In its CELF judgement of 12 February 2008 the European Court of Justice expressly stated that the national courts can if necessary order repayment of aid that is formally unlawful even if the European Commission has in the meantime taken the final decision that the aid is materially within the law and compatible with the Common Market.¹⁶⁵ This applies without prejudice to the right of the member state to grant the aid again. In addition, the national courts are obliged to impose on the recipient of the aid to pay interest on the amount for the period of illegality. As the European Court of Justice has convincingly shown, the unjustified advantage to the recipient lies firstly in the fact that he has not paid interest on the aid in question, whereas he would have had to pay interest if he had borrowed the same amount on the market until the decision by the European Commission was issued, and secondly in the improvement of his competitive position against other market participants during the period when the aid was formally unlawful. In its CELF judgement the European Court of Justice also states – without further concretisation – that the national court could also be induced to approve claims for damages suffered through the (formal) illegality of the aid.

152. The examination to be undertaken by the national courts under Art. 88, Para. 3 EC Treaty can be complex – even if it does not include the examination of material legality. Answering the question whether a measure meets all the criteria of aid in Art. 87, Para. 1 EC Treaty or if it does not need to be notified owing to a block exemption, can be difficult, involving both factual and legal problems. The national courts can, or must, apply to the European Court of Justice for a preliminary decision if there are legal doubts (Art. 234, Paras. 3 and 4 EC Treaty). In addition, the courts may consult the European Commission, question it on its usual practice in classifying a measure as aid and ask for information, like statistics, market studies and economic analyses.¹⁶⁶

153. The classification of a measure as aid by national courts could in future be made more difficult if – as the Monopolkommission advocates – the criterion of distortion to competition in Art. 87, Para. 1 EC Treaty were to be established, not generally but only with justification based on economic considerations. This could create legal uncertainty. It applies correspondingly to the decision to be made by member states on the question of obligatory notification, as under Art. 88, Para. 3 EC Treaty only those measures are to be reported to the European Commission that are aid in the meaning of Art. 87, Para. 1 EC Treaty, and as the criterion of

¹⁶⁴ Cf. BGH, Judgement of 4 April 2003, V ZR 314/02, EuZW 2003, p. 444

¹⁶⁵ Cf. ECJ, Judgement of 12 February 2008, Case C-199/06, CELF.

¹⁶⁶ Notice from the European Commission on cooperation between the Commission and the Courts of Member States on State aid, OJ EC C 312 of 23, November 1995, p. 8.

distortion of competition is regarded as a component of the concept of aid. However, this could be countered in two ways. Firstly, the low requirements for proof of distortion of competition under Art. 88, Para. 3 EC Treaty could be retained, while more proof could be required from the European Commission under Art. 87, Para. 1 EC Treaty. Secondly, and as an alternative, the concept of aid could be interpreted differently by not regarding the criterion of distortion of competition as essential to qualify a measure as aid. Consequently, only the other criteria listed in Art. 87, Para. 1 EC Treaty, and which justify supranational aid control by the European Commission, would be regarded as reasons for taking up a case, while the criterion of distortion of competition would be interpreted purely as a criterion for intervention, which only the European Commission would have to observe.

154. As well as the actions to stop and remove aid, which are intended to prevent formally unlawful aid from being disbursed or to require its repayment, competitors affected can also sue for damages. They have the possibility of claiming against the member state that has granted the aid and infringed the ban in Art. 88, Para. 3 EC Treaty, in accordance with the principles in the Francovich jurisprudence by the European Court of Justice.¹⁶⁷ In Germany the obligation to pay damages in European law is realised through a claim on official liability under § 839 Civil Code, in conjunction with Art. 34 of the Basic Law. Claims for damages can be made against the public authorities under the following conditions: (1) The regulation in European law that has been infringed is directly applicable and is designed to protect the plaintiff's subjective interests, (2) the infringement is sufficiently qualified, (3) there is a direct causal relation between the infringement and the damage suffered. Competitors will frequently succeed in providing evidence of the first two conditions.¹⁶⁸ However, competitors negatively affected by aid generally fail to make a successful claim for damages on the third condition. Proof that specifically the infringement of the ban in the EC Treaty has caused concrete damage to his enterprise is difficult to provide – without easier conditions provided in legislation.

155. It is unclear whether, if there is infringement of Art. 88, Para. 3 EC Treaty, a competitor can only bring an action against the public donor of the aid, or whether he can also claim on the private enterprise that has benefited from the aid. The clauses in civil law that apply here are §§ 8 and 9 in conjunction with § 3 Unfair Competition Law and §§ 1004, Para. 1, analogous in conjunction with 823, Para. 2 Civil Code. However, these regulations on claims for cessation, removal and damages only apply if the defendant has infringed an obligation. In some opinions this is denied on the grounds that under the wording of the provision the obligation to notify aid and the ban on granting aid in Art. 88, Para. 3 EC Treaty only apply to member states.¹⁶⁹ Others hold the view that the beneficiary should generally be regarded as a liable party as well (§§ 830, 840 Civil Code), sharing responsibility for the infringement of the ban.¹⁷⁰ In support of the latter view it can be said that a market participant who achieves an

167 Cf. ECJ, Judgement of 19 November 1991, Cases C-6/90 and C-9/90, Francovich/Italy, Rec. 1991, 5357ss.

168 The first condition is fulfilled, as the ban in Art. 88, Para. 3, Sentence 3 EC Treaty is intended to ensure before the European Commission approves aid that no competitive disadvantage will accrue to private third parties and they can exercise their procedural rights in the formal investigation procedure before the European Commission, or before the Community courts. The second condition can also be regarded as fulfilled. Infringement of Community law is sufficiently qualified if the member state clearly and considerably goes beyond the limits of its power to act. That can be assumed on infringement of the obligation to report aid and the ban on granting aid in Art. 88, Para. 3 EC Treaty, as member states have no discretionary powers in this. If it is doubtful whether a measure is aid member states must report the measure to the European Commission, which can take a binding decision.

169 Schmidt-Kötters, T., in: Heidenhain, M. (ed.), loc. cit., § 58, No. 34.

170 Cf. Tilmann, W., Schreiberbauer, M., Rechtsfolgen rechtswidriger nationaler Beihilfen, Gewerblicher Rechtsschutz und Urheberrecht 104, 2002, pp. 212-224, 222.

advantageous position in competition through the receipt of aid is the actual beneficiary of the measure that has to be reported, and that such favouring at the expense of third parties can only be justified if the prescribed procedure is observed. Hence it appears appropriate to interpret the meaning and purpose of Art. 88, Para. 3 EC Treaty as that the beneficiary is a member of the group obliged to notify, and that competitors affected can bring an action directly against him if he infringes that obligation. Accordingly, they can require the beneficiary to cease participation in the granting of unreported aid in future and repay to the public donor aid already granted. However in claims for damages against the beneficiary enterprise the problem arises that it will scarcely be possible to prove damage and causality, since, unlike antitrust law, for instance (§ 33, Para. 3, Sentences 2 to 4 Act against Restraints of Competition) the law does not offer easier conditions.

156. In view of this it is not surprising that, according to a study commissioned by the European Commission, claims for damages by private market participants are extremely rare before the courts of member states, either in the form of claims against a public authority on grounds of official liability, or in the form of cases in civil law against the benefiting enterprise. So far, not a single case is known in which the claim was successful.¹⁷¹ In regard to actions for an injunction and removal brought by private parties before national courts on grounds of infringement of Art. 88, Para. 3 EC Treaty the study differentiates between the following: (a) a private market participant wishes to defend himself against positive favouring of a competitor and (b) the plaintiff objects to an obligation laid upon him and by which other market participants are not affected (e.g. a selective environmental charge). The latter accounts for the clear majority of claims brought by competitors.¹⁷² This is probably due firstly to the fact that there can be no doubt in such cases that the plaintiff is individually affected, and secondly, the first situation probably presents a greater obstacle, as the enterprise is not directly affected and would like itself to profit from future aid. So competitors have a rational reason not to sue. Actions for injunction and removal are also very rarely brought by competitors in the European courts.

157. In the view of the Monopolkommission, legal protection on national level could be improved by enabling associations to bring actions, similar to their rights in antitrust law (§ 33, Para. 2 Act against Restraints of Competition- GWB). Incorporated associations can claim under antitrust law for injunction and removal under § 33, Para. 1 GWB to promote commercial or independent professional interests (but they cannot claim for damages), if a considerable number of their member enterprises are selling goods or services of the same or related kind on the same market, if they are capable, especially due to their staffing, material and financial situation, of fulfilling their statutory tasks in the pursuit of commercial or independent professional interests, and if the infringement will affect the interests of their members.¹⁷³ No doubt an association cannot necessarily be expected to sue enterprises in the same member state, particularly if they are its own members. But the situation is different if the beneficiary is an enterprise in a different member state and is competing with its members who cannot benefit from the – foreign – aid. An action here seems very possible. An incentive to effective private implementation of the law could be created for situations where a large number of enterprises

¹⁷¹ Study on the Enforcement of State Aid Law at National Level, March 2006, Jones Day, Lovells, Allen & Overy, http://ec.europa.eu/comm/competition/state_aid/studies_reports/studies_reports.efin, pp. 48ss.

¹⁷² Loc. cit., pp. 33ss.

¹⁷³ There is a similar model in EC Directive 98/27/EC by the European Parliament and the Council of 19 May 1998 on pleas for injunction to protect consumer interests, but it only covers actions for injunction under consumer law. OJ EC L 166 of 11 June 1998, p. 51.

are affected. This could overcome the rational disinterest on the part of the individual competitors in bringing a court action.

158. To improve efficiency and legal certainty the possibilities for legal protection on national level should be regulated as a whole and adjusted to the legislation on aid. Beside excluding the delaying effect of actions for repayment, the admission of associations and easier proof requirements for claims for damages, a special competence could be created to represent legal protection interests in aid cases. It could be regulated analogous to the legislation on public procurements.¹⁷⁴ To ensure a more uniform application of the law within the EU, minimum standards that would apply generally should also be laid down in an EU directive. The Monopolkommission recommends the European Commission to commence the preliminary work for such a package of directives, which could be oriented to the comparable project for the private implementation of Arts. 81 and 82 EC Treaty.¹⁷⁵

6. Reform Projects by the European Commission – Establishing a More Economic Approach in Aid Control

6.1 The European Commission's State Aid Action Plan

159. The objectives and substance which the European Commission is pursuing in its proposed reforms to European aid control are not identical with those it is pursuing as more economic approach in European antitrust law. In this section the European Commission's reform projects in aid are first discussed in more detail, before the characteristics of a more economic approach in aid are compared with those in antitrust law.

160. Under the Commissioner for Competition Neelie Kroes the European Commission is endeavouring to carry out comprehensive reform of European aid control, and on 7 June 2005 it published the State Aid Action Plan (SAAP).¹⁷⁶ The plan contains a roadmap for the revision of the rules on aid in secondary law.¹⁷⁷ The Community frameworks, communications and regulations that have applied so far are to be redrafted between 2005 and 2009 in the light of a more economic approach, while the primary law regulations in the EC Treaty (Arts. 87ss.) are retained. The SAAP is conceived as a consultation paper intended to stimulate political debate on reform of European aid policy. Several measures have now been taken to implement the reform concept in the SAAP.

6.1.1 The Contents of the SAAP

161. In the SAAP the European Commission names four principles that are to be pursued in reforming aid legislation:

- less and better targeted state aid
- more efficient procedures, better application of the law, greater predictability and more transparency

¹⁷⁴ See 4.3.

¹⁷⁵ Cf. most recently the White Paper "Damages Actions for breach of the EC competition rules", 2 April 2008, COM(2008) 165 final.

¹⁷⁶ European Commission State Aid Action Plan: http://ec.europa.eu/comm/competition/state_aid/reform/reform.cfm.

¹⁷⁷ In a speech to the European Committee of the German Federal Parliament on 6 July 2006 Neelie Kroes said: "We are overhauling all our rules in order to firmly ground them on rigorous economic analysis and improve the speed, transparency and predictability of their application."

- shared responsibility between the European Commission and member states and
- a refined economic approach.¹⁷⁸

6.1.1.1 Less and Better Targeted State Aid

162. The SAAP takes up the objective formulated by the European Council in the Lisbon Strategy for member states to grant less and better targeted state aid in the future.¹⁷⁹ The quantitative level of state aid is to be lowered and aid concentrated on the objectives of the Lisbon Strategy (innovation, research and development, investment in human capital and the promotion of new businesses). According to the SAAP the European Commission would like to reduce aid to a minimum that does not serve common interests of the Community. The particularly problematic rescue and restructuring aids should be avoided as far as possible. Aid given by member states should be more horizontal and in contrast to sectoral aid not limited from the start to individual sectors. Aid should be permissible particularly for cases of market failure.

On principle the Monopolkommission welcomes these objectives. However, it points out that the European Commission does not have any fiscal policy competence in aid control under Arts. 87ss. EC Treaty. The supervision of the use of resources by member states is not one of its tasks. So the European regulations on aid cannot be used directly to lower the quantitative level of aid given in member states. Reducing aid and preventing waste of (member) state funds must first and foremost be secured on national level. The focus of future aid control should rather be on ensuring less distortion to competition through aid and on better targeting aid to keep cross-border distortion of competition on the EU internal market as low as possible. In the view of the Monopolkommission such a European competition policy would indirectly lead to a welcome reduction of the volume of aid.

6.1.1.2 More Efficient Procedures, Better Application of the Law, Greater Predictability and More Transparency

163. One of the European Commission's main objectives in the planned reform is to reduce its own work load. It wants to concentrate on the more difficult cases, and for this purpose it intends to extend the area of application of the De Minimis Regulation and pass a uniform block exemption regulation. The aim of reducing the work load was also the background for the new Antitrust Procedure Regulation, in which Art. 81, Para. 3 EC Treaty, that had been

¹⁷⁸ This is the wording in the English SAAP, Item 18.

¹⁷⁹ At a special summit held in Lisbon in March 2000 the heads of state and government of the EU member states (the European Council) agreed on the Lisbon Strategy, the aim of which is to make the EU the most competitive and dynamic knowledge-based economic area in the world within ten years. Productivity and the speed of innovation are to be increased by various political measures. The Lisbon strategy is mainly concerned with innovation and the international competitiveness of the EU, and at a meeting in March 2005 the European Council made an interim assessment. As the growth gap, particularly to the United States, had widened in the past five years no concrete targets were formulated at this meeting. However, a revitalisation of the Lisbon growth targets was decided, for which each member state was to draw up its own reform programme. In its concluding remarks the European Council also discusses national state aid, urging member states to continue to lower the general level of state aid besides conducting an active competition policy. Any market failures must be taken into account. This tendency must involve a redirection of funds towards certain horizontal aims, like research and innovation and investing in human capital. Regional aid should also be reformed as agreed in the Lisbon Strategy to encourage a high level of investment and reduce the gap between regions.

interpreted as a preventive ban with the possibility of exemption, was declared a directly applicable legal exception.

6.1.1.3 Responsibility shared between the European Commission and Member States

164. In the SAAP the European Commission urges member states to endeavour to achieve greater efficiency and transparency and a better implementation of aid policy. In particular, more care in notification should be taken to shorten procedures.¹⁸⁰ The European Commission also intends to issue best practices guidelines.

165. The idea of setting up independent authorities in member states to support the European Commission in implementing aid law is also aired in the SAAP.¹⁸¹ In this the European Commission is building on experience in the last accession process, when controlling authorities in the new member states were responsible for checking state aid.

166. In the view of the Monopolkommission, as already explained, macroeconomic aid control should be carried out on national level by an independent national body.¹⁸² This body could also be required to work closely with the European Commission and support it in the implementation of the European aid rules to protect competition.

6.1.1.4 More Refined Economic Approach

167. The European Commission would also like to “refine” the economic approach in aid control in order to “ensure a proper and more transparent evaluation of the distortions to competition and trade associated with state aid measures. This approach can also help investigate the reasons why the market by itself does not deliver the desired objectives of common interest and in consequence evaluate the benefits of state aid measures in reaching these objectives. One key element in that respect is the analysis of market failures”.¹⁸³

168. So, according to the SAAP, whether granting state aid for economic policy purposes is justified is to depend in future on whether there is market failure. The possible reasons for market failure named by the European Commission are external effects, public goods, asymmetrical information, lack of coordination and market power.¹⁸⁴ But even if, as the European Commission desires, correcting market failure is to occupy a central place in future, the social, distribution policy and cultural objectives named in the EC Treaty may still justify aid.

169. In assessing compatibility on the justification level, when the positive and negative effects of aid are weighed, the European Commission intends in future to proceed according to a uniform scheme. As explained in more detail in the Community framework for state aid for research, development and innovation, a three-stage balancing test is to be carried out (cf. Table VI.2).¹⁸⁵

180 SAAP, Item 49.

181 SAAP, Item 51.

182 Cf. Item 69 in this chapter.

183 SAAP, Items 22 and 23.

184 On compensating for market failure as a possible reason for granting aid see 2.2 above.

185 OJ EU C 323 of 30 December 2006, p. 1.

Table VI.2:**The European Commission's Three-Stage Balancing Test**

Stage 1
Does the planned aid measure serve an exactly defined purposes of common interest, to remove market failure or a different aim (e.g. regional or social)?
Stage 2
Is the aid instrument likely to achieve the purpose that is in the Community interest, i.e. correct the market failure, or pursue some other aim?
a) Is state aid the appropriate means?
b) Will it have an incentive effect, i.e. will it change companies' behaviour?
c) Is the aid proportionate, i.e. could the same change in behaviour also be achieved with less aid?
Stage 3
Are the disadvantages – especially the distortions to competition and trade – limited, so that the positive consequences of the aid outweigh the negative?
How greatly aid distorts competition is to depend on
<ul style="list-style-type: none"> • the criteria by which the beneficiaries are chosen and which charges or conditions are attached to the aid, • the characteristics of the market and the beneficiaries, and • how large the aid will be and what kind of instrument it is.

Source: European Commission

170. The Monopolkommission welcomes the European Commission's intention to typify the compatibility assessment it will undertake on the justification level (Art. 87, Para. 3 EC Treaty). However, the European Commission has neglected to include in the SAAP a more in-depth economic analysis of the circumstances requiring aid (Art. 87, Para. 1 EC Treaty). Generally the European Commission only makes the cursory and general examination outlined above in such cases – and particularly when assessing any distortion to competition. This is far less than the standards that have traditionally been applied in EU antitrust law, and which the European Commission now wishes to replace with a more economic approach. A more detailed examination of the initial market structure and competition situation is, as the European Commission proposes, only to be made on justification level in Stage 3 of the balancing test. The test amounts to an examination of proportionality, in which the suitability, necessity and adequacy of a state measure are to be assessed.

171. However, before an examination of proportionality generally a more detailed examination is made of whether the case constitutes an intervention, meaning not intervention in the narrower sense, that is, intervention in a specific subjective legal position, but intervention in the form of restraint of competition on the European internal market. Only if there is such restraint is the European Commission empowered as part of its aid control under Arts. 87ss. EC

Treaty to forbid a member state from executing the measure. For, as already shown, the protection of competition on the internal market is the only purpose of the European rules on aid. The Monopolkommission regards it as generally appropriate to assume distortion to competition from certain forms of aid given by member states, and to work with assumptions on other aspects of aid. But as the criteria of selectivity and the restriction of trade between member states are interpreted very broadly, a general assumption is not justified in every case. Hence, in the view of the Monopolkommission, reform to aid legislation should start on the factual level in Art. 87, Para. 1 EC Treaty, especially regarding distortion to competition and trade between member states.

6.2 Implementing the SAAP – Examples

172. Since the SAAP was published in June 2005, a large number of measures have already been taken to implement the reform announced in it.¹⁸⁶ Moreover, the Directorate-General for Competition has also taken internal organisational measures to move towards a more economic approach. Like the Merger Task Force the State Aid department has been split up and its staff moved into the existing departments for the various industrial sectors to make use of the knowledge available there. To make the approach to reform taken by the European Commission clearer three different implementation measures will now be discussed in more detail as examples.

6.2.1 Extending the De Minimis Regulation

173. The European Commission had already announced in the State Aid Action Plan that it intended to raise the upper limit for de minimis aid, and the corresponding regulation has now been issued. Before this financial aid that did not exceed the total amount of EUR 100,000 within three years was not regarded as state aid. Under the new De Minimis Regulation this amount is raised to EUR 200,000 and credit guarantees are admitted up to an amount of EUR 1.5 million.

¹⁸⁶ They include: In services of general economic interest: Decision by the European Commission of 28 November 2005 on the application of Art. 86, Para. 2 EC Treaty to state aid granted as compensation to enterprises entrusted with the provision of certain services of general economic interest (OJ EU L 312 of 29 November 2007, p. 67) and a Community framework for state aid granted as compensation for the provision of public services (OJ EU C 297 of 29 November 2005, p. 4).

In regional aid: Commission Reg. EC 1628/2006 of 24 Oct. 2006 on the application of Arts. 87 and 88 EC Treaty to regional investment aid given by member states (block exemption regulation on regional investment aid, OJ EU L 302 of 1 Nov. 2006, p. 29) and the Guidelines for state aid for regional objectives 2007-2013 (OJ EU C 54 of 4 March 2006, p. 13). In these Guidelines the European Commission explains under which conditions it will regard aid to promote the economic development of certain disadvantaged areas within the EU as compatible with the common market under Art. 87, Para. 3 a) and c) EC Treaty. So it differentiates between investment aid to large companies, operational aid and investment aid to SMEs domiciled in these disadvantaged areas.

Other examples are: The De Minimis regulation (Commission Reg. 1998/2006 of 15 Dec. 2006 on the application of Arts. 87 and 88 EC Treaty to de minimis aids, OJ EU L 379 of 28 Dec. 2006, p. 5), the Community Guidelines on state aid to promote risk capital investment in small and medium-sized enterprises (OJ EU C 194 of 18 August 2006, p. 2), the communication from the Commission to member states to amend the communication under Art. 93, Para. 1 EC Treaty on the application of Arts. 92 and 93 EC Treaty to short-term export credit insurance (OJ EU C 325 of 22 Dec. 2005, p. 22), Community framework for state aid for research and development and innovation (OJ EU C 323 of 30 Dec. 2006, p. 1) and the Community Guidelines for state environmental protection aid (OJ EU C 82 of 1 April 2008, p. 1).

The European Commission has also put forward several proposals for future regulations, especially a draft general block exemption regulation for state aid.

174. However, the regulation only applies to “transparent” aid.¹⁸⁷ An aid is only regarded as transparent if its gross grant equivalent¹⁸⁸ can be calculated exactly in advance without requiring a risk assessment.¹⁸⁹ Such precise calculation is possible for grants, interest grants and limited tax concessions, for example, but it is not possible for capital injections by public authorities. As a consequence of this condition many municipal projects, like those in the form of a public private partnership, cannot benefit from the exemption allowed in the De Minimis Regulation. On the contrary, these projects have to be notified under Art. 88, Para. 3, Sentence 1 EC Treaty, and so they involve heavy transaction costs for the participants. But the transparency criterion has the advantage that the De Minimis Regulation is clear and easy to handle for those applying the law.

175. One possible objection to the De Minimis Regulation is that it sets an absolute threshold that applies to all branches equally. This can cause inappropriate results as the exemption applies independent of the size of the market, the position of the beneficiary on the market and the specific competition situation. Moreover, when a general threshold applies the distortion to competition that an aid might cause cannot be correctly estimated. Nevertheless, the Monopolkommission regards the use of a general threshold, below which aid in small amounts is exempt, as a meaningful way to simplify procedures; it increases legal certainty and allows to avoid bureaucracy costs. This eases the work load on the European Commission and enables it to concentrate on difficult cases, where considerable distortion to competition may ensue. However, the new threshold of EUR 200,000 is still very low.

176. The Monopolkommission holds the view that easier exemption conditions should also be introduced for higher volumes of aid. Power to intervene could be granted to the European Commission for aid of an amount to be specified – it could be EUR 1 million.¹⁹⁰ For aid below that threshold it could arguably be assumed that there is no noticeable distortion to competition under Art. 87, Para. 1 EC Treaty. However, this assumption should only apply if the aid is also tied to particular activities, if the intensity¹⁹¹ is relatively low (not more than 30%) and the grant is given in an open and transparent procedure.¹⁹²

6.2.2 Draft of a General Block Exemption Regulation

177. In order to reduce the number of aids requiring notification the European Commission is also increasingly using block exemption regulations. These are directly applicable rules and their correct use can be examined before the national courts – for instance in cases brought by a competitor of the beneficiary. The European Commission announced in the SAAP that the former block exemption regulations would be consolidated, replaced by a uniform regulation on block exemption, and extended to include more areas. It has now published the draft of a general block exemption regulation,¹⁹³ which provides for the possibility of exemption for almost every economic sector and, if it is implemented, will cover a wide range of aid cases. In

¹⁸⁷ Art. 2, Para. 4 De Minimis Regulation.

¹⁸⁸ The grant equivalent or the cash value of promotion shows the economic benefit of the measure. It is frequently given in percent of the total project costs (that can be taken into account). The gross grant equivalent differs from the net grant equivalent in that the tax payable on the promotional funds is not taken into account.

¹⁸⁹ Cf. Preamble 12 of the De Minimis Reg.

¹⁹⁰ See 1015ss. above.

¹⁹¹ Aid intensity is the share of the promotion in the total expenditure on the project.

¹⁹² See 1106ss. Below.

¹⁹³ Request for comment on the draft general block exemption regulation for state aid, OJ EU C 210 of 8 September 2007, p. 14.

future member states would no longer be obliged to report to the European Commission aid that is covered by this regulation and meets its requirements, nor would they have to wait for the Commission's approval before granting the aid. They could put their aid measures into practice without delay.

178. The five block exemption regulations issued so far (for aid to small and medium-size enterprises or SMEs,¹⁹⁴ for research and development by SMEs, employment, training and regional promotion) are to be integrated in the general block exemption regulation, which is also to include new groups of aid: environmental protection, risk capital, and research and development aid for large companies.

179. The maximum permissible intensities of aid for the various groups and the eligible costs are defined in more detail in the draft. With the level of permissible aid intensity as the share a member state may contribute to the (recognised) total costs of a project the European Commission shows how high it sets the risk of distortion to competition in each category of aid, and the expected benefit of the aid to the general community. The greater the aid intensity, the less restraint of competition is feared. Fixing the intensity of the aid thus involves weighing – albeit generally and roughly – the positive and negative effects of the aid. According to the draft regulation, for general training measures, for example, in which transferable qualifications are acquired, a higher intensity is permitted (65%) than for specific training measures that will primarily benefit the company providing the training (35%). Moreover, in several places the draft envisages favourable treatment for SMEs.¹⁹⁵ If an aid meets the conditions named in the draft and does not exceed the intensity specified for its group it is to be assumed compatible with the common market. Beside these conditions for assumption the draft also contains conditions that set higher requirements for those applying the law. For aids to large companies, for example, it must be shown positively that the aid will have an incentive effect. That will not be the case if the recipient would carry out the project to be promoted under market conditions, also without the aid.

180. An incentive effect is assumed for aid to SMEs if the company concerned applies for aid to the member state before starting to implement the project or embark on the activity to be promoted (Art. 8, Para. 2 of the draft regulation). In the case of aid to large companies the member state must check (Art. 8, Para. 3 of the draft) whether the recipient has analysed the viability of the project or the activities to be promoted with and without the aid in an internal

194 SMEs are defined as follows in Annex 1 of Commission Regulation (EC) 70/2001 of 12 January 2001 on the application of Articles 87 and 88 EC Treaty to state aid to small and medium-sized enterprises, OJ EU L 10 of 13 January 2001, p. 33:

SMEs are enterprises that employ fewer than 250 persons and have an annual turnover of at most EUR 40 million or an annual balance sheet total at most EUR 27 million and which meet the criterion of independence defined in Para. 3. Should it be necessary to distinguish between small and medium-sized enterprises, a small enterprise is one which employs fewer than 50 persons and has an annual turnover of at most 7 million or an annual balance sheet total of at most EUR 5 million and which meets the criterion of independence defined in Para. 3.

195 For instance, under the draft regulation investment and employment aids, aid for early adjustment to future Community norms and aids for the use of consultancy services are only to be exempt if granted to SMEs. For groups of aid in which on principle large companies could also profit from the exemption, higher intensity figures are envisaged for SMEs. Finally, easier conditions of proof are to apply for SMEs (Art. 8, Para. 2 draft reg.). The European Commission classifies SMEs as particularly deserving of promotion, as they play a decisive role in creating jobs and are one of the pillars of social stability and economic dynamic. So the European Commission expects positive external effects to come from promoting SMEs. It also assumes that SMEs are typically disadvantaged owing to market failure. They often have difficulty in raising risk capital or loans, owing to the unwillingness to bear these risks frequently found on certain financial markets and because SMEs can offer less security.

paper. The recipient company must carry out this analysis *ex ante* using quantitative and qualitative indicators. The member state must check the analysis and include it in the records.

181. The Monopolkommission regards it as positive that the former block exemption regulations on aid are to be grouped into a single regulation to improve transparency and legal certainty. In the view of the Monopolkommission block exemption regulations can make an important contribution to simplifying procedures. However, they can only fulfil that purpose if the conditions for exemption are formulated clearly and implementing them is not complicated. Providing the positive proof of the incentive effect envisaged in the draft for aid to large companies, on the other hand, will be costly and time-consuming. Large companies will certainly draw up a business plan before applying for aid, and for this they will already have made a detailed analysis, weighing one alternative against another. However, the requirement for authorities in the member state to check the analysis in detail will involve considerable bureaucratic expenditure and it hardly seems efficient, as the office granting the aid is responsible for control. So in the view of the Monopolkommission the proposed provision should not be included in a directly applicable block exemption regulation.

6.2.3 *The Community Framework for Research, Development and Innovation*

182. The Community framework for research, development and innovation (R&D&I) of 22 November 2006 can be taken as a typical example of how the European Commission envisages to realise the aims specified in the SAAP, especially the more economic approach. Unlike the previous regulation it includes innovation projects as well as research and development. This Community framework only applies to those aid measures that are not already exempt from the notification requirement in Art. 88, Para. 3, Sentence 1 EC Treaty under the De Minimis regulation or a block exemption. In the R&D&I framework the European Commission also touches upon the question of the model for European aid control.¹⁹⁶ The legitimate aim of R&D&I aids is economic efficiency. Without explaining why the main concern here is not consumers' welfare, as it is in the other areas of competition policy, the European Commission mentions the general welfare as the determinant model only in passing.

183. In the R&D&I Community framework the European Commission envisages two test procedures of differing intensity: firstly, a faster procedure in which legal assumptions will also play a part, then a very elaborate test procedure, in which concrete application of the three-stage balancing test will be made adjusted to the R&D&I field. A detailed assessment is to be undertaken if the aid exceeds certain upper limits laid down in Chapter 7 of the Community framework. These thresholds will differ depending on the kind of aid and the activity promoted.¹⁹⁷ The framework also contains special instructions for appraising the incentive effect.

¹⁹⁶ Fig. 1.1, Para. 3 of the Community framework states "The objective is through State aid to enhance economic efficiency (Footnote 3) and thereby, contribute to sustainable growth and jobs. Therefore, State aid for R&D&I shall be compatible if the aid can be expected to lead to additional R&D&I and if the distortion of competition is not considered to be contrary to the common interest, which the Commission equates for the purposes of this framework with economic efficiency. The aim of this framework is to ensure this objective and in particular to make it easier for Member States to better target the aid to the relevant market failures." Footnote 3 adds to this: "In economics, the term 'efficiency' (or 'economic efficiency') refers to the extent to which total welfare is optimised in a particular market or in the economy at large. Additional R&D&I increases economic efficiency by shifting market demand towards new or improved products, processes or services, which is equivalent to a decrease in the quality adjusted price of these goods."

¹⁹⁷ According to 7.1 of the R&D&I Community framework the following thresholds will be determinant:

- in case of project aid and feasibility studies
- for projects mainly in basic research: EUR 20 million per enterprise and project/feasibility study;
- for projects chiefly in industrial research EUR 10 million per company and project/feasibility study;

184. In Chapter 5 of the R&D&I Community framework the European Commission first defines various categories of aid for which it sets concrete conditions and the permissible aid intensity.¹⁹⁸ The further from the market the promoted activity is the higher may the state aid's share in the project be (100% in basic research, 50% in industrial research and 25% in experimental research). These limits are based on the correct assumption that harmful distortion to competition on product markets is more likely the more the planned investment is concerned with developing new or changing products or processes.

185. In Chapter 6 of the R&D&I Community framework the European Commission then discusses the criterion of the incentive effect, which it regards as of crucial importance. For certain types of aid, namely project aid for large companies, project aid for SMEs above EUR 7.5 million, aid for process and organisational innovation in the services sector and aid for innovation clusters the member state notifying the aid must provide concrete proof of the incentive effect. In such cases, and regardless of whether the threshold named in Chapter 7 for that specific activity has been exceeded or not, the member states must present to the European Commission an ex ante assessment of the increased R&D&I activity, based on a comparison of the situation without the aid with the situation after it was granted. As possible indicators the European Commission names increase in the size of the project, increase in its range, acceleration of the process and increase in total expenditure on R&D&I.¹⁹⁹

186. If the aid fulfils the criteria in Chapter 5, does not exceed the threshold for the promoted activity laid down in Chapter 7²⁰⁰ and the incentive effect can be shown in accordance with the procedure described in Chapter 6, no further examination will be made. It will be assumed that the three-stage balancing test would yield a positive result. As the European Commission thus relies on thresholds and not on market shares, for instance, the assumption will be made independently of the size of the market and the market position of the beneficiary.

187. If the threshold laid down for that activity is exceeded the three-stage balancing test is to be carried out for the individual case and in accordance with the procedure described in more detail in Chapter 7.

In Stage 1 the member state must first prove a justified common interest. Under the R&D&I Community framework aid can only be justified if the aim is to remove market failure.²⁰¹ Other social or distribution policy aims are not accepted by the European Commission as areas to which the framework applies. It holds the view that the forms of market failure con-

- for all other projects: EUR 7.5 million per enterprise and project/feasibility study;
- for process or organisational innovation in the services sector: EUR 5 million per enterprise and project;
- for innovation clusters: EUR 5 million per cluster.

198 Aid intensity is the level of gross aid expressed in percent of the eligible costs of the project. All the amounts entered are amounts before tax or other charges. If aid is not given in the form of a grant the level of the aid will be determined by its grant equivalent (Fig. 2.2 c) R& D&I Community Framework).

199 If the threshold named in Ch. 7 has not been exceeded the European Commission would like to assume as a general rule that the planned aid will have an incentive effect, if significant changes can be shown in at least one of these factors, taking into account normal behaviour in the sector in question. Otherwise more stringent proof requirements apply.

200 The criteria include

- project aid and feasibility studies for which the aid is given to an SME and the amount per SME and project is below EUR 7.5 million (project aid plus aid for the feasibility study),
- aid for the cost of commercial patents to be borne by SMEs,
- aid for young innovative enterprises,
- aid for innovation consultancy and for services in support of innovation, and
- aid to lease highly skilled personnel.

201 Cf. 1.3.2 RDI Community framework.

ceivable in the field of research, development and innovation are knowledge spillover, imperfect and asymmetrical information and lack of coordination and networking. It is not enough to claim that these are evident, the member state must provide proof of why there is a specific market failure in a particular case.

In Stage 2 then the European Commission is to examine whether the aid is an appropriate instrument, if there is an incentive effect and if the aid is proportionate. A measure is regarded as an appropriate instrument if the member state has considered other measures and estimated their consequences, and has (demonstrably) reached the conclusion that granting an aid with selective effect will have advantages. In this context the European Commission allows member states scope for estimates. But for the incentive effect it requires definite proof. This involves extremely complex and expensive analysis, which goes beyond the requirements named in Chapter 6. Calculating the incentive effect is, according to statements by the European Commission, the most important condition for the analysis of a state R&D&I aid in the balancing test.²⁰² By contrast, for its examination of proportionality the European Commission only requires member states to provide concrete evidence of in how far an open selection procedure has been held and whether the aid will exceed the stipulated minimum amount.

Finally, in Stage 3 of the test possible distortion to competition and trade are analysed and weighed against the positive effects of the aid (removal of the market failure). As distortion to competition that can be caused by an R&D&I aid the European Commission names: Reducing the dynamic innovation incentives for competitors by stronger presence of the favoured enterprise on the product markets (displacement effect); in this context the European Commission wishes to take into account the amount of the aid,²⁰³ the market proximity/type of aid,²⁰⁴ the method of granting the aid,²⁰⁵ any possible barriers to exit,²⁰⁶ the competition incentives for a future market,²⁰⁷ the product differentiation and the intensity of competition.²⁰⁸

- Creating or maintaining market power; the European Commission announces that the level of entry barriers,²⁰⁹ the buyer power²¹⁰ and the selection process will be incorporated in its examination.²¹¹ It explains that it is unlikely that competitive concerns due to market power

202 Cf. 7.3.3 RDI Community framework.

203 In the view of the European Commission considerable displacement effects are more likely from particularly large amounts of aid (measured by total private R&D expenditure in the sector concerned).

204 With increasing market proximity of R&D activity promoted by state aid the likelihood of considerable displacement effects grows, according to estimates by the European Commission.

205 Aid granted on the basis of objective criteria is assessed more positively by the European Commission.

206 The European Commission argues that competitors will be more inclined to maintain their investment, or even increase it, if the barriers to abandoning the innovation process are high. That can be the case if much of the earlier investment expenditure by the competitor is tied into a particular RDI technology.

207 In the view of the European Commission RDI aids can induce competitors of the beneficiary to decide not to compete on a future market, as the advantages brought by the aid (in degree of technical advance or time advantage) make it less profitable for him to enter the market.

208 If the product innovation is directed to developing more differentiated products (e.g. in relation to certain trademarks, norms, techniques or consumer groups) competitors will generally be less strongly affected, in the view of the European Commission. The same applies when many effective competitors are active on the market.

209 The European Commission explains that the barriers to access for newcomers in the RDI field can be high. Here it includes legal barriers (especially intellectual property rights), size and association advantages, barriers to access to networks and infrastructures and other strategic barriers to market access or growth.

210 The market power of a company can be limited by the market position of its customers, according to the European Commission. The presence of big customers can mean that a strong market position is of less importance if it can be assumed that the customers will try to ensure that there is sufficient competition in the market.

211 In the view of the European Commission aid is questionable if it enables companies with a strong market

will arise on a market on which every beneficiary has a share of less than 25% and the market concentration is below an HHI of 2000.²¹²

- Maintaining inefficient market structures; the European Commission wishes to examine whether the aid is being granted on markets with excess capacities, for shrinking economic sectors or in sensitive sectors.

188. It is to be welcomed that the European Commission has expressly typified the distortions of competition that R&D&I aid can cause and expressly named the criteria for assessment in a Community framework. The examination of the negative effects in Stage 3 of the test requires a detailed analysis of the competition on the basis of a concrete definition of the materially and geographically relevant market. In this competition analysis the European Commission studies various market characteristics (the position of the beneficiary company in the relevant market, the level of market shares and market concentration, barriers to market entry, the degree of product differentiation and excess capacities on the market) and the characteristics of the aid (the method of granting it,²¹³ the amount, the type of aid and the market proximity of the activity promoted).

189. In view of the fact that the justification in Art. 87, Para. 3 EC Treaty is very broadly formulated the Monopolkommission regards it as positive that the European Commission intends to concretise the procedure for its examination in more detail and adjust it to the particular features of R&D&I aid. This will increase the transparency and economic foundation of the European Commission's decisions on aid in the R&D&I field over earlier practice. A critical view can be taken of the fact that in its examination of compatibility in Stage 3 of the balancing test the European Commission does not examine the competition situation on the factual level (Art. 87, Para. 1 EC Treaty) but only on the justification level. In contrast to the concept followed by the European Commission and current practice, the cross-border distortion of competition should be established on the factual level with well-founded economic data, before the European Commission examines in its compatibility test the suitability and necessity of an aid for the economic and distribution policy aims it is intended to serve.

190. In the view of the Monopolkommission criticism can also be levelled at the fact that the European Commission accords the incentive effect a central position compared with the other points examined, describing it as the most important condition in its balancing test.²¹⁴ In the view of the Monopolkommission this criterion should not be overvalued compared with other issues in the test, nor should such elaborate and complex proof be required as is envisaged in Chapter 7 of the R&D&I Community framework. Although aid should on principle only be given if it creates an incentive to change behaviour, as otherwise windfall gains will ensue, in regard to competition simply the non-existence of an incentive effect is not proof of restraint of competition. If the aid does not change behaviour in relation to the project promoted that means that without the aid the beneficiary enterprise would not have made any other price or quantity decisions on the markets in question, and in so far would not have caused any distortion of competition. Admittedly, conversely it cannot be concluded from the lack of an incen-

position to influence the selection process, e.g. if they have the right to recommend companies in the selection process or can influence the research path in such a way that alternative paths are unjustifiably disadvantaged.

212 HHI is the abbreviation for Herfindahl-Hirschmann Index, which describes the sum of squared market shares of companies on the market in question.

213 Aid granted as part of a broad aid programme or in an open selection procedure is *ceteris paribus* less distorting than targeted ad hoc measures for individual firms.

214 Cf. 7.3.3 R&D&I Community framework.

tive effect that there is no distortion of competition, as an enterprise can in the long term view use the resources made available to it through the aid, and which improve his operating result, to achieve a competitive advantage – on neighbouring markets, for instance. But the incentive effect is not a suitable a criterion for the balancing test which the European Commission conducts to protect cross-frontier competition.

191. If the functioning of a certain market is seriously restricted undistorted competition will not produce efficient allocative results. However, in its compatibility examination the European Commission should look more closely at in how far the market failure in question can be specifically and effectively removed by the aid, and whether milder means are clearly available that will be less distorting of competition. For even if there is market failure this does not automatically mean that the situation can be improved by state intervention. There is, rather, a risk that aid will fail to have the desired effect owing to erroneous estimates by the state, and that the competition will be changed for the worse. The European Commission should therefore also examine whether there are several market failures and the competition situation is likely to be worsened by the state intervention (second best problem) – if only one market failure is being targeted with the aid.

6.3 The Characteristics of the More Economic Approach in Aid Control

6.3.1 The Origins of the More Economic Approach in EU Competition Law

192. In introducing a more economic approach the European Commission was initially only aiming gradually to change the focus of its competition regulations on companies (antitrust law).²¹⁵ This is the origin of the new reform approach by the European Commission, which operates on several levels and issues:

- what the main aim and model should be,
- how to typify law, respectively guidelines (soft law/policy), and
- what economic knowledge and methods should form the basis of individual decisions.

So the concept of the more economic approach is complex and its realisation in competition law is conceivable in various forms. There is no generally valid definition. In this chapter the approach pursued specifically by the European Commission as a more economic approach will be characterised in greater detail. The aims pursued by the European Commission in anti-trust law can be summarised as follows:

- Directing the competition rules to protecting consumer welfare
- The importance of the effects of the behaviour or transactions in question on the market outcome (effects-based approach)
- Carrying out a comprehensive analysis of difficult individual cases (instead of undifferentiated per-se rules)
- Admission of the efficiency objection throughout, and
- The use of new economic models, knowledge and quantitative methods.

193. The more economic approach which the European Commission wishes to adopt in anti-trust law is the subject of numerous scientific studies and controversial discussions. The Monopolkommission will not enter into these arguments in this chapter, instead it will assess the opportunities and risks of applying a more economic approach in aid control. However, in order to clarify the common factors and differences between the more economic approach de-

²¹⁵ The term “antitrust law” is used in this chapter in a broad sense and also covers abuse and merger control.

sired by the European Commission in antitrust law on the one side and aid control on the other, the characteristics of the two reform concepts will be compared.

6.3.2 *Characteristics of the More Economic approach desired by the European Commission in State Aid Control compared with that in Antitrust Law*

6.3.2.1 *The Model*

Antitrust Law

194. Securing a competitive market structure and protecting the freedom of competition are the traditional aims of German competition law, which for decades has also influenced European competition law. According to this model competition as such is in itself a good worth protecting. This interpretation, formed by *ordo-liberal* ideas, is based on the assumption that protecting competition will in the long term and indirectly also benefit the end-user, and it is based on whether the behaviour in question entails restriction of action by competitors and market participants on up- or downstream market stages. In this approach securing freedom has independent weight. It has two aspects, firstly, protection of individual freedom of economic action, and secondly, protection of the market economy order in civil law from the dangers that can ensue if interest groups try to obtain privileges through the political process.

195. In adopting a more economic approach the European Commission would like to establish a model in EU antitrust law in which economic results will be of particular importance. The efficiency of the market results are to form the main parameter. It must be stressed that models are not descriptive but normative. As the European Commission is clearly not aiming to change the bases in primary law through the European legislature it must orient the discussion it is conducting over the model to the existing legislation and its requirements. Hence the discussion can at most aim for a different interpretation of the existing regulations and features of the law (such as restraints of competition in Art. 81, Para. 1 EC Treaty), whereby the European courts will take the final and binding decision on these interpretations. The European Commission intends to put the main focus on the protection of consumers (consumer welfare standard). Competition is thus not to be protected for its own sake or as an institution, it is to be used as a means of achieving that objective.²¹⁶

196. Establishing a standard of consumer welfare is not uncontroversial. Some authors, like the European Commission, are in favour of a more economic approach in which efficiency would be the model for competition policy. Nevertheless, they are not in favour of a consumer welfare standard, preferring a total welfare standard, which beside the benefit to the consumer would also include the advantages to producers.²¹⁷

216 In a speech at the 13th International Conference on Antitrust Law on 27 March 2007 in Munich, “Consumer Welfare and Efficiency – New Guiding Principles of Competition Policy?” Director-General Philip Lowe commented on the model question as follows: “Ladies and Gentlemen, my overall message is short and simple. Yes, consumer welfare and efficiency are the new guiding principles of EU competition policy. Whilst the competitive process is important as an instrument, and whilst in many instances the distortion of the process leads to consumer harm, its protection is not an aim in itself. The ultimate aim is the protection of consumer welfare, as an outcome of the competitive process. And believe me that as head of the competition authority charged with protecting consumer welfare, I am at least as concerned about false negatives, i.e. under-enforcement, as I am about false positives, i.e. over-enforcement. I am therefore committed to make the new rules work in practice.” http://ec.europa.eu/competition/speeches/text/sp2007_02_en.pdf.

217 Cf. Schmidchen: Der “more economic approach” in der Wettbewerbspolitik, *Wirtschaft und Wettbewerb* 56, 2006, pp. 6-17, 6s.

197. In explanation of the European Commission's decision not, as is usual in economics, to make the total welfare standard its model but the consumer welfare standard, it is pointed out that in the relation between the competition authority and the enterprise notifying aid there is asymmetry of information, moreover consumers lack the possibility and incentive to lobby which financially strong companies have.²¹⁸ Hence asymmetry must deliberately be introduced, and the competition authorities need to take more account of the benefit to consumers than of the profits to producers. The fact that this approach is easier to handle in industrial economics and analytical studies may have helped to make it more widely used. The new accentuation by the European Commission was probably also largely influenced by competition practice in the United States, where the consumer welfare standard has long been the basic model.²¹⁹

198. The European Court of Justice, which is responsible in the final instance for interpreting the European legislation, commented on the question of the determinant purpose of protection, and the model to be used, in its judgement on the British Airways case of 15 March 2007. It pointed out that Art. 82 EC Treaty does not only refer to behaviour that can directly harm consumers but also to behaviour that can cause them harm through intervention in the structure of existing competition, as referred to in Art. 3, Para. 1 g) EC Treaty.²²⁰ So the ECJ is not against the protection of consumers as an aim of competition law, indeed, it expressly acknowledges that aim by stating that Art. 82 EC Treaty not only refers to behaviour that can be directly disadvantageous to consumers. Nevertheless it stresses that intervention in the structure can be sufficient to establish infringement of competition. So it follows the traditional structure-oriented approach, which is still the determinant approach in German competition law. Hence direct harm to consumers' interests is not an essential condition for intervention under European competition law, and the ECJ is not in favour of exclusive use of the consumer welfare standard.

State Aid Law

199. The State Aid Action Plan does not contain any information on the question of which model is determinant in EU aid control. As already shown, in discussing the question of the model the existing legal framework conditions in the EC Treaty must be observed. In the new R&D&I Community framework the European Commission mentions casually that in European aid control – unlike other areas of competition policy – it is not consumer welfare but the total welfare standard that should be determinant, as beside the benefit to consumers it also includes the benefit to producers.

218 Cf. Röller, L.-H., Neven, D.J., Consumer Surplus vs. Welfare Standard in a Political Economy, Model of Merger Control, *International Journal of Industrial Organization* 23, 2005, pp. 829-848; Heidhues, P., Lagerlöf, J., On the Desirability of an Efficiency Defense in Merger Control, *International Journal of Industrial Organization* 23, 2005, pp. 803-827.

219 Some economists are against using economic efficiency in the sense of the welfare approach and instead want freedom of competition to be the model. However, they also want to see the effects for consumers used as the main criterion for the application of competition rules. Promoting the freedom of one market participant always means restricting the freedom of another. The freedom of entrepreneurial decision for companies with a strong market position should accordingly also be protected, and must be weighed against the freedom of competition for each competitor or the opposite market side. Consumer interests are accordingly a suitable indicator of whose freedom of competition deserves greater protection in any individual case. Cf. Hellwig, M., Effizienz oder Wettbewerbsfreiheit, *Zur normativen Grundlegung der Wettbewerbspolitik*, Preprint 2006/20, Max-Planck-Institut zur Erforschung von Gemeinschaftsgütern, Bonn, August 2006, pp. 2ss. http://www.coll.mpg.de/pdf_dat/2006_20online/pdf.

220 ECJ, Judgement of 15 March 2007, Case C-95/04, No. 106.

200. The Chief Economists' Team at the Directorate-General for Competition suggested in a study that in the field of aid a standard of consumer welfare should be used, but one in which – unlike EU antitrust law – the interests of taxpayers would also be taken into account.²²¹ In a further study commissioned by the European Commission as part of its planned aid reform, the authors argue that both the interests of consumers and the interests of competitors in making a profit should be taken into account.²²²

201. Independent of how one sees the new model used by the European Commission in European antitrust law, a pure and exclusive consumer welfare standard should not be used in aid control. A simple transfer of this approach, in which the direct effects for consumers on the product markets in question is the main criterion, would entail the risk of an inaccurate and over-positive assessment of aids. In the short-term view aids can initially result in lower prices. That will certainly be the case if the aid granted leads to a reduction in variable costs or the entry to the market of other companies. At first sight allocative gains in welfare could generally be expected on the relevant product markets.²²³

202. However, that would be to ignore the fact that aid – which would have to be financed through taxation, which in turn causes welfare losses – can in the medium and long term lead to restraint of competition, which will result in over-pricing and ultimately leave consumers worse off. Aid to established companies can frighten efficient newcomers away from the market. Moreover, inefficient firms can acquire market shares at the expense of more efficient firms that have not received promotional funding. Moreover, aid can become a habit of mind and reduce cost pressure (soft budget constraint), leading to inefficient production. For companies have less incentive to produce efficiently and to invest if they can assume that the state will come to their assistance if they find themselves in financial straits (for instance to preserve jobs). Moreover, continuous aid can cause distortion in the economy as a whole, as it permanently changes price relations and causes misallocation of resources. The Monopolkommission therefore welcomes the fact that the European Commission evidently does not intend to establish a consumer welfare standard in aid control in the form which it approves in anti-trust law.²²⁴

203. As already shown, under Art. 87, Paras. 1 and 2 and Art. 3, Para. 1 g) EC Treaty the protection of competition on the European internal market is the determinant aim of European aid control. The European Commission does not have fiscal policy competence under Arts. 87ss. EC Treaty. Hence in aid control it should concentrate on preventing negative effects of aid on cross-border competition on the European internal market, in keeping with its statutory obligation, or reducing these to the unavoidable level. To assess whether an aid is causing restraint of competition the short-term price trend on the relevant product markets, which consumers see as a result of the aid, should be one of several factors to be taken into account. To

221 Cf. Friederiszick, H.W., Röller, L.-H., Verouden, V., loc. cit, pp. 39ss.

222 Cf. Nitsche, R., Heidhues, P., Study on methods to analyse the impact of State aid on competition, European Economy, Economic Papers No. 244, February 2006, pp. 5ss. http://ec.europa.eu/economy_finance/publications/economic_papers/2006/economicpaper244/en/htm.

223 That is, unless perfect competition is assumed, which is unrealistic.

224 In an experts discussion between members of the Monopolkommission and representatives of the General-Directorate on Competition on 10 April 2008 in Bonn the latter confirmed that the European Commission does not intend to adopt the consumer welfare standard applied in antitrust law in aid law. “Even leaving equity considerations aside, State aid assessment focuses on the effect of the aid on rivals and on the competitive process rather than measuring the direct effect on consumers. Such a focus is justified by the fact that if efficient rivals are weakened by aid measures, effective competition may be hindered with the result that allocative efficiency is reduced in the long run.”

what extent the aid is likely to have negative effects on the other market participants – on the same market stage, upstream and downstream and on neighbouring markets – and to intervene across frontiers in the functioning of markets is also of considerable importance.

6.3.2.2 *The Effects-Based Approach*

Antitrust Law

204. In its introduction of the consumer welfare standard as model the European Commission is reorienting European competition law to the more economic approach in antitrust law. Its aim is to establish an effects-based approach in contrast to the traditional structure-oriented or form-based approach.²²⁵ The main concern of the form-based approach is to secure a competition structure that functions, and risk in the abstract is enough to justify intervention by the competition authorities. It is generally easier to prove infringement in regard to structural features than if the effects-based approach is used, where the concrete effects of a measure are determinant. To justify a ban in the effects-based approach more information must be used than hitherto in critical individual cases.

205. The effects-based approach is evident in the formulation of recent secondary law and in the guidelines in which the European Commission explains the basic principles of its own application of the law and in so far binds itself (soft law).²²⁶ The European Commission intends the effects-based approach to play a major role in practice in individual cases. Hence the effects on the market result are to be examined comprehensively in difficult cases, using industrial economics models and quantitative analyses. In accordance with the consumer welfare standard the determinant factor is to be whether the effect could be of advantage to consumers, whereby the actual and probable effects are to be considered.²²⁷ So in assessing a merger, for instance, what matters is how prices are expected to develop following the merger. Changes in market structures or the form of competition are to be important in so far as they enable statements to be made on the consequences for consumers.²²⁸

State Aid Law

206. Neither the State Aid Action Plan nor the implementation measures taken to date provide for the European Commission to examine the economic effects on competition more closely on the factual level, i.e. Art. 87, Para. 1 EC Treaty. In practice so far, only a general economic examination has been made in regard to cross-frontier trade and distortion to competition under Art. 87, Para. 1 EC Treaty, without a more precise delineation of the market. This practice is not being changed. In the past it has also been supported by the European courts. Hence the economic proof required of the European Commission by the courts in aid law differs fundamentally from the requirements set by the ban in the antitrust rules, Art. 81 and 82 EC Treaty and Art. 2, Para. 3 of the Merger Control Regulation.

²²⁵ Cf. Albers, M. (member of DG Competition), *Der more economic approach bei Verdrängungsmissbräuchen: Zum Stand der Überlegungen der Europäischen Kommission*, pp. 2s.; <http://ec.europa.eu/comm/competition/antitrust/art82/index.html>.

²²⁶ One example is in the Guidelines on the assessment of horizontal mergers (OJ EU C 31 of 5 February 2004, p. 5), and the comments on non-coordinated effects (unilateral effects) in Nos. 24ss.

²²⁷ Cf. Albers, M., *loc. cit.*, p. 2.

²²⁸ Cf. European Commission, Guidelines on vertical restraints, OJ EU C 291 of 13 October 2000, p. 1, here § 3, No. 7; Guidelines on the assessment of horizontal mergers, *loc. cit.*, Nos. 8s. and DG Competition discussion paper on the application of Article 82 of the Treaty to exclusionary abuses, December 2005, No. 4, <http://ec.europa.eu/comm/competition/antitrust/art82/index.html>.

207. Accordingly, in future, too, in order to prove restraint of cross-frontier competition and trade by state aid (Art. 87, Para. 1 EC Treaty) the European Commission need neither take due account of the requirements of the effects-based approach, which it is now applying in antitrust law, nor meet the requirements that have traditionally been determinant in antitrust law under the form-based approach.

208. A study of the market situation and the effects of state aid on competition is only to be made as part of the examination of compatibility under Art. 87, Para. 3 EC Treaty, to be more precise on Stage 3 of the balancing test outlined above. In many cases, however, this test will never be made. For if an aid does not pass one of the preceding stages of the balancing test – because it is either not intended to remove a market failure (Stage 1) or not suitable or necessary for this (Stage 2) – the test will be stopped. Accordingly in future, too, cases will be conceivable in which the European Commission forbids an aid without examining its negative effects on competition in the EU internal market. That would appear to be problematic, as the European Commission is only legitimised to exercise aid control following the protective goals of Arts. 87ss. EC Treaty, if competition in the European internal market would be restricted by the aid.

6.3.2.3 Individual Case Analysis instead of Per Se Rules

Antitrust law

209. The European Commission intends in future to examine the effects of aid on the market in especially critical individual cases. This will form part of an exact and complex individual case analysis, which should enable the European Commission to take economically efficient decisions. So in such cases it will not rely on generalising risk factors and applying per-se rules. It is characteristic of the latter that behaviour or restriction of action defined in concrete terms are classified per se as either impermissible or permissible under competition law. Per-se rules have the advantage that the outcome of the procedure is generally easier to forecast for those involved, and this can increase legal certainty. However, the European Commission does not intend generally to cease to rely on assumptions and per se rules in future, an exact and elaborate consideration will only be made of difficult cases. In merger control, for instance, a low number of competition cases will be affected. The European Commission is also aiming to revise the per-se rules used to date and formulate more differentiated economic rules.

State Aid Law

210. The European Commission is not pursuing the aim of ceasing altogether to use per-se rules and assumptions in future European aid control, either. Rather, as already shown, in its reform it has increased the area of application of the De Minimis Regulation and raised the upper limit for exempt aid. The rules in this regulation are clear and easy to handle. Moreover, the European Commission has also proposed a general block exemption that should free more aid than hitherto from obligatory notification and create a uniform legal framework.

211. Should an aid meet neither the requirements of the De Minimis Regulation nor a block exemption regulation it must be notified under Art. 88, Para.3, Sentence 1 EC Treaty and it will be examined by the European Commission. The principles of this balancing test are concretised in guidelines and Community frameworks. It is typical of the guidelines published since the reform that they provide for two different kinds of procedure – firstly a faster proce-

procedure, in which legal assumptions are also used, and a more detailed procedure for difficult cases and large projects, in which an exact economic analysis is to be made, using the balancing test outlined above. As the first cases where the new R&D&I framework was used show, this involves an examination that is much more complex and elaborate than the test used so far on compatibility level. As the European Commission has so far only used the more economic approach on the justification level (Art. 87, Para. 3 EC Treaty) and not on the factual level (Art. 87, Para. 1 EC Treaty), it is not the European Commission but the member state that bears the onus of proof. If a detailed test is carried out the member state responsible for providing proof – and as a secondary instance the beneficiary enterprise – will incur considerable expenditure to convince the European Commission that the aid is compatible, as they must provide a large amount of information. This is one of the main differences from antitrust law, where the more economic approach has created more stringent proof requirements for the European Commission. The structure of aid control which the European Commission is endeavouring to achieve can be shown in the form of Table VI.3 below.

Table VI.3:

The Structure of the Aid Test

De Minimis Regulation
<ul style="list-style-type: none"> • directly applicable by member states • criteria that are easy to handle • no obligatory notification
General Block Exemption
<ul style="list-style-type: none"> • directly applicable by member states • more stringent requirements to apply the law (proof of incentive effect) • no obligatory notification
Test in Individual Cases
<ul style="list-style-type: none"> • Obligatory notification • Conceivable variants, where envisaged in guidelines: <ol style="list-style-type: none"> a) faster test procedure, in which assumptions are (also) applied b) elaborate test procedure with balancing test actually performed.

Source: Monopolkommission

6.3.2.4 Taking Proven Efficiency Advantages into Account

Antitrust law

212. In applying the more economic approach in antitrust law the European Commission intends to enable efficiency advantages to be taken into account throughout. The EC Treaty expressly provides for consideration of efficiency advantages, that is, possible welfare gains, in Art. 81, Para. 3 EC Treaty, if consumers participate appropriately.²²⁹ Art. 82 EC Treaty does not contain a corresponding clause. In its *British Airways* judgement of 15 March 2007 the ECJ first established the disadvantageous displacement effect of British Airways' discount and premium arrangement, and then expressly permitted efficiency advantages as an objection under Art. 82 EC Treaty.²³⁰ In this regard, and unlike the question of the model, the *British Airways* judgement is a success for the European Commission's more economic approach. This jurisprudence is based on the assumption that market behaviour can have a dual effect, that is, it can restrict competition and promote welfare.²³¹

Efficiency advantages have been important in merger control since the reform carried out in 2004 to introduce a more economic approach.²³² As the European Commission states in its guidelines for horizontal mergers, it takes all the proven efficiency advantages into account in its overall assessment of a merger. These must benefit consumers, be specific to the merger and be provable.

State Aid Law

213. The European Commission will not admit an objection of efficiency in aid control identical to that in the antitrust competition rules. Nor would it be possible there, as the parties that may cause restriction of competition are not companies but sovereign states. However, the criterion of market failure can be described as a kind of efficiency objection in state aid. For the fact of market failure, which is to play a central role in future in the examination of compatibility under Art. 87, Para. 3 EC Treaty, is given, in the European Commission's definition, if the market is not producing an economically efficient result. Moreover the member states – as always under Art. 87, Para. 3 EC Treaty – are responsible for proving that there is sufficient market failure in the meaning of the three-stage balancing test. As the onus of proving market failure is on the member states, and it is not easy to produce that proof, the more economic approach which the European Commission wishes to apply in competition law may not auto-

229 Under Art. 81, Para. 3 EC Treaty an agreement can be exempt from the ban on cartels if it “contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not: a) impose on the undertaking concerned restrictions which are not indispensable to the attainment of these objectives or b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.” The onus of proof that the conditions for exemption are met under Art. 81, Para. 3 EC Treaty is on the enterprises that claim under this rule (Art. 2, Sentence 2 Regulation 1/2003).

230 ECJ, Judgement of 15 March 2007, Case C 95/04, *British Airways*, No. 86.

231 By contrast, the European Advisory Group on Competition Policy (EAGCP), a body of independent experts who advise the General-Directorate for Competition, have proposed that any pro-competition effects should be examined in all cases by the European Commission as part of its abuse control, and always taken into consideration. Cf. European Advisory Group on Competition Policy (EAGCP, Gual, J., Hellwig, M., Perrot, A., Rey, P., Schmidt, K., Stenbacka, R.), *An Economic Approach to Article 82*, EAGCP, http://www.europa.eu.int/comm/competition/publications/studies/eagcp_july_21_05.pdf.

232 Cf. Merger Control Regulation, No. 29, and the statements by the European Commission in the guidelines for horizontal mergers Nos. 76-88 and in the guidelines for non-horizontal mergers (Guidelines for the merger of enterprises linked vertically or in conglomerates, No. 53).

matically result in a more positive assessment of aids and excessive awarding practice. On the contrary, more restrictive aid control is to be expected.

6.3.2.5 Economic Analysis Methods

Antitrust Law

214. In the more economic approach which it wishes to adopt the European Commission will make greater use of industrial economic models and quantitative analyses in its decision-making. It will rely on the Herfindahl-Hirschman Index (HHI), which has long been used in US merger control to establish the degree of concentration on a market before and after a merger.²³³ The European Commission uses price correlation analyses, shock analysis²³⁴ and in particular the hypothetical monopoly test (SSNIP test, small but significant non-transitory increase in price)²³⁵ to define a market materially and geographically.²³⁶ It also uses simulation models directly to obtain the effects of a merger on prices, quantities and welfare, especially for mergers of producers of differentiated goods.²³⁷

State Aid Law

215. If a detailed examination of compatibility is made on the justification level the European Commission intends in future to carry out complex economic analyses, which it has not used before. They will be used particularly to assess the criterion of the incentive effect. Unlike under the antitrust prohibitions, in state aid control the European Commission does not intend to apply new economic methods on the factual level (Art. 87, Para. 1 EC Treaty). Initially, only the cursory examination will be made, which is still very much less than the standard applied in EU antitrust law in the form-based approach that precedes the more economic approach.

7. Proposals by the Monopolkommission

7.1 The Economic Approach under Art. 87 EC Treaty

216. The Monopolkommission is in favour of a more economic interpretation of distortion to competition under the ban in Art. 87, Para. 1 EC Treaty. It recommends that the objective likelihood of an aid noticeably distorting competition should be examined under Art. 87, Para. 1 EC Treaty, as is the practice under the antitrust rule in Art. 81, Para. 1 EC Treaty.

233 The HHI shows the sum of squared market shares for companies on the market in question.

234 Past events and shocks on the market in question (like the introduction of a new product) are used to assess the market, cf. Schwalbe, U., Zimmer, D., *Kartellrecht und Ökonomie*, Frankfurt a.M. 2006, pp. 133.

235 This test examines whether the customers of the parties to a merger will react to an assumed small but permanent increase in relative prices (between 5% and 10%) for the products and areas under consideration by switching to easily available substitutes or not. If the substitution is so great that a price increase would not be profitable due to the fall in sales, other products will be included in the materially and geographically relevant market until a slight permanent increase in price would yield profits. For more detail cf. Schwalbe, U., Zimmer, D., loc. cit., pp. 104s.

236 For more detail see Christiansen, A.: Der "more economic approach" in der EU Fusionskontrolle, *Zeitschrift für Wirtschaftspolitik* 55, 2006, pp. 150-174, 153, and Brinker, I., *Praktische Probleme der Marktabgrenzung aus rechtlicher Sicht*, in: Schwarze, J. (ed.): *Recht und Ökonomie im europäischen Wettbewerbsrecht*, Baden-Baden 2006, pp. 41-52, 47s.

237 For more detail cf. Schwalbe, U., Zimmer, D. loc. cit., pp. 211s. and Monopolkommission, *Hauptgutachten 2004/2005*, loc. cit., Item 684. See also No. 29 of the Guidelines on horizontal mergers by the European Commission on the calculation of possible unilateral (one-sided) effects of a merger.

217. Under the ban in Art. 87, Para. 1 EC Treaty so far an in-depth economic analysis has only been made on “favouring”, and in the private investor test, which is determinant here. Distortion to competition is not generally subject to a more differentiated economic assessment, the European Commission only makes a general sector-specific examination, which is clearly less than the standards traditionally applied in EU antitrust law, where the European Commission now wishes to replace it with the more economic approach. Nor is “noticeable” distortion to competition required as an unwritten rule in aid control, as it is under the anti-trust rule in Art. 81 EC Treaty. No change to this practice is envisaged, in either the State Aid Action Plan or the implementation measures to date. The European Commission’s more economic approach only starts on the justification level, where the member state is responsible for providing proof. On this level the European Commission examines whether an aid can be approved as an exception (Art. 87, Para. 3 EC Treaty). That is not convincing, as the European ban on aid only takes effect and justifies intervention by the European Commission as the controlling body if a risk of distortion to competition on the internal market has been established (Art. 3, Para. 1 g) EC Treaty). In the view of the Monopolkommission the objective likelihood of an aid noticeably distorting competition should be examined under Art. 87, Para. 1 EC Treaty. This should be combined with a restriction of the area of application of aid control by the European Commission, and should be flanked by the introduction of complementary aid control on national level and by private right of appeal.²³⁸

218. In regard to the restriction of trade between member states in Art. 87, Para. 1 EC Treaty it should be an unwritten rule – as it is in antitrust law – that the restriction must be “noticeable”. This will avoid the area of application of Art. 87, Para. 1 EC Treaty also being extended to matters of less importance between member states and of only local focus. That would appear to be appropriate as aid control, like antitrust law, is designed to protect competition on the internal market (Art. 3, Para. 1 g) EC Treaty). So only if there is proven risk of negative cross-frontier effects can aid control give rise to a ban on European level.

219. The following remarks contain suggestions from the Monopolkommission on how these aims can be achieved. In general, it does appear to be appropriate to assume that certain aids will cause noticeable distortion of competition. However, as the concept of “favouring” (selectivity) in Art. 87, Para. 1 EC Treaty is very broadly interpreted a general assumption does not appear to be justified in every situation. Measures can also be classified as aid if they benefit all the companies in a region or all of a certain size. The same applies to measures that are horizontal in effect and benefit companies in very different branches.

220. Distortion to competition can be assumed for rescue aid to companies in financial difficulties. The danger of inefficient promotion at the expense of more efficient competitors must be regarded as particularly great here. The same applies to aid to benefit sectors with considerable excess capacities (restructuring aids). These aids can help to maintain inefficient market structures, and a closer examination should be made on the justification level to establish whether the measure is permissible by way of exception, owing to market failure (failure to adjust) or for non-economic reasons (especially social considerations).

221. The Monopolkommission recommends carrying out a test of noticeability under Art. 87, Para. 1 EC Treaty for all the other forms of aid. Elements of the “significant impact test” (SIT) could be used here. The European Commission had intended to introduce this in 2003, in order to be able to concentrate more on the more difficult cases of distortion to competition

²³⁸ See 4.3 and 7.4 for more detail.

in future.²³⁹ But it was not introduced owing to opposition from member states, who could not reach agreement, particularly on the positive list in the test, which names certain branches to be fixed in advance and where noticeable cross-frontier effects are to be regarded as unlikely.

222. In the view of the Monopolkommission the objection that could be raised to the positive list is that it would be an inflexible instrument and might have omissions. It could be more meaningful to set the following conditions, analogous to the SIT proposed by the European Commission:

- the aid should not be limited from the start to a specific enterprise or a specific sector,
- the aid granted to an individual enterprise within a period of three years would not exceed EUR 1 million,
- the aid would be activity-related, and its intensity, that is the share of the promotion in the total expenditure on a project, would not be more than 30%, and
- the aid would be given in an open procedure. That means that under general rules on aid it must be available to all the enterprises that meet certain criteria, and that individual aids must be given in a transparent tender procedure.

223. In addition, market shares and the resultant degree of concentration should be used as instruments in aid control to help identify distortion to competition. Analogous to the values which the European Commission has named in its guidelines for the assessment of horizontal mergers, a threshold of 25% for a market share and an HHI of 1000 could serve as orientation.²⁴⁰

224. In the case of aid to established companies with a strong market position there is a risk that they will be able to extend their advantage over their competitors. Entry to the market will also be made more difficult for newcomers and displacement practices facilitated. The greater the market concentration, the more likely is it that the competition will be distorted by

239 The SIT presented a new concept for the assessment of low amounts of state aid and of certain aids with limited effects on trade within the Community. Ultimately it consisted of two different tests, the LASA test and the LET test. Aid control would not be carried out if the measures met the criteria of both these tests. In the LASA (limited amount of state aid test) test, as under the De Minimis Regulation, a low level of aid would be determinant. Some further conditions would also be set. The test was to be made independent of the sector and include the following criteria:

- The aid must be directly intended for the eligible costs of a defined aim that is in the Community interest (e.g. R&D, environmental protection).
- The aid intensity, that is the share of the promotion in the total costs of the project, must be no more than 30%.
- Maximally EUR 1 million would be granted to any single enterprise within three years.
- The aid must be entered in a national register.
- A maximum upper limit would be fixed for the total amount of aid granted under the LASA test by each member state and must not be exceeded.

Under these conditions the LASA test would allow the assumption that an aid would have only limited effects on competition and trade and so that aid control by the European Commission would not be necessary.

The LET (limited effect on trade) test, unlike the LASA test, did not envisage an upper limit and also covered larger amounts of aid. Its key features were:

- A positive list would be drawn up of certain branches to be fixed in advance and where significant cross-frontier effects would be unlikely, e.g. branches without intensive competition on Community level.
- The aid must be given in an open procedure. Under general, abstract rules the aid must be available to all companies that meet certain criteria, and individual aid must be given in a transparent tender.
- The aid intensity must not exceed 30%.

240 Cf. European Commission, Guidelines for the assessment of horizontal mergers, OJ EU C 31 of 5 February 2004, here p. 7, Nos. 18s.

aid to established companies, as in a tight oligopoly the decision of each market participant influences the decisions of others. In this case actual distortion to competition can be assumed. Moreover, the political incentives to grant aid that will distort competition are particularly great here.

225. Conversely, the European Commission could be obliged to provide more reasons if the shares of the company benefiting are relatively low on the markets on which it is operating, or if the market is characterised by low concentration.

226. The degree of selectivity of the measure in question could also serve as a filter.²⁴¹ If the aid in question is highly selective, distortion to competition can be assumed. But if the measure is not very selective, e.g. because all the companies of a certain size category or within a certain region are to benefit, the European Commission would be obliged to examine the threat of distortion to competition from the aid more closely, and give reasons for this.

227. Should none of the above factors lead to a clear result the European Commission must clarify whether the measure will cause noticeable cross-frontier restriction of trade in a more detailed examination. Several factors need to be taken into account concerning both the aid and the way it will be given (aid criteria), as well as the relevant markets, the foreseeable effects on competition and the market position of the enterprise benefiting (market criteria). The aid criteria to be considered are the amount of the aid, its size in relation to the costs of the activity promoted (aid intensity) and the way it will be given. Here it is relevant whether the aid will be given only once or repeatedly, and whether an open and transparent procedure has taken place. Market criteria are whether there are excess capacities, the market share of the company benefiting, the market concentration, the distance in market share to the nearest competitor, the level of the barriers to market entry (high sunk costs), the degree of the company's vertical integration, the degree of product differentiation and the price development to be expected as a result of the aid.

228. The investigation outlined above presumes that, instead of a general sector-specific examination, the European Commission will define the markets in question materially and geographically in future in aid procedures as well, as it does under antitrust law, and establish the market position of the beneficiary. A specific delineation of the market with identification of the market share of the beneficiary, however, is only possible if the individual enterprise benefiting and the project to be promoted are already clear. But the ban on aid in Art. 87, Para. 1 EC Treaty not only covers aid of this kind, it also covers general aid schemes. In the case of aid with horizontal objectives it is frequently not fixed which companies in which sectors will benefit and which markets specifically will be affected. In that case the examination should be limited to establishing whether the state measure is likely to cause noticeable intervention in the market and affect the competition process in the EU internal market.

229. It must be remembered that the European courts are ultimately responsible for interpreting the ban on aid and the distortion to competition which it contains, and that traditionally they have set very low requirements for establishing that criterion. This problem could be solved by legal clarification. However, it is also conceivable that a change in the practice of applying the law would suffice, and the European courts could move away from their traditional jurisprudence. The judgement by the ECJ on the *Le Levant* case of 22 February 2006

²⁴¹ This is suggested by the British Office of Fair Trading in its response to the European Commission's State Aid Action Plan of September 2005, http://www.offt.gov.uk/shared_offt/reports/oft_response_to_consultations/oft820.pdf.

could be taken as an indication of this, for the Court expressly admonished the European Commission for not making a more detailed examination of distortion to competition in the negative decision against which appeal was made.²⁴²

230. If these more stringent requirements to identify distortion of competition are to be applied in future it could be objected that this could make it more difficult for member states to assess whether a measure should be notified under Art. 88, Para. 3 EC Treaty or not. This could be countered by retaining the low requirements in Art. 88, Para. 3 EC Treaty and only laying upon the European Commission a more stringent obligation under Art. 87, Para. EC Treaty.

7.2 The More Economic Approach on the Justification Level (Art. 87, Para. 3 EC Treaty)

231. The justification grounds given in Art. 87, Para. 3 EC Treaty are very broadly formulated and they allow the European Commission considerable scope for discretion. In view of this it is welcome that the European Commission has concretised the condition for decisions under these discretionary powers in more detail as part of its more economic approach, by introducing a three-stage test. The more economic approach the European Commission would like to introduce in aid control will thus provide greater transparency and legal certainty.

232. In the balancing test the European Commission will focus on the criterion of market failure as the possible ground for justifying aid.²⁴³ In this connection it must be asked whether a closer examination should be made of whether there is market failure, by way of exception, and the aid is the appropriate and necessary means of correcting it, on the factual level, in considering distortion to competition under Art. 87, Para. 1 EC Treaty. For should that be the case the competition situation will generally not be worsened, the aim is rather to improve the framework conditions for competition. However, in many cases where – presumed – market failure is to be removed there is a risk of state failure owing to erroneous prognoses, with consequent deterioration in the current competition situation (second-best problem). In view of the threat of over-optimal state intervention it would appear appropriate for the onus of proving a specific market failure to be on member states, and so a detailed examination would only be made on the justification level, which is the current practice by the European Commission. Accordingly, distortion to competition could be affirmed on factual level if the aid is likely to intervene noticeably in the cross-border competition process, and steer the behaviour of market participants and their investment decisions into a very different direction. So the criterion of market failure would have a function on the justification level comparable with the objection of efficiency in the European ban on cartels (Art. 81, Para. 3 EC Treaty).

233. A critical view can be taken of the fact that the European Commission sees the incentive effect as the main condition of its new balancing test. Aid should certainly only be granted if it will have an incentive effect, that is, change behaviour by the enterprise benefiting, as otherwise there would not be an additional economic benefit and public funds would be wasted. The powers of the European Commission in aid control are, however, limited to the protection of cross-border competition. In contrast to the draft regulation by the European Commission the incentive effect should not be included in a uniform, directly applicable block exemption regulation, either.²⁴⁴

²⁴² ECJ, Judgement of 22 February 2006, Case T 34/02, *Le Levant/Commission*, Rec. 2006, II-267, No. 127.

²⁴³ Non-economic aims of general interest (e.g. regional coherence) can also be grounds for justification.

²⁴⁴ Cf. 181.

7.3 An Efficient Procedural Design

234. As shown in 5.4 in the view of the Monopolkommission the efficiency of the aid control procedure could be increased by bringing it into line with the European antitrust procedure.²⁴⁵ In this context the procedural rights of competitors and the recipients of state aid should be strengthened, the European Commission's powers to investigate companies improved and shorter, binding deadlines for approval introduced. Instead of the legality principle in force to date (Art. 10, Para. 1 Procedural Regulation) the European Commission should also be granted discretion over whether to take up a case, as it has in antitrust law, if the aid does not exceed a volume still to be determined. That would enable the European Commission to set priorities and concentrate on important cases. The discretionary powers should be flanked by the introduction of the right of private parties to bring an action for a declaratory judgement.

235. The Monopolkommission recommends allowing appeals by the recipient of the aid, competitors affected and their associations before the Community courts, on general aid regulations as well. In addition, competitors should be able to obtain legal protection on European level more easily.²⁴⁶

236. Legal protection on national level should be regulated as a whole and take account of the requirements in aid law.²⁴⁷ In this connection especially a right of appeal should be introduced for associations, analogous to German antitrust law (§ 33, Para. 2 Act Against Restraints of Competition, GWB). The suspensive effect of lawsuits when recovery of the aid is ordered should also be excluded and an efficient legal protection system created, comparable to the rules on public procurements (§§ 104ss. GWB).

7.4 Complementary Aid Control on National Level

237. As well as negative consequences for competition in allocative, productive and dynamic regard, the award of state aid can involve considerable costs for the economy as a whole. State aid involves financing costs or other opportunity costs, and it causes loss of welfare, partly through the necessary taxation in other areas and partly through erroneous prognoses and free riding. While the competence of the European Commission in European aid control is limited to protecting cross-border competition, the member states must take account of all the economic costs in awarding state aid and weigh these against the expected benefit.

238. If European aid control is reduced to protecting cross-frontier competition as described above, its area of application will be limited compared with the European Commission's administrative practice to date. In the view of the Monopolkommission it is then absolutely essential to create at the same time effective complementary control mechanisms on national level. Otherwise there is a risk that owing to insufficient density of control aid would be granted on an inefficiently high and economically harmful level.

239. In the view of the Monopolkommission national aid programmes should be subject to regular success control, and in serious cases, where the individual aid or the aid programme exceeds an as yet unspecified volume, ex ante macroeconomic control should be carried out by an independent national body. Moreover, aid should on principle be given in an open and transparent procedure. Aid designed right from the start for individual companies or a specific

²⁴⁵ Cf. 130ss.

²⁴⁶ Cf. 146ss.

²⁴⁷ Cf. 158.

branch should be forbidden, and only permitted in exceptional cases after national ex ante control. As well as a time limit on aid programmes and digressive long-term promotion, state aid that exceeds a specific volume should be made known in advance by the public authority awarding it on a central Internet website. In particular, the subjective rights of potential recipients of aid, competitors affected and their associations should be upheld and an efficient system of legal protection created analogous to the law on public procurements (§§ 104ss. GWB).

240. The proposals by the Monopolkommission to reduce European aid control and build up national aid control are intended as a package that should only be implemented as a whole.

7.5 Summary of the Recommendations

241. The Monopolkommission believes that in the aid control procedure – as under Art. 81, Para. 1 EC Treaty – an examination should be made on the factual level of Art. 87, Para. 1 EC Treaty of the objective likelihood that an aid will noticeably distort competition and restrict trade between member states. Unlike antitrust law it is not an unwritten rule that an aid measure must have noticeable effects. Consequently, the area of application of aid control also covers cases of mainly local importance. In regard to distortion of competition the European Commission has so far generally only made an overall sectoral examination which is clearly less than the standard which is traditionally applied in EU antitrust law, where the European Commission would now like to supplement it with flexible economic criteria in a more economic approach. The European Commission's envisaged reform, with a more detailed examination of the initial structural situation on the market and the competitive situation to be made only on the justification level (Art. 87, Para. 3 EC Treaty), does not appear convincing, as the European ban on aid will only fulfil its purpose of protection if there is a threat of distortion of competition on the internal market and it has been appropriately identified.

242. In the view of the Monopolkommission it is entirely appropriate to assume distortion of competition from certain forms of aid granted by member states (for instance rescue and restructuring aids). But as the principle of favouring named in Art. 87, Para. 1 EC Treaty is very broadly interpreted a general assumption does not appear justified in every situation. In the view of the Monopolkommission a noticeability test that can be refuted should be introduced, with simplified exemption allowed on the basis of various criteria for aid below a threshold still to be specified (e.g. EUR 1 million). Should neither the noticeability test nor other assumptions yield the required result the European Commission should clarify in a more detailed assessment whether the measure will cause distortion to cross-border competition. In this regard several factors must be taken into account, affecting both the aid and the way it is granted (the aid criteria) and the relevant markets, the foreseeable effects on competition and the market position of the beneficiary enterprise (market criteria).

243. The procedure used in aid control should, in the view of the Monopolkommission, be reformed and in certain points brought into line with European antitrust procedures. In this connection the procedural rights of competitors and recipients of aid should be strengthened, the powers of the European Commission to investigate companies improved and shorter, binding deadlines for approval introduced. It should be considered replacing the current legality principle with discretion for the European Commission over whether to take up a case, as it has in antitrust law, if an aid does not exceed a certain volume. That would enable the European Commission to set priorities and concentrate on important cases. The discretionary powers could be flanked with the introduction of private right of appeal for a declaratory judgement.

The Monopolkommission also recommends admitting suits by recipients of aid, competitors affected and their associations before the Community courts, on general aid regulations as well. In addition, competitors should be able to obtain legal protection on European level more easily. Legal protection on national level should be regulated as a whole, and take due account of the requirements of aid law. In particular, right of appeal for associations should be introduced analogous to German antitrust law (§ 33, Para. 2 GWB). The minimum standards to be introduced for this in member states could be the subject of an EU directive. In addition, the suspensive effect of lawsuits in recovery cases could be excluded and an efficient system of legal protection created, similar to that in the law on public procurements (§§ 104ss. GWB).

244. If European aid control is reduced to the protection of cross-border competition its area of application will be limited compared with the previous administrative practice by the European Commission. In the view of the Monopolkommission it is necessary to create effective complementary control mechanisms on national level at the same time.²⁴⁸

245. Finally, the aid (subsidies) given by the EU itself and which, unlike the aid given by member states, does not come under the area of application of Arts. 87ss. EC Treaty, should be subject to more detailed examination. It should be considered extending control of EU subsidies to a new independent European supervisory authority, that could act free of political influence. Beside any EU-related measures the EU and member states should work more on international level for the introduction of a better system of control within the WTO framework.

248 See 7.4.