COVID-19 and State Aid: The EU Commission Swiftly Approves Multiple State Aid Measures

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The global pandemic COVID-19 has caused major disruptions to supply and demand chains throughout Europe and the world. European governments have therefore implemented a number of measures to support their national businesses and economies by granting various forms of aid, ranging from loans on favorable terms and public guarantee schemes to tax reliefs and compensation (see overview).

On 13 March 2020, the EU Commission ("Commission") set out a European coordinated response to counter the economic impact of COVID-19. "*We will do whatever is necessary to support the Europeans and the European economy*", said Commission President Ursula von der Leyen. Since then, the Commission mobilized a total of EUR 65 billion to provide liquidity, i.e. EUR 37 billion from the existing EU budget and structural funds, EUR 28 billion of unallocated structural funds and an additional EUR 800 million from the EU Solidarity Fund for hardest-hit Member States.

The main financial response has, however, come from the individual Member States. As at 2 April 2020, they together mobilized more than EUR 2.7 trillion to mitigate the socio-economic impacts of the pandemic. Such aid has been made possible under the "Temporary Framework" (the "Framework"), which was adopted by the Commission on 19 March 2020 and which relaxes the existing State aid rules to allow Member States to provide fiscal stimulus to businesses and ensure that sufficient liquidity is available.

On 3 April 2020, the Commission supplemented the Framework with a first amendment. And on 8 May 2020, the Commission adopted a second amendment to the Framework, which allows Member States to provide recapitalisations and subordinated debt schemes to companies in need—as a last resort—in return for equity. In the prelude to the second amendment's implementation, Executive Vice-President and competition commissioner Margarethe Vestager reiterated that, "*We continue working* *with Member States to make sure that the European economy can weather this storm, and bounce back even stronger*".

A further extension of the Framework has been implemented on 29 June 2020. This third amendment mainly widens the scope of the framework by expanding aid to small and micro companies, with a focus on innovative start-ups. On this occasion, Vestager emphasized that "*Micro, small and start-up companies are crucial for the economic recovery of the Union. They have been particularly affected by the coronavirus outbreak, and face greater difficulties to access financing*".

Additionally, the Commission revealed on 27 May 2020 its own EUR 750 billion pandemic recovery plan, the realisation of which will require the unanimous approval of all Member States.

The Framework

The Framework provides for a relaxation of European State aid rules to allow Member States to remedy the economic disturbance caused by the COVID-19 outbreak.

It applies to State aid measures put in place between 1 February and 31 December 2020 granted especially to small- and medium-sized enterprises ("SMEs") but also large companies, active in industries particularly affected by the COVID-19 outbreak such as transport, tourism, culture, hospitality, retail and event organizers.

As a general rule, under Article 107(1) TFEU, EU Member States are prohibited from giving aid in any form that distorts competition by favouring certain companies or sectors, if it affects trade within the EU. The prohibition aims *inter alia* at ensuring a level playing field between European companies. Exceptions are available, for example, to make good the damage caused by exceptional occurrences (Article 107(2) *lit*. b TFEU) or to remedy a serious disturbance in the economy of a Member State (Article 107(3) *lit*. b TFEU). The Framework concretizes such and other exceptions available for the Member States to mitigate the economic impact of the COVID-19 outbreak. In addition, it provides guidelines on which State aid measures need to be notified to the Commission, and which not.

Measures that do not require approval by the Commission

Certain measures do not fall under the State aid rules and can therefore be put in place by Member States immediately, without prior approval by the Commission. These include:

- Public support measures available to *all* companies, i.e., without differentiation by sector or region, such as wage subsidies, suspension of tax payments or social security contributions. These do not qualify as State aid because they do not provide a selective benefit.

- Public financial support granted directly to consumers, e.g., for cancelled services or tickets that are not reimbursed by the operators concerned. These types of measures also do not qualify as State aid because they do not provide benefit to a company.

- Public aids which fall under the General Block Exemption Regulation ("GBER"). This includes risk finance aid for SMEs of up to EUR 15 million per company.

- Public aids which fall under the *de minimis* Regulation. This includes aid of up to EUR 200,000 over three years in most sectors, subsidized loans of up to EUR 1 million, and subsidized guarantees for loans of up to EUR 1.5 million.

Measures that require approval by the Commission

The Framework allows Member States to provide five types of aid to support the economy, particularly to overcome a "serious disturbance in the economy" under Article 107(3) *lit*. b TFEU:

- **Direct grants, tax advantages and advance payments**. Member States may grant up to EUR 800,000 per company, conditional upon (i) a scheme with an estimated budget and (ii) the company not having been in financial difficulty on 31 December 2019. Exceptions apply for agriculture, fishery and aquaculture.

- **State guarantees for loans taken by companies from banks**. Member States may provide State guarantees to ensure that banks provide loans to companies facing sudden liquidity shortage.

- **Subsidized public loans to companies**. Member States will also be able to grant loans at favorable interest rates for a limited period of six years. Certain conditions apply. For example, loans with a maturity beyond 31 December 2020 may not exceed 25% of the company's revenues in 2019.

- **Safeguards for banks that channel State aid to the real economy**. State guarantees and reduced interest rates can be channeled through banks and other financial institutions to support businesses, particularly SMEs. The Framework specifies that such aid is considered as direct aid to the banks' customers, not to the banks themselves, and gives guidance on how to ensure minimal distortion of competition between banks.

- **Short-term export credit insurance**. Member States or State supported insurers are able to provide short-term export credit insurance for trade within the EEA and certain OECD countries, including the USA, Canada, Japan and Australia, which under the Framework are not considered as marketable risks.

To be compatible with the State aid rules, aid that falls under the above must be (i) directly linked to the damage caused by the COVID-19 outbreak; and (ii) proportionate, i.e. the compensation should not exceed what is necessary to make good the damage. Where these conditions are satisfied, the Commission has no discretion but to declare the aid compatible with the internal market.

First Amendment to the Framework

The first amendment extends the Framework to allow Member States to consider aid beyond access to liquidity and finance to companies, such as facilitating COVID-19 relevant research and development ("R&D") and testing facilities or preserving employment by contributions to wage costs. It provides for five types of additional State aid measures in the form of direct grants, tax advantages or repayable advances:

- **Support for Coronavirus-related R&D**. Member States can provide aid for R&D addressing the current health crisis. This includes all costs necessary for the project, including personnel; equipment; (pre-)clinical trials; obtaining, validating and defending patents; and marketing, etc.

- **Support for construction and upgrading of testing facilities**. Member States can provide aid for investments in infrastructure necessary for the development and testing of medicinal products (including vaccines) and treatments; hospital and medical equipment such as ventilators, protective clothing and diagnostic tools; disinfectants; and data collection and processing tools.

- **Support for the production of Coronavirus-related products**. Aid can also be granted by Member States to incentivize a rapid production of medicinal products (including vaccines); hospital and medical equipment and devices mentioned above; disinfectants, etc.

- **Deferrals of tax payments and/or of social security contributions**. To reduce liquidity constraints of companies and preserve employment (including self-employment), Member States can temporarily defer tax payments and social security contributions for *selected* sectors or companies that are particularly affected by the pandemic.

- **Wage subsidies for employees**. To preserve employment, Member States may contribute to the wage costs of *selected* companies (including the self-employed) to prevent lay-off of personnel. This is subject to aid being granted to companies from sectors or regions particularly affected by the pandemic and for a period of not more than twelve months; and the wage subsidy not exceeding 80% of the monthly gross salary of the individual.

In addition, the first amendment also allows Member States to grant zero-interest loans and guarantees on loans that cover 100% of the risk or to provide equity. Member States are permitted to provide such direct aid up to the nominal value of EUR 800,000 per company.

Second Amendment to the Framework

The Commission extended the scope of the Framework by way of a second amendment to enable Member States to provide recapitalizations to companies in need. This amendment allows Member States to buy stakes in companies in trouble (e.g., in the airline sector), as they did similarly during the 2008 financial crisis – but such measures should be adopted as a last resort. Italy has indicated it will renationalize Alitalia and the recapitalization of Germany's Lufthansa was already approved by the Commission.

In order to avoid distortions to competition, such bail-outs are subject to certain conditions. These include conditions on the:

- **Necessity, appropriateness and size of intervention**. Recapitalizations should only be granted if no other similarly effective solution is viable and common interest demands it, e.g., the market exit of a company would lead to social hardship or disruption to a vital service. The recapitalization aid must be limited to restoring a company's market viability.

- **Member State's recapitalization and remuneration**. The investment should be compensated and ought to encourage the sale of the shares acquired by the Member State to the beneficiary or third parties.

- **Exit plan**. The beneficiary and the Member State have to formulate an exit strategy, within six to seven years after the aid has been granted. Otherwise, the Commission must be informed of a restructuring plan for the beneficiary.

- **Governance conditions**. The beneficiary must not pay out dividends and commit share buybacks until the exit of the Member State has been fully completed.

Management remunerations must not exceed the level of 31 December 2019 if at least 75% of the recapitalization aid has not been redeemed.

- **Prohibition of cross-subsidization and acquisitions**. A beneficiary may not use the recapitalization aid to support integrated companies that were in economic difficulties prior to 31 December 2019. Non-SME beneficiaries are prevented from acquiring stakes of 10% or more in competitors until at least 75% of the aid has been redeemed.

Member States must also publish the identity of recipients of recapitalization aid within three months so as to maintain transparency. Furthermore, they will need to ensure that renationalized companies return to viability without further State support when the economy has stabilized.

Interventions by Member States are particularly noteworthy as the Commission has already urged them to prevent hostile takeovers of strategic companies by foreign purchasers; for more information see here. The second amendment to the Framework complements the Commission's guidelines to ensure that Member States make full use of their foreign direct investment screening tools to protect critical European assets and technology in a time of public health crisis and related economic vulnerability.

Third Amendment to the Framework

Under the third amendment of the Framework, State aid subject to the rules of the Framework may also be granted to micro and small companies that already were in financial difficulty on 31 December 2019, unless a company is in insolvency proceedings, has already received rescue aid that has not been repaid or is subject to a restructuring plan under the State aid rules.

Micro and small companies are undertakings with fewer than 50 employees and EUR 10 million of annual turnover or annual balance sheet total. Aid measures granted to SMEs are regarded as less harmful to competition due to the limited size of these companies. Assistance to start-ups is considered crucial, since they often don't generate income in their initial growth phase. The third amendment also adds incentives to private investors to participate in a Member State's recapitalization aid measure. If the private participation is significant, i.e., it represents 30% of the new equity injected, then certain restrictions for recapitalizations under the Framework are lifted or relaxed, such as the dividend bans for shareholders.

Rapid Response by Commission

Since the implementation of the Framework, the Commission has evidenced an unprecedented pace of action and responsiveness. Already on 12 March 2020, the Commission approved a Danish State aid scheme within 24 hours of its adoption to compensate for damages caused by the COVID-19 outbreak. The Commission has since continued to approve State aid schemes notified to it in a swift and expedited manner (within 24 to 48 hours of notification), benefitting from its experience gained during the financial crisis in 2008 and moving faster than it did then as a result.

Up to date, all 27 Member States and the UK have received approvals for State aid schemes. The Commission has also re-assigned additional staff to its State aid units to help during this initial crisis period, and is approving State aid measures on a continuous basis, including on weekends, without exception.

Until end June 2020, the Commission has approved over 170 State aid measures. The Commission will continue to refine its tools and assess whether the Framework would need to be extended beyond 31 December 2020 to ensure legal certainty.

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For more information regarding the legal impacts of the coronavirus, please visit our Coronavirus Resource Center.

Please do not hesitate to contact us with any questions.

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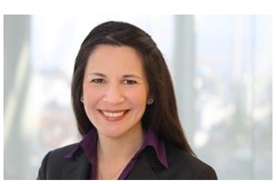

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