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REPORT

State Aid Scoreboard

- autumn 2005 update -

(presented by the Commission)

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Executive Summary

Downward trend in the overall volume of State aid has leveled off …though the vast majority of Member States have heeded the call to favour horizontal objectives

How are Member States responding to the call for “less and better targeted aid”? Although there are clear differences between the EU-25 Member States, broadly-speaking the answer is “no” to less aid but “yes” to better targeted aid. After the considerable fall in the level of aid at the end of the nineties, the underlying trend over the last five years has been stable rather than downward. The vast majority of Member States do however appear to be shifting the emphasis from supporting individual companies or sectors towards tackling horizontal objectives.

While the overall level of aid has remained stable in most Member States, the picture is not homogeneous throughout the Union

While, for the Union as a whole, the volume of State aid has remained stable, the situation in some Member States has changed significantly. For example, the overall level of aid relative to GDP has fallen sharply in Cyprus, Czech Republic and Malta due largely to the phasing out of pre-accession measures. Ireland, too, experienced a significant decrease, primarily the result of a cut in the Irish Corporation Tax coupled with an increase in GDP. In contrast, aid in relation to GDP increased significantly in a number of Member States: in France, due largely to the restructuring of Alstom in 2004 while in Sweden and the United Kingdom the rise can be explained largely by increases in aid for horizontal objectives, particularly aid to the environment.

Reducing aid by making better use of alternative instruments

In the context of reducing the overall volume of State aid, the Commission has been examining with Member States to what extent alternative instruments can be used in place of (potentially) distortive State aid measures. One of the best ways to reduce the level of State aid is clearly to make better use of alternative measures such as general and regulatory measures. Before resorting to State aid, which should in general only be the “second best” option, Member States should verify whether it represents the most appropriate solution, whether it is targeted carefully to problem areas and is limited to necessary amounts and effective means. Some types of instrument not only help to avoid distortions to competition, but also support Member States efforts to restore and maintain healthy public finances, which is also one of the main pillars of the Lisbon Strategy for Growth and Jobs.

How can Member States ensure that their state aid policies are pursuing these objectives? The answer lies to a large extent in the granting procedures and practices of State aid in the Member States. As a first step towards identifying best practices that support a “less and better targeted” state aid policy, the Commission addressed a written questionnaire to Member States in May 2005 and discussed these topics at a meeting with State aid experts in July. Part Three of the Scoreboard presents a summary of the replies.

The share of horizontal aid has increased largely due to a sharp increase in aid for environmental and energy saving objectives coupled with a reduction in sectoral aid for some Member States, particularly to the coal sector

In line with the commitments undertaken at successive European Councils, Member States have continued to redirect aid towards horizontal objectives. Over the period 2000-2002 and 2002-2004, the share of total aid for horizontal objectives increased by 4 percentage points, largely as the result of significant increases in aid for the environment and energy saving (+6 points) as well as a reduction in sectoral aid for some Member States.

EU-wide, there were no other significant increases in the share of aid for other horizontal objectives such as research and development. As stated in the recent draft Communication on State Aid for Innovation, the Commission makes clear that state aid is not the response to all Europe's competitiveness or innovation problems. While the Commission recognises that, in an effort to create growth and jobs, state aid policy can be used pro-actively to support innovation, by tackling the market failures that prevent markets from naturally delivering innovation, it also stresses that for business to embark on a more innovative path it requires, first and foremost, effective competition.

By 2004, the share of horizontal aid had risen to 76% of the total amount of aid (excluding agriculture, fisheries and transport). The four main horizontal objectives were environment and energy saving (25% of total aid), regional economic development (18%), R&D (12%) and SMEs (12%). The remaining 24% was aid directed at specific sectors (mainly coal) including aid to rescue and restructure ailing firms.

While the vast majority of Member States have redirected aid to horizontal objectives, the share in total aid varies considerably between the Member States

In around half the Member States, more than 90% of all the aid awarded in 2004 was earmarked for horizontal objectives. In another group of Member States (Spain, France and Ireland) the share was around 60% while in several other countries, the share was significantly lower: 50% or less in Hungary, Cyprus, Slovakia, Poland, Portugal and Malta. The low share of horizontal aid (and thus relatively high share of sectoral aid) in Portugal was due a large regional aid tax scheme in Madeira. In Ireland, although aid awarded through the Irish Corporation Tax has decreased significantly it still accounts for a relatively high share of total aid. France, Germany and Spain have relatively high shares of aid to the coal sector although the low share of horizontal aid in France is due mostly to the large award of aid to Alstom while in Germany, the large guarantee provided as a part of the restructuring package to Bankgesellschaft Berlin AG[1] in 2002 is another important factor. For a number of the new Member States, the disparity can be explained in part by the relatively strong support of several industries (e.g., financial sector, coal and steel) before accession in the context of privatisation or to ensure viability.

Overall level of aid earmarked for the least developed regions has increased significantly with enlargement

Each Member State targets part of its State aid towards the least developed regions, the so-called 'assisted regions'. For the Union as a whole, an estimated €12.3 billion of aid was

1 C28/2002

earmarked exclusively for assisted 'a' regions in 2004[2]. This represents 27% of total aid (less agriculture, fisheries and transport for which a regional breakdown is not available).

With the exception of Cyprus, and the cities of Prague and Bratislava which qualify for assistance under Article 87(3)(c) of the Treaty, the entire territories of the ten new Member States are eligible at 'a' level.

Significant increase in aid for environmental and energy saving objectives

Expenditure on environmental and energy aid increased from an annual average of € 6.5 billion in the period 2000-2002 to € 9.3 billion during 2002-2004. While such aid is clearly directed at a commonly accepted horizontal objective, only a relatively small proportion comprises aid to make investments that reach higher environmental standards than community standards or to undertake further investment to reduce pollution or for the development of renewable energy sources. On the other hand, a large proportion of aid (accounting for around 80% of total environmental and energy saving aid in 2004) comprises tax exemptions of which the largest part had to be accepted in order to allow for certain types of environmental taxes to be introduced, e.g., to limit the impact of such taxes on the competitiveness of specific companies or sectors. Although the tax exemptions from environmental taxes do not aim at reaching higher environmental standards, such exemptions are only allowed where the taxes themselves are intended to make a significant contribution to protecting the environment and the exemptions should not undermine the general objectives pursued. Such exemptions have been used in particular by Germany, Sweden and the United Kingdom. Part Two of the Scoreboard provides an in-depth look at the environment by describing the State aid rules applicable in this area.

More than €3 billion awarded under the block exemption regulations

By the end of 2004, more than 800 measures had been submitted by Member States under the block exemption regulations covering aid to SMEs[3], training, employment. Five Member States, Italy (26% of the total), the United Kingdom (22%), Germany (11%), Spain (8%) and Belgium (7%) accounted for 75% of all exempted measures in 2004. As regards expenditure, an estimated €3.4 billion was awarded in 2004 under the three block exemption regulations. This represents around 10% of all aid directed at horizontal objectives.

Around €3.4 billion of unlawful aid remains to be recovered

Of the € 9.4 billion of aid to be recovered under decisions adopted since 2000, some € 7.9 billion (a principal amount of € 5.9 billion plus almost € 2 billion interest) had been effectively recovered by the end of June 2005. Excluding interest, this represents 63.5% of the total amount to be recovered.

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2 The Article 87(3)(a) regions are largely identical to the Objective 1 regions under the EU Structural Funds. This figure includes all aid specifically earmarked for assisted 'a' regions regardless of the overall objective of the aid.

3 Excluding measures exempted under the block exemption regulation for agriculture (No 1/2004 of 23 December 2003 on State aid to SMEs in the agricultural sector, OJ L 1, 03.01.2004, pages 1-16) for which there were 72 cases in 2004.

Main State aid figures for 2004

The overall level of State aid[4] granted by the twenty-five Member States was estimated at €62 billion in 2004, the equivalent of 0.6% of GDP. In sectoral terms, around €40 billion of aid was earmarked for the manufacturing and service sectors, €15 billion for agriculture and fisheries, €5.5 billion for coal and a little over €1 billion for the transport (excluding railways) sector.

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4 Total State aid in the sense of Article (87)1 of the Treaty, covering manufacturing, services, coal, agriculture, fisheries and transport with the exception of the railway sector. For the ten new Member States, comparable data for the transport sector are not yet available.

INTRODUCTION

The main aim of this update of the Scoreboard is to assess Member States progress towards meeting the Lisbon objectives and response to successive European Councils call for "less and better targeted State aid". The European Council of March 2005 invited Member States to "continue working towards a reduction in the general level of State aid, while making allowance for any market failures. This movement must be accompanied by a redeployment of aid in favour of support for certain horizontal objectives such as research and innovation and the optimisation of human capital. The reform of regional aid should also foster a high level of investment and ensure a reduction in disparities in accordance with the Lisbon objectives." These goals were underlined by the Commission Recommendation on the Broad Economic Policy Guidelines for 2005-2008[5].

The Scoreboard is divided into four main parts. Part One looks at the extent to which Member States have responded to the Lisbon Strategy by first providing an overview of the amount and type of (potentially) distortive State aid awarded by the Member States in 2004 and then examining the underlying trends. Part Two provides a special focus on State aid for the environment and energy saving, an area which has seen a sharp increase in aid levels in recent years.

Part Three looks to what extent Member States assess whether or not State aid is the most appropriate form of intervention and what alternatives to State aid are used. It also includes an update of the recovery of unlawful State aid. Finally, Part Four summarises ongoing work to modernise State aid control through legislative and policy means.

Improvements have been made to the coverage, quality and timeliness of the State aid data published in this Scoreboard. This is the first time that information has been presented for all EU-25 Member States even though the data for the ten new Member States prior to accession are not entirely comparable with those of the EU-15 Member States[6]. A revised Standardised Reporting Format[7] has improved the comparability of information provided by Member States and for the first time the Commission has been able to publish data for the previous year, i.e. 2004 data in this update of the Scoreboard.

In addition to this paper edition, a permanent online Scoreboard consisting of a series of key indicators and a range of statistical information for the EU Member States is available on the on the homepage of the Competition Directorate General's Internet site (http://europa.eu.int/comm/competition/state_aid/scoreboard/).

The spring 2006 Scoreboard will include a focus on enlargement, looking in particular at the state aid situation in Bulgaria and Romania.

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5 COM(2005) 141 final, 12.4.2005 http://europa.eu.int/comm/economy_finance/publications/european_economy/2005/comm2005_141en.pdf

6 See autumn 2004 Scoreboard for further explanation on methodological issues.

7 The new provisions can be found in Commission Regulation (EC) No 794/2004 of 21 April 2004. Annex IIIA covers all sectors except agriculture (Annex IIIB) and fisheries (Annex IIIC) http://europa.eu.int/eur-lex/en/archive/2004/l_14020040430en.html

1. PART ONE: PROGRESS TOWARDS THE LISBON AGENDA

This chapter provides an overview of (potentially) distortive State aid granted in the EU Member States in 2004 and examines the underlying trends. The main purpose is to measure the extent to which Member States have met the call for less and better targeted aid. Although there are clear differences between the EU-25 Member States, broadly-speaking the answer is "no" to less aid but "yes" to better targeted aid. After the considerable fall in the level of aid at the end of the nineties, the underlying trend over the last five years has been stable rather than downward. The vast majority of Member States do however appear to be shifting the emphasis from supporting individual companies or sectors towards tackling horizontal objectives.

1.1. State aid in absolute and relative terms

Total State aid[8] granted by the EU-25 Member States was estimated at €62 billion in 2004. In absolute terms, Germany granted the most aid (€17 billion) followed by France (€9 billion) and Italy (€7 billion).

In sectoral terms, around €40 billion of aid was earmarked for the manufacturing and service sectors, €15 billion for agriculture and fisheries, €5.5 billion for coal and a little over €1 billion for the transport (excluding railways) sector.

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8 The total covers aid to manufacturing, services, coal, agriculture, fisheries and part of the transport sector but excludes aid to the railway sector (see section 1.3).

Table 1: State aid awarded in the EU-25 Member States, 2004

	Total state aid less railways in billion €	Total state aid less agriculture, fisheries and transport in billion €	Total aid less railways as % of GDP	Total aid less agriculture, fisheries and transport as % of GDP
EU-25	61,6	45,5	0,60	0,44
EU-15	56,4	42,0	0,57	0,43
10 new MS	5,2	3,4	1,09	0,70
BE	1,0	0,7	0,34	0,24
CZ	0,4	0,2	0,41	0,19
DK	1,4	1,0	0,71	0,52
DE	17,2	15,1	0,78	0,69
EE	0,0	0,0	0,39	0,09
GR	0,5	0,3	0,29	0,20
ES	4,0	3,1	0,47	0,37
FR	8,9	6,3	0,54	0,39
IE	1,0	0,4	0,65	0,27
IT	7,0	5,4	0,52	0,40
CY	0,2	0,1	1,48	1,06
LV	0,0	0,0	0,39	0,16
LT	0,1	0,0	0,68	0,13
LU	0,1	0,0	0,31	0,17
HU	1,0	0,7	1,26	0,87
MT	0,1	0,1	3,10	2,71
NL	1,8	0,9	0,39	0,18
AT	1,4	0,5	0,61	0,22
PL	2,9	2,0	1,47	1,01
PT	1,5	1,1	1,09	0,83
SI	0,2	0,1	0,96	0,53
SK	0,2	0,2	0,64	0,63
FI	2,5	0,6	1,66	0,38
SE	2,7	2,2	0,99	0,80
UK	5,4	4,2	0,32	0,25

(Potentially) distortive State aid as defined under Article 87(1) EC Treaty that has been granted by the twenty-five EU Member States for all sectors except railways and has been examined by the Commission. Comprehensive data on transport are not yet available for the ten new Member States. All data are quoted at constant prices. Source: DG Competition

Disparities between Member States in the share of State aid as a percentage of GDP

In relative terms, State aid amounted to 0.6% of EU Gross Domestic Product (GDP) in 2004. This average masks significant disparities between Member States: the share of total aid to GDP ranges from 0.4% or less in Belgium, Czech Republic, Estonia, Greece, Latvia, Luxembourg, the Netherlands and the United Kingdom to 1.5% or more in Cyprus, Malta, Poland and Finland (Table 1). The high proportion in some of the new Member States is due largely to pre-accession measures that are either being phased out under transitional arrangements or limited in time though in Poland there has also been considerable financial support provided to the coal sector. In Finland, the explanation can be found in the relatively large amount of aid to agriculture which represents more than 70% of total aid in this country.

Indeed, due to the particularities associated with aid to agriculture and fisheries, it is worth looking at total aid less these sectors. This second indicator produces a rather different ranking of Member States. For example, such aid in Finland represents 0.38% of GDP, just below the EU-wide average of 0.44%.

It is important to bear in mind that some aid measures can not be quantified. Although the number of measures is limited, the distortion of competition is often very significant and has an impact on the overall level of State aid, e.g., the unlimited State guarantees previously available to Electricité de France (EDF) and the German Landesbanken. Moreover, of the 96 recovery decisions adopted since 2000, there are 24 cases for which the aid can not yet be quantified. See recovery of unlawful aid (section 4.2).

Downward trend in the overall volume of State aid seems to have levelled off

Since the rapid decline towards the end of the 1990s (see spring 2005 Scoreboard), the downward trend in the overall volume of aid appears to have leveled off since the year 2000, in spite of pledges by Member States at successive European Councils to reduce the overall level of aid. The degree to which Member States have achieved this goal or not can be measured by looking at total state aid relative to GDP over a period of one year, i.e. the trend from 2003 to 2004 or by observing the underlying trend over the periods 2000-2002 and 2002-2004. In order to eliminate as far as possible annual fluctuations, the latter option is preferred. For the Union as a whole, total aid less agriculture, fisheries and transport relative to GDP remained unchanged between the two periods under review. This average masks however differences between Member States. The sharpest falls can be observed in Cyprus, Czech Republic and Malta due largely to the phasing out of pre-accession measures. Ireland, too, experienced a significant decrease, primarily the result of a cut in the Irish Corporation Tax[9] coupled with an increase in GDP.

In contrast, aid in relation to GDP increased significantly in a number of Member States: in France, due largely to the restructuring of Alstom[10] in 2004; in Poland, the rise can be attributed to the exceptional award of aid to the coal sector in 2003; while in Sweden and the United Kingdom the rise can be explained largely by increases in aid for horizontal objectives, particularly aid to the environment.

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9 The rate of corporation tax in Ireland has been cut progressively in recent years and is 12.5% from 2003. This has reduced the comparative value of the preferential 10% rate to the manufacturing sector, therefore contributing to the decline, in monetary terms, of aid to this sector.

10 C58/2003

Table 2: Trend in the level of State aid in the EU Member States, 1994-2004

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	Annual average 2000-02	Annual average 2002-04
EU-25													
Total state aid less agriculture, fisheries and transport in billion €							46,0	47,0	52,7	48,8	45,5	48,5	49,0
as % of GDP							0,46	0,47	0,52	0,49	0,44	0,48	0,48
EU-15													
Total state aid less railways in billion €	77,5	77,0	75,5	95,5	64,3	54,8	56,6	58,0	63,5	55,3	56,4	59,4	58,4
as % of GDP	1,08	0,98	0,95	1,14	0,74	0,61	0,60	0,61	0,66	0,58	0,57	0,62	0,60
Total state aid less agriculture, fisheries and transport in billion €	58,9	57,0	56,7	76,2	48,8	38,5	40,9	42,5	46,8	39,4	42,0	43,4	42,9
as % of GDP	0,82	0,73	0,71	0,91	0,56	0,43	0,43	0,45	0,48	0,41	0,43	0,45	0,44

Note: The exceptionally high figure in 1997 can be largely attributed to the Credit Lyonnais case in France. Similarly the relatively high figure in 2002 is due in part to the substantial guarantee awarded as a part of the restructuring package to Bankgesellschaft Berlin AG (C28/2002). For the ten new Member States, no data on transport are available while data on agriculture are available for 2004 only. Source: DG Competition.

In making comparisons between Member States, it is important to bear in mind the effect that the trend in GDP has on this indicator. Member States which have experienced relatively high economic growth over the period under review could theoretically increase the level of aid and still demonstrate a downward trend.

1.2. Sectoral distribution of aid

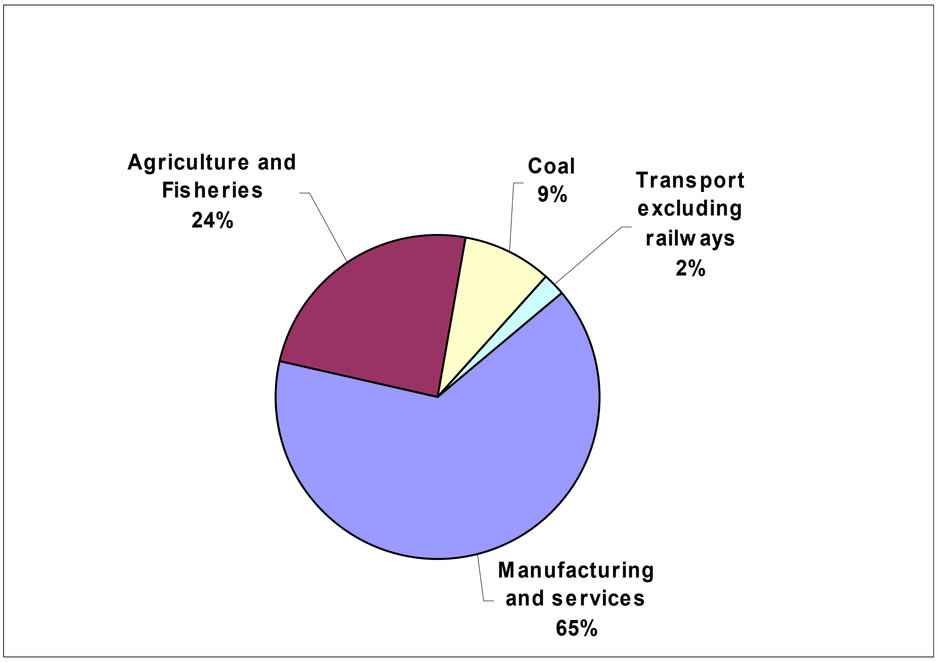
Sectoral distribution of aid varies considerably among Member States and over time

Although the data do not provide an accurate picture of the final recipients of the aid, they nevertheless give some indication as to which sectors are favoured by each Member State. In 2004, around 65% of State aid in the EU-25 Member States was earmarked for the manufacturing[11] and service sectors. A further 24% was directed towards agriculture and fisheries, 9% for coal and the remaining 2% going to the transport (excluding railways) sector. (Graph 3)

There are significant differences between Member States in the sectors to which they direct aid (Table 3). Aid directed at the manufacturing and service sectors represented 75% or more of overall aid in Italy, Malta, Sweden and Slovakia. Aid to the agricultural and fisheries sectors accounted for 60% or more of total aid in Austria, Estonia, Finland, Latvia and Lithuania while the share of aid to the coal industry was relatively high in Spain (28%), Germany (18%) and Poland (17%).

[11] For the purposes of the Scoreboard, the manufacturing sector includes aid for steel, shipbuilding, other manufacturing sectors, aid for general economic development and aid for horizontal objectives including research and development, SMEs, environment, energy saving, employment and training for which the specific sector is not always known. As a result, data on aid to manufacturing may be overestimated.

Graph 1: Total State aid by sector, EU-25, 2004



Note: (Potentially) distortive State aid as defined under Article 87(1) EC Treaty that has been granted by the EU-25 Member States for all sectors except railways and has been examined by the Commission. Source: DG Competition, DG Transport and DG Fisheries and DG Agriculture.

Table 3: Sectoral distribution of aid by Member State, 2004

	% of total							Million euro
	Manufacturing	Services (including tourism, financial, media and culture)	Agriculture	Fisheries	Coal	Transport excluding railways	Other non-manufacturing	Total
EU-25	59	5	23	1	9	2	1	61617
BE	65	4	26	0	0	2	2	972
CZ	37	5	47	6	4	0	0	352
DK	71	2	20	1	0	6	0	1375
DE	66	4	12	0	18	0	0	17236
EE	24	0	76	0	0	0	0	35
EL	66	3	28	2	0	0	1	473
ES	49	1	18	3	28	0	0	3975
FR	54	7	26	1	10	2	0	8915
IE	33	8	58	0	0	0	0	951
IT	72	5	16	2	0	6	0	7037
CY	35	24	29	0	0	0	12	184
LV	25	15	60	0	0	0	0	44
LT	16	0	81	1	0	0	3	122
LU	48	8	45	0	0	0	0	78
HU	63	1	31	0	5	0	0	1015
MT	87	0	13	0	0	0	0	134
NL	47	0	45	0	0	8	0	1813
AT	32	4	63	0	0	0	0	1427
PL	51	0	31	0	17	0	1	2873
PT	13	61	24	1	0	0	2	1475
SI	46	1	45	0	6	0	2	250
SK	98	0	2	0	0	0	0	212
FI	22	1	74	0	0	3	0	2483
SE	75	4	12	0	0	7	2	2745
UK	71	0	18	2	1	2	6	5442

Due to the rounding of figures, the percentages of some Member states do not sum up to exactly 100. Source: DG Competition, DG Transport and DG Fisheries and DG Agriculture.

1.3. State aid to the transport sector

The Commission's State aid control in the transport sector is rather complex arising from the need to take account not only of the general provisions on State aid, but also the special rules in the Treaty and secondary legislation dealing specifically with transport, in particular Article 73 of the Treaty as implemented by Regulations 1191/69[12], 1107/70[13] and 1192/69[14]. In addition, to reinforce the Internal market and economic and social cohesion, Article 154 EC Treaty provides for Community support, in the context of open and competitive markets, of trans-European networks. Moreover, many transport operators perform public service functions and for that benefit from public financing; while Community law, in the transport field in particular, does indeed contain a number of mechanisms effectively offering the

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12 Regulation (EEC) No. 1191/69 of the Council of 26 June 1969 on action by Member States concerning the obligations inherent in the concept of a public service in transport by rail, road and inland waterway.

13 Regulation (EEC) No. 1107/70 of the Council of 4 June 1970 on the granting of aid for transport by rail, road and inland waterway.

14 Regulation (EEC) No. 1192/69 on common rules for the normalisation of accounts of railway undertakings is particularly important from a State aid monitoring perspective as it exempts from the notification procedure a number of different compensations from public authorities to railway undertakings.

possibility for Member States to provide services of general economic interest (SGEI), the Commission must check that the public financing granted complies with the rules laid down in order to ensure that this financing does not distort competition. States are also involved in financing transport infrastructure, and this is raising more and more questions about the application of the State aid rules with the development of the commercial operation of certain infrastructures (ports, airports, etc.). The Commission is having to develop and specify its practice, distinguishing in particular between infrastructures used by an economic or commercial operator and infrastructures that are clearly connected with public authority functions or those that are open to all users on a non-discriminatory basis and which do not benefit a particular undertaking.

For the transport sector as a whole, excluding railways, around €1.5 billion of aid was awarded per year over the period 2002-2004, a slight increase on the annual average over the period 2000-2002. These data refer to the EU-15 Member States only as comprehensive data on all existing aid to the transport sector are not yet available for the ten new countries (Table 4).

More than 60% of total transport aid (around €1 billion per year) was awarded to the maritime sector during the period 2002-2004. The largest amounts were given by Denmark, France, Sweden and the United Kingdom.

Before liberalisation of the airline sector, considerable amounts of aid (exceeding €2.5 billion in 1994 and 1995) were awarded to national airlines for restructuring in the mid-nineties. Since 1997, however, aid levels to the industry have fallen dramatically though some aid continues to be authorised. Over the period 2002-2004, an annual average of €330 million of aid was awarded to the air transport sector (Table 4). The increase as compared to the previous period is mainly due to the rescue aid package for Alitalia in 2004.

Table 4: State aid to the transport sector (excluding railways), EU-15, 2000-2004

€ million

Transport sector	Annual average 2000-2002	Annual average 2002-2004
Road and combined transport	170	207
Maritime transport	905	1012
Inland water transport	5	6
Air transport	265	332
Total	**1 345**	**1 557**

Note: Comprehensive data on all existing aid to the transport sector are not yet available for the ten new Member States. Source: DG Energy and Transport

Railways

Much of the public financing of the railways is not notified to the Commission, either because the financing, due to the lack of liberalisation of the sector, is not deemed by Member States to constitute State aid within the meaning of Article 87(1) of the Treaty, or because it represents compensation for public services in accordance with Regulation 1191/69. Member States are however required to report to the Commission overall public expenditure to this sector. Disparities between Member States may reflect different interpretations of the scope of this annual reporting exercise (Table 5).

Table 5: Subsidies(1) to the railway sector, 1998-2004

in million current €

	1999	2000	2001	2002	2003	2004
EU-15	20.188	21.367	29.029	27.107	25.281	24.710
BE	1.783	1.815	1.843	1.905	2.024	1.909
DK	120	181	197	213	202	243
DE	5.218	4.760	4.871	4.887	4.433	3.475
EL	514	446	625	552	636	n.a.
ES	1.061	1.112	1.107	1.098	1.089	1.119
FR	4.577	4.857	6.146	6.244	4.890	6.205
IE	41	206	219	277	321	180
IT	3.822	4.578	5.045	5.483	4.268	3.920
LU	112	134	162	178	201	207
NL	1.693	1.974	2.613	2.865	3.232	2.668
AT	15	13	13	16	13	n.a.
PT	9	8	13	15	35	36
FI	357	330	283	331	407	488
SE	763	817	816	844	954	1.121
UK	104	137	5.077	2.198	2.577	3.141

(1) Includes all public subsidies that have been communicated to the Commission as well as subsidies that have been notified and authorised by the Commission under relevant State aid rules. However the figures exclude compensation for services of general economic interest. Data for EL, AT and ten new Member States are not available for 2004. Source: DG Energy and Transport.

See also section 4.4 on legislative and policy developments in the transport sector.

1.4. State aid to the agriculture and fisheries sectors

The total amount of State aid awarded to the agricultural sector by the EU-25 Member States was estimated at just over €14 billion in 2004[15]. France (€2.3 billion), Germany (€2 billion) and Italy (€1.1 billion) reported the highest figures. The data are based on a new annual reporting exercise introduced for the first time this year[16].

Expenditure figures are currently not available by type of aid measure (investment aid, crisis management etc) used by the various Member States in the agricultural sector. However, an analysis of the 1 277 decisions taken by the Commission between 1 June 2000 and 1 October 2005 provides a useful overview of the situation in the EU-15 Member States. These decisions involved 1 717 new aid measures which comprise aid schemes and (rather rare) one-off support measures for individual companies.[17] Notifications frequently cover more than one type of aid. For example, investment aid may be combined with aid for consultancy costs.

Of the total 1 717 aid measures, 523 or 30% were notified by Italy followed by Germany (246), Spain (287) and France (288).

15 Based on 2003 data for Luxembourg and Portugal (no data received for 2004) and Italy (incomplete report)

16 Commission Regulation (EC) No 794/2004 of 21 April 2004, Annex IIIB

17 This analysis is limited to notifications made from 1 June 2000 onwards. Not all of the 1 717 measures are still in force. Also, Member States may still apply measures introduced before June 2000.

Table 6: Main types of aid measure for the agricultural sector, EU-15, 2000-2005

Type of aid	Number of new aid measures in EU 15 Member States June 2000 – Sep 2005	% of total
On-farm investment	186	11
Processing & market invest.	125	7
Producer group start up	58	3
Technical support (1)	366	21
Crisis management (2)²	494	29
Research & development	78	5
Promotion & advertising	100	6
Other	310	18
Total	1 717	100

(1) Technical support consists of: technical aid, quality products: control and soft aid
(2) Crisis management consists of natural disaster, adverse weather, animal diseases, TSE, BSE, plant disease, insurance premia, closing of production and rescue & restructuring. Note: A more comprehensive table broken down by Member State and more detailed types of aid measure will be available on the online Scoreboard. Source: DG Agriculture.

The total amount of State aid awarded to the fisheries sector by the EU-25 Member States was estimated at around €500 million of which Italy and the United Kingdom each accounted for €120 million and Spain €100 million.

1.5. State aid to the coal and steel sectors

The European Coal and Steel Community Treaty expired on 23 July 2002 upon which a new Council Regulation was established as the new legal framework for state aid to the Community coal industry.[18]

The overall amount of State aid to the coal sector in the Union stood at €5.6 billion in 2004. The underlying trend is downward with the annual average dropping from €7.6 billion for the period 2000-2002 to €7.2 billion for the period 2002-2004. Germany contributed most to this fall (Table 7). The decrease over this period would have been even larger had it not been for the exceptional award of aid in Poland in 2003 (around €4 billion).

In 2004, around 55% of the total related to current production. As from 2003, aid to current production has decreased significantly and steadily in line with the agreements on the reduction of volumes of aid to the coal industry until 2005. The total amount of aid to current production to be granted annually shall in any event not exceed the amount of aid authorized

[18] Council Regulation (EC) No 1407/2002 of 23 July 2002. In addition, the provisions of Article 88 EC Treaty and Council Regulation (EC) No 659/1999 also apply.

by the Commission for the reference year 2001. In 2004, production aid per employee in the EU was much lower than in previous years as the new Member States, of which Poland has by far the most workers (around 100,000 underground), did not grant production aid, with the exception of Hungary.

Eight Member States[19] granted aid to the coal sector in 2004, including four new Member States: Germany (€ 3 billion), Spain (€ 1.1 billion), France (€ 890 million), Poland (€ 490 million), Hungary (€ 48 million), the United Kingdom (€ 29 million), the Czech Republic (€ 14 million) and Slovenia (€14 million). With regard to Germany, the Commission approved the restructuring plan for the period 2003-2005, which foresees a reduction in total aid from € 3.3 billion in 2003 to € 2.7 billion in 2005. Spain also notified a restructuring plan concerning the period 2003-2005, but the Commission has opened an investigation procedure and has not yet approved the aid measures. For France, aid measures were approved to cover the costs of closure of the last underground mines in France which closed in April 2004. For the United Kingdom, the Commission has approved an investment aid scheme covering the period 2003-2005 which amounted to just under € 90 million.

Broadly-speaking, coal mining in the new Member States is more competitive than in the EU-15 Member States. Poland has by far the largest coal industry and produces far more than the rest of the EU together. The Commission approved a long term restructuring plan aiming as well to deal with inherited liabilities of the past amounting to € 1.5 billion for the period 2004 - 2006. For Hungary, the Commission approved a long term restructuring plan, which contains the granting of production aid, up to 2010 to the value of €255 million. For the Czech Republic, the Commission approved aid measures not related to production but to inherited liabilities of the past up to 2007 amounting to € 74 million.

Table 7: State aid to coal mining, 2000 - 2004

	Yearly average of aid destined to current production (in million €)		Yearly average of aid not destined to current production (in million €)	
	2000 -2002	**2002 - 2004**	2000 -2002	**2002 - 2004**
EU-25	4441	**3980**	3110	**3210**
CZ	-	-	1	**6**
DE	3003	**2498**	1244	**832**
ES	755	**597**	827	**552**
FR	367	**202**	686	**748**
HU	-	-	16	**24**
PL	213	**676**	319	**1013**
SI	-	-	11	**16**
SK	-	-	5	**2**
UK	103	**8**	0	**17**

Note: The Commission has not yet approved the aid to the Spanish coal industry for 2003. Source: DG Energy and Transport

State aid to the steel sector fell dramatically in the EU-15 Member States from an annual average of around €2 billion in the mid-nineties to €58 million in 1998 after which it has

[19] Slovakia reported aid to the coal sector for the period 2000-2003

remained relatively stable. A total of €12 million was awarded in 2004 almost exclusively for environmental purposes. Of the new Member States, the Czech Republic (€177 million in 2003), Slovakia (€74 million) and Poland (€500 million in 2003 though none in 2004) continue to award significant amounts of aid.

1.6. State aid to the shipbuilding sector

The amount of State aid to the shipbuilding sector fell from an annual average of €1127 million for the period 2000-2002 to €688 million for the period 2002-2004. The highest amounts of aid were given to the restructuring of public yards in Spain in 2000 (just over €1 billion). In 2004, an estimated €540 million was granted to the EU-25 shipbuilding sector mainly by Germany (27% of the EU total), Italy (24%) and Poland (22%).

1.7. State aid for horizontal objectives

State aid for horizontal objectives, i.e. aid that is not granted to specific sectors, is usually considered as being targeted to market failures and as being less distortive than sectoral and ad hoc aid. Research and development, safeguarding the environment, energy saving, support to small and medium-sized enterprises, employment creation, the promotion of training and aid for regional economic development are the most prominent horizontal objectives pursued with State aid. Due to data constraints, which the Commission aims to resolve in 2006, this section looks at horizontal objectives in the context of total aid less agriculture, fisheries and transport.

In around half the EU Member States, more than 90% of all the aid awarded in 2004 was for horizontal objectives

On average, aid earmarked for horizontal objectives, accounted for 76% of total aid less agriculture, fisheries and transport in 2004. The four main horizontal objectives were environment and energy saving (25% of total aid), regional economic development (18%), R&D (12%) and SMEs (12%) – see Table 8.

The remaining 24% was aid directed at specific sectors: coal (12%), manufacturing (9%) and services (3%)[20] including aid to rescue and restructure ailing firms. In interpreting these figures, however, it is important to bear in mind that some aid measures can not be quantified (see section 1.1). Another factor that keeps the volume of sectoral and individual aid artificially low is that Commission decisions which follow an unlawful aid procedure[21] tend to refer to aid that was granted up to several years previously and involve ad hoc awards of aid to individual companies. Although the data for all years are adjusted retrospectively when the Commission takes its decision, the overall level is underestimated.

In twelve Member States, more than 90% of all the aid awarded in 2004 was earmarked for horizontal objectives. In another group of Member States (Spain, France and Ireland) the share was around 60% while in several others the share was significantly lower: Hungary (48%), Cyprus (46%), Slovakia (35%), Poland (26%), Portugal (22%) and Malta (8%). The low share of horizontal aid (and thus relatively high share of sectoral aid) in Portugal was due to a large regional aid tax scheme in Madeira. In Ireland, although aid awarded through the

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[20] These percentages exclude those measures with a horizontal objective that are nevertheless earmarked for the manufacturing and services sectors

[21] Such cases are denoted by a 'NN' case number

Irish Corporation Tax[22] has decreased significantly it still accounts for a relatively high share of total aid. France, Germany, Poland and Spain have relatively high shares of aid to the coal sector although the low share of horizontal aid in France is due mostly to the large award of aid to Alstom[23] while in Germany the large guarantee provided as a part of the restructuring package to Bankgesellschaft Berlin AG[24] in 2002 is another important factor. For a number of the new Member States, the disparity can be explained in part by the relatively strong support of several industries (e.g., financial sector, coal and steel) before accession in the context of privatisation or to ensure viability. For example, faced with a general banking crisis, the Czech Republic paid out €2.6 billion in 2002 in the form of guarantees in order to restructure and subsequently privatise several banks. In Cyprus, aid was mainly granted through tax relief under the International Business Enterprises Act (almost 60% of total aid over the period 2000-2003). In Malta, restructuring aid to shipbuilding and the ship repair sector accounted for around 50% of total aid prior to accession. Furthermore, it should be noted that in countries with relatively low overall aid levels, the grant of a single, relatively large ad hoc aid may cause large variations.

Large disparities between Member States in the share of aid awarded to various horizontal objectives

When making comparisons between Member States, it is important to bear in mind that aid measures are classified according to their primary objective at the time the aid was approved and not to the final recipients of the aid. Notwithstanding the measurement difficulties, the data do give an indication as to which horizontal objectives are favoured by each Member State (see Table 8). For example, the share of total aid directed exclusively to research and development in the Netherlands, Finland, Austria, Estonia, Czech Republic and Belgium was more than twice the EU average of 12%. Meanwhile, Sweden (88% of total aid), Denmark (54%), the Netherlands (52%) and Germany (44%) tended to favour environmental and energy saving objectives (EU average 25%). For the Union as a whole, 12% of total aid was made up of measures for which the primary objective was SMEs. In addition, €1.2 billion of aid, 3% of total aid, was directed exclusively at SMEs as a 'secondary' objective. For the most part, the primary objective of these aid measures was R&D. Combining primary and secondary objectives, 39% of aid in Italy was earmarked exclusively for small and medium-sized enterprises, 38% in Belgium and 34% in the United Kingdom compared with an EU average of 15%.

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22 The rate of corporation tax in Ireland has been cut progressively in recent years and is 12.5% from 2003. This has reduced the comparative value of the preferential 10% rate to the manufacturing sector, therefore contributing to the decline, in monetary terms, of aid to this sector.

23 C58/2003

24 C28/2002

Table 8: State aid for horizontal objectives and sectoral aid, 2004

Percentage of total aid less agriculture, fisheries and transport

	Horizontal Objectives	R&D	Environment and energy saving	SME	Employment aid	Training aid	Regional development n.e.c. (1)	Other horizontal objectives	**Sectoral aid** (2)	Coal	Manufacturing	Services	**Total aid less agriculture, fisheries and transport in million €**
EU-25	**76**	12	25	12	4	3	18	3	**24**	12	8	3	**45.461**
BE	**100**	25	2	33	4	8	23	4	**0**	0	0	0	**685**
CZ	**82**	33	2	10	0	0	36	0	**18**	8	0	10	**165**
DK	**97**	1	54	0	38	0	0	3	**3**	0	3	0	**1003**
DE	**78**	11	44	3	1	0	18	1	**22**	20	1	1	**15128**
EE	**100**	21	1	3	0	0	31	44	**0**	0	0	0	**8**
EL	**97**	2	8	12	4	0	67	5	**3**	0	2	0	**330**
ES	**62**	13	3	12	1	1	31	1	**38**	35	2	0	**3136**
FR	**59**	15	2	19	4	1	14	4	**41**	14	25	2	**6348**
IE	**62**	10	2	3	12	3	20	12	**38**	0	27	11	**393**
IT	**95**	18	1	34	7	13	20	4	**5**	0	3	2	**5415**
CY	**46**	2	1	1	0	5	5	32	**54**	0	37	3	**131**
LV	**100**	0	0	8	0	0	92	0	**0**	0	0	0	**17**
LT	**49**	2	0	12	0	0	34	1	**51**	0	35	0	**23**
LU	**100**	19	0	21	0	0	31	30	**0**	0	0	0	**43**
HU	**45**	2	0	4	1	0	26	10	**55**	7	48	1	**696**
MT	**8**	0	0	3	0	1	0	4	**92**	0	92	0	**117**
NL	**96**	25	52	14	1	0	4	1	**4**	0	4	0	**854**
AT	**96**	28	18	23	5	6	13	3	**4**	0	3	1	**524**
PL	**26**	1	1	0	13	0	10	0	**74**	25	48	0	**1972**
PT	**22**	3	0	8	1	4	5	0	**78**	0	0	78	**1114**
SI	**70**	18	19	2	17	3	6	5	**30**	10	17	0	**137**
SK	**35**	0	0	0	0	2	32	1	**65**	0	65	0	**207**
FI	**98**	25	38	8	6	0	15	6	**2**	0	0	2	**571**
SE	**100**	4	88	1	0	0	3	5	**0**	0	0	0	**2231**
UK	**99**	16	27	22	0	5	26	3	**1**	1	0	0	**4211**

(1) Aid for general regional development not elsewhere classified. (2) Aid for specific sectors awarded under measures for which there was no horizontal objective as well as aid for rescue and restructuring. Figures under sectoral aid also include aid to other non-manufacturing sectors not included in the table. Source: DG Competition.

1.8. Trend in State aid for horizontal objectives

In the mid-1990s, when State aid levels were much higher, the share of total aid granted for horizontal objectives was around 50%. In line with the commitments undertaken at the various European Councils, Member States have however continued to redirect aid towards such horizontal objectives. The share of horizontal objectives in total aid increased by 4 percentage points (+7 points for the EU-15 Member States) between 2000-2002 and 2002-2004. This upward trend was almost exclusively the result of a significant increase in aid for environmental and energy saving objectives (+6 points) as well as a reduction in sectoral aid, particularly coal, for some Member States.

The positive trend was observed, to varying degrees, in the majority of Member States, particularly in Ireland (+16 points), Spain (+14 points) and the United Kingdom (+11 points). In contrast, the share in Poland went down considerably due to the large amount of aid awarded to the coal sector in 2003.

Over the period under review, there were appreciable increases in the share of total aid for environmental and energy saving objectives in Sweden (+41 points), Finland (+16 points), the United Kingdom (+14 points) and Germany (+10 points) - see special focus in Part Two and in particular Tables 12 and 13. For the Union as a whole, there was no significant change in the share of aid for other horizontal objectives such as R&D and SMEs. However, expenditure patterns have changed in some Member States. For example, in the UK the share of aid directed at SMEs increased significantly.

1.8.1. State aid for research and development (R&D)

Investment in R&D is a crucial factor to make the EU economy competitive and to ensure sustainable growth. The Barcelona European Council of March 2002 recognised this by setting the objective for expenditure on R&D to 3% of GDP by 2010. In addition, two thirds of this expenditure should be funded by the private sector. Following this, the spring 2004 European Council stressed in particular that besides public funding, increased private funding of investment is crucial to achieve a sustainable level of 3% and accorded priority status to the strengthening of business investment in R&D.

National governments have a range of measures to choose from to fund and consequently trigger R&D, the exact range and balance of which depend on the national context and form the policy mix. These public measures, when granted on a selective basis, might contain State aid. Even though State aid constitutes only a small part of public R&D funding, competition could be distorted by favouring some enterprises over others. On the other hand, state aid may in certain circumstances be the best available option to provide incentives triggering additional private R&D investment. The Commission thus tries to strike a balance through the application of the framework on R&D aid thereby ensuring that R&D is furthered to the largest extent while minimising distortions of competition as far as possible.

Figures for 2003 show that investment in R&D is not sufficient to meet the Barcelona objectives: for the Union as a whole, R&D investment stood at 1.9% of GDP, Sweden and Finland being the only countries to reach the 3% level with 4.0 and 3.5% respectively. Drawing conclusions from the so far sluggish development of R&D investment, it is clear that with growth remaining at the current level, the European economy will not achieve the Barcelona targets by 2010. Rather, growth needs to be accelerated and new impetus given to investment in R&D.

As regards (potentially) distortive State aid to R&D, total expenditure stood at €5.5 billion in 2004. After a significant increase in 2001, the level of R&D aid has remained rather stable. State aid to R&D represents a relatively small share in public funding (EU-wide, 0.05% of GDP in 2004) although there are significant differences between Member States. With the exception of Slovenia and Czech Republic, the share of aid directed at R&D in the ten new Member States is comparatively low.

Table 9: State aid for research and development (R&D)

	Aid to Research & Development (in million €), 2004	Share of R&D aid in total aid, annual average 2002-2004	Share of R&D aid in total aid (% point difference 2000-2002 and 2002-2004)	Share of R&D aid to GDP (in %), 2004
EU-25	5553,4	12	0,4	0,05
BE	173,7	22	5,4	0,06
CZ	54,9	3	1,0	0,06
DK	13,6	2	-2,7	0,01
DE	1595,2	10	0,6	0,07
EE	1,8	20	10,7	0,02
EL	5,7	1	1,1	0,00
ES	403,9	11	3,2	0,05
FR	958,0	19	-1,4	0,06
IE	39,3	10	6,0	0,03
IT	951,6	15	0,6	0,07
CY	3,2	1	0,3	0,03
LV	-	-	-	-
LT	0,5	1	0,0	0,00
LU	8,1	13	-2,3	0,03
HU	13,1	2	-1,3	0,02
MT	-	-	-	-
NL	217,2	28	2,0	0,05
AT	147,2	33	-2,3	0,06
PL	25,2	1	-1,1	0,01
PT	33,3	2	1,3	0,02
SI	24,3	21	6,4	0,09
SK	0,8	2	-3,4	0,00
FI	144,7	29	-4,5	0,10
SE	82,6	6	-13,2	0,03
UK	655,8	21	-2,1	0,04

Source: DG Competition.

1.9. State aid supporting regional development and cohesion

Each Member State targets part of its State aid towards the least developed regions, the so-called 'assisted regions'. For the Union as a whole, an estimated €12.3 billion of aid[25] was earmarked exclusively for assisted 'a' regions[26] in 2004. The discrepancy with the figure

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25 This figure includes all aid specifically earmarked for assisted 'a' regions regardless of the overall objective of the aid. However, due to an absence of data on the final beneficiaries of the aid, it is not possible to quantify the amount of aid granted through nation-wide schemes from which assisted regions will also clearly benefit. See spring 2003 update of the Scoreboard for further information on methodological issues.

26 Article 87(3)(a) provides that aid "to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment" may be considered compatible with the common market. The 'a' regions are largely identical to the Objective 1 regions under the EU Structural Funds.

published in previous Scoreboards is due to enlargement. With the exception of Cyprus, and the cities of Prague and Bratislava which qualify for assistance at ‘c’ level[27], the entire territories of the ten new Member States are eligible at ‘a’ level. Although a number of aid measures in these countries are not earmarked for a specific region, the aid is thus deemed to be ‘reserved for’ assisted regions.

The EU-wide figure of €12.3 billion represented 27% of total aid (less agriculture, fisheries and transport for which a regional breakdown is not available). Disparities between the Member States in the levels of aid reserved for assisted ‘a’ regions (Table 10) reflect not only differences in regional policy but also the size of each country’s eligible population as well as the extent to which each Member State grants aid at a sub-central level.

Table 10: State aid specifically earmarked for assisted ‘a’ regions, 2004

	Total state aid less agriculture, fisheries and transport, mio €	Aid for assisted 'a' regions, mio €	Aid for assisted 'a' regions as a percentage of total aid less agriculture, fisheries and transport
EU-25	45.461	12.339	27
CZ	165	92	56
DE	15.128	3.040	20
EE	8	8	100
GR	330	330	100
ES	3.136	1.210	39
FR	6.348	853	13
IE	393	345	88
IT	5.415	2.151	40
LV	17	17	100
LT	23	23	100
HU	696	696	100
MT	117	117	100
AT	577	21	4
PL	1.972	1.972	100
PT	1.114	953	85
SI	137	137	100
SK	207	143	69
FI	571	4	1
UK	4.211	266	6

Note: There are no assisted ‘a’ regions in B, DK, L, NL and S. For CZ, ES, IE, PT, SK, all measures qualify for either ‘a’ or ‘c’ status. The figures in the table above refer to those measures which were specifically earmarked for ‘a’ regions. In Cyprus, all measures qualify for ‘c’ assisted status. All data exclude agriculture, fisheries and transport for which a regional breakdown is not available. It is therefore not possible to measure aid to assisted ‘a’ regions as a proportion of total State aid. Source: DG Competition.

[27] Article 87(3)(c)

1.10. Aid awarded under the block exemption regulations

With a view to reducing the administrative burden for specific types of aid, block exemptions for aid to SMEs, training aid, employment aid, certain types of aid in the fisheries sector and aid to SMEs in the agricultural sector have come into force over the past few years.[28] As one would expect, the number of notifications for these types of aid has fallen as Member States make increasing use of the possibilities offered by the block exemption regulations. By the end of 2004, more than 800 information sheets had been submitted (Table 11). Almost two-thirds of the exempted measures concerned aid for SMEs. Five Member States, Italy (26% of the total), the United Kingdom (22%), Germany (11%), Spain (8%) and Belgium (7%) accounted for 75% of all exempted measures in 2004.

Table 11: Trend in the number of aid measures submitted under the block exemption regulations

Type of block exemption regulation	Year				
	2001	2002	2003	2004	Total
SME	101	124	139	150	514
Training	48	81	53	79	261
Employment	0	0	8	21	29
Total number	149	205	200	250	804

Figures exclude cases withdrawn and cases submitted under the block exemption regulation for fisheries (1 in 2004) and agriculture (72 in 2004). Source: DG Competition.

As regards expenditure, an estimated €3.4 billion was awarded in 2004 under the three block exemption regulations. This represents around 10% of all aid directed at horizontal objectives though for several Member States the share was considerably higher: Belgium 14%, Greece 16%, Poland 21%, United Kingdom 22% and Italy 31%.

The overall figure of €3.4 billion was made up of €2.1 billion to SMEs, €1.1 billion to training aid and €0.2 billion for employment aid.

1.11. State aid instruments

Majority of Member States tend to provide aid to manufacturing and services in the form of grants …

All State aid represents a cost or a loss of revenue to the public authorities and a benefit to recipients. However, in some cases the actual aid element may differ from the nominal amount as in the case of a subsidised loan or guarantee.

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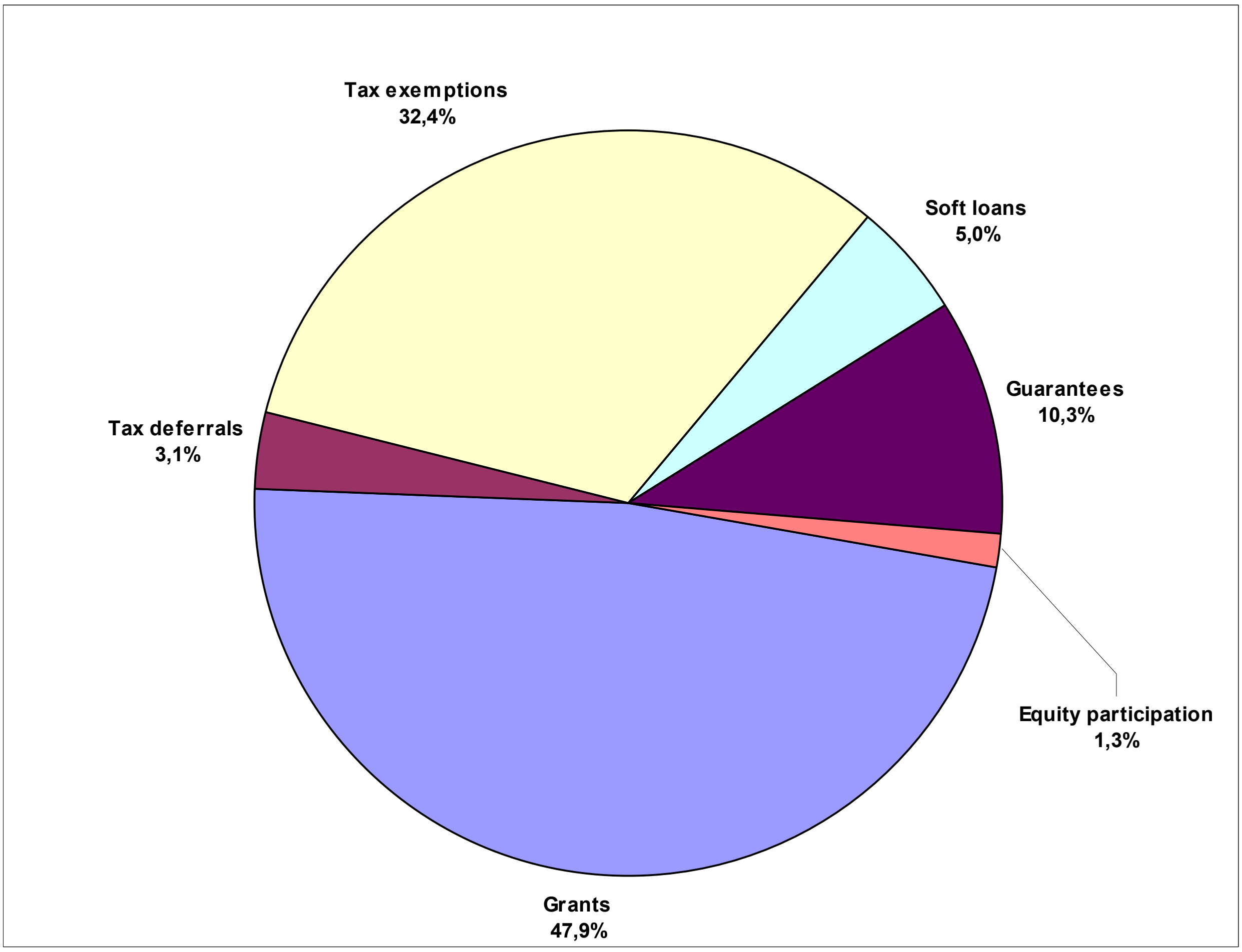
28 Commission Regulations (EC) No 70/2001 of 12 January 2001 on State aid to SMEs (OJ L 10, 13.01.2001, pages 33-42); No 68/2001 of 12 January 2001 on training aid (OJ L 10, 13.01.2001, pages 20-29); No 2204/2002 of 5 December 2002 on State aid for employment (OJ L 337, 13.12.2002, pages 3-14). No 1/2004 of 23 December 2003 on State aid to SMEs in the agricultural sector (OJ L 1, 03.01.2004, pages 1-16).

Graph 2: Share of each aid instrument in total aid for manufacturing and services, EU-25, 2002 – 2004



Note: This section on aid instruments excludes the coal sector. Source: DG Competition

… though significant differences still exist in the use of instruments

During the period 2002-2004, grants accounted for just under 50% of total aid in the manufacturing and service sectors. In addition to aid awarded through the budget, other aid is paid through alleviation from the tax or social security system. Tax exemptions made up 32% of the total (Graph 2). While Belgium, Denmark, Estonia, Luxembourg and Austria provided at least 85% of their aid in the form of grants, other Member States tended to make greater use of tax exemptions: accounting for 75% or more of total aid in Cyprus, Lithuania, Portugal and Slovakia. A similar instrument is a tax deferral which was used by just under half the Member States during the period under review. Tax deferrals accounted for 19% of all aid in Italy compared with an EU average of 3%.

There are other forms of aid instrument which vary from one Member State to another. One such category covers transfers in which the aid element is the interest saved by the recipient during the period for which the capital transferred is at his disposal. The financial transfer takes the form of a soft loan or tax deferral. The aid elements in this category are much lower than the capital values of the transfers. EU-wide, soft loans represented around 6% of all aid to manufacturing and services. In Finland, France, Malta and the United Kingdom the proportion was 10% or more.

Aid may also be in the form of state equity participation which represented around 1% of all aid to the manufacturing and service sectors. Finally, aid may be provided in the form of guarantees. The aid elements are generally much lower than the nominal amounts guaranteed, since they correspond to the benefit which the recipient receives free of charge or at lower than market rate if a premium is paid to cover the risk. EU-wide, guarantees made up 10% of total aid. During the period under review, large guarantees were awarded in particular to the banking sectors in Germany (18% of total aid) and Czech Republic (80% of total aid).

2. PART TWO: SPECIAL FOCUS ON STATE AID FOR THE ENVIRONMENT AND ENERGY SAVING

Introduction

The earth's ability to absorb pollution and continue providing natural resources is limited. Protecting the environment is crucial for the quality of life of current and future generations. Although the EU's primary goals were economic development and free trade, environmental aspects have also been taken into account. Environmental action by the Community began in 1972 with four successive action programmes. In 1993, environmental protection became a recognised policy as part of the Treaty on European Union. Furthermore, the Treaty of Amsterdam (which entered into force 1999) recognized the principle of sustainable development as one of the EU's aims.

Competition policy also recognised the importance of environmental policy at an early stage – the first rules on granting State aid for environmental purposes were established in 1974[29]. Initially, aid could be authorized mainly to help undertakings to make necessary investments to achieve certain mandatory minimum standards. The evolution of environmental State aid policy has limited this kind of aid in order to introduce the 'polluter pays principle', which requires that economic agents must bear the full cost of the pollution caused by their activities.

2.1.1. Policy context and rationale for environmental and energy policy

Environmental policy

The legal basis for EU environmental policy is laid down in Articles 6 and 174-176 of the EC Treaty. Article 174 establishes four main objectives of the Union policy on the environment: preserving, protecting and improving the quality of the environment; protecting human health; prudent and rational utilisation of natural resources; and promoting measures at international level to deal with regional or worldwide environmental problems. In order to achieve these objectives, the EU has introduced Environmental Action Programmes. The 6th programme, entitled *Environment 2010: Our Future, Our Choice*[30] covers the period 2001 to 2010 and identifies four environmental areas to be tackled for improvements: Climate change, Nature and biodiversity, Environment and health and quality of life, and Natural resources and

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29 Commission memorandum on State aid in environmental matters. SEC(74) 4264 of 6 November 1974.

30 Decision No 1600/2002/EC of the European Parliament and of the Council of 22 July 2002 laying down the Sixth Community Environment Action Programme was published in OJ L 242 of 10.9.2002

waste.The key priority for the Sixth Environmental Action Programme is the implementation of the Kyoto Protocol to cut greenhouse gas emissions by 8% below 1990 levels by 2008-2012. The Programme identifies the system of trading of emission allowances ("emission *trading"*) as one of the appropriate instruments to meet this target. The programme stresses the importance of protecting the nature and bio-diversity, which are under the risk due to the pollution, unsustainable use of the land and sea.

Lisbon Strategy and Environmental Policy

Beyond the above improvements, environmental policy can also contribute to economic development. Environmental policy and eco-innovation are an essential part of the Lisbon Strategy because they can promote sustainable economic growth, maintain and create jobs, and contribute to the long-term competitiveness of the EU economy. Based on the Lisbon mid-term review 'package', the March 2005 Summit concluded that appropriate resources - including cohesion policy - must be mobilised to a greater degree in the Strategy's three dimensions (economic, social and environmental) and synergies must be developed. The June 2005 Summit then approved a set of Integrated Guidelines for Growth and Jobs 2005-2008 which include a specific guideline (number 11) on the environment[31].

Implementation of policy by Member States

Although EU legislation has done much to improve environmental quality, to create a level playing field for companies across the EU, and to help promote new market opportunities, there is still room for improvement. Full implementation of the EU environmental legislation by Member States remains a challenge, including in the new Member States. By the end of 2004, environment cases accounted for one quarter of all open cases for non implementation of EU law. The Commission services analysed the main areas of difficulty (waste, water, air, nature protection and environmental impact assessment) and are now drawing up action plans aimed at improving implementation of environmental community law.

EU Energy Policy

The objective of the European Union's energy policy is to ensure a supply of energy to all consumers at affordable prices while respecting the environment and promoting healthy competition on the European energy market. A sustainable energy policy aims at reducing harmful emissions, mainly NO_X, SO_X and CO_2, which are emitted every time fossil fuels are burnt, and at reducing the dependency of the European Union on energy imports. The angle of attack the Commission proposes is twofold: first, it proposes to reduce the overall energy consumption; second, it aims at producing as much energy as possible from renewable energy sources.

In 2005, the Commission adopted a Green paper on Energy efficiency, which describes possible courses of action towards a reduction of the overall energy consumption. At the same time, different legislative acts have already started to implement that aim, either by imposing energy-efficient standards (e.g., for buildings, cars and electronic appliances), or by giving

31 Integrated Guidelines For Growth And Jobs (2005–2008), Communication to the Spring European Council Working Together for Growth and Jobs, http://europa.eu.int/growthandjobs/index_en.htm

economic incentives for less energy-intensive production and thus also reduced environmental impacts (e.g., directive on energy taxation,[32] directive on emission trading[33]).

As far as the promotion of renewable energy is concerned, the Community has set itself ambitious targets for the production of electricity from renewable energy sources (directive 2001/77/EC) and from combined heat and power (directive 2004/8/EC). The energy taxation directive foresees the promotion of biofuels through lower taxation, and the Commission is planning to present an action plan on biomass.

2.1.2. Environmental measures – when do they constitute State aid?

Member States have introduced a wide range of national environmental policy measures to protect the environment: to limit pollution (air, water and soil), protect natural resources, promote renewable energy resources, manage waste etc. Most of these objectives are targeted through general measures, i.e. applied throughout a particular country without regional or sectoral selectivity. However, there are also environmental measures or exemptions from general measures (e.g., environmental tax relief) which favour certain companies or the production of certain goods. Such selective measures may distort competition between companies and it is therefore important that the benefits of environmental protection measures are well balanced with the distortion of competition they cause.

EU State aid policy is aimed at avoiding disproportionate State support measures which unduly distort competition. Member States are required to notify to the Commission all State aid measures before putting them into effect. The Commission analyses State support measures in two steps: 1) whether the measure constitutes State aid within the meaning of Article 87(1) of the EC Treaty, and if yes, 2) whether such potential distortion of competition is justified and balanced. If the aid is justified and compatible with common market and the distortion of competition is marginal, the Commission approves the aid measure.

As any measure imputable to public authorities, an environmental support measure is considered to be a State aid measure as defined under Article 87(1) of the EC Treaty if it fulfils all the following four criteria[34]:

- Transfer of state resources
- Advantage for the undertaking
- Selectivity
- Distortion to competition and effect on trade between Member States

In some instances, the interpretation as to whether one or other criteria is fulfilled and thus whether or not the measure constitutes State aid is difficult and complex. Some examples relevant for environmental measures are given below.

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32 Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity

33 Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003 establishing a scheme for greenhouse gas emission allowance trading within the Community and amending Council Directive 96/61/EC

34 See explanation 'What is a State aid' in State aid Scoreboard Spring 2004 update, COM(2004) 256 final

Transfer of state resources includes grants from the central, regional or local government's budget, revenue forgone i.e. environmental tax relief or government authorities selling (buying) environment related goods and services or land below (above) market price. Transfer of state resources criteria is also fulfilled in case of a fund which is set up by the State and which is financed by contributions imposed and managed by the State. For example, the Netherlands set up two measures called MEP (*Milieukwaliteit van de Electriciteits Productie*) to support Dutch producers of renewable electricity[35] and of combined heat and power (CHP)[36]. As the measures were financed through a compulsory contribution by all electricity consumers in the form of an increased connection fee and the contributions were collected to the state established fund, the Commission decided that the measures constitute State resources in the light of Article 87(1) and therefore the measures were considered to be State aid for Dutch energy producers.

In the PreussenElektra case[37], the Court of Justice decided that to the extent that the German law imposed on private electricity distributors to pay a higher feed-in price for electricity generated from renewable sources, it does not involve transfer of State resources. The crucial element for the Court appeared to have been that the German electricity pricing system required private companies to pay other companies a higher price for renewable electricity, so the resources involved were coming from private companies. There was no State body or fund established by the State to collect and redistribute the benefits as it was in the above-mentioned Dutch case promoting renewable electricity and combined heat and power measure.

The Commission considers also the emission trading instruments such as quotas, allowances, certificates and credits to be intangible assets for recipients if they are tradable in the market. When the State on its own initiative allocates such assets free of charge, the allocation can constitute State aid. For the first trading period (2005-2007), the emission trading scheme (ETS)[38] obliges Member States to allocate at least 95% of the allowances free of charge. Thus, Member States can sell at maximum 5% of the allowances at market price. If the Member State does not use this possibility and hands over also the 5% of allowances to the companies free of charge, then it is considered as State revenue forgone and therefore it might constitute State aid.[39]

Most environmental support measures constitute also an **advantage for the undertaking**, but in some cases the Commission has found that there is no advantage. For instance, in the Netherlands case *Waste disposal system for car wrecks*[40], the Commission found that there is no economic advantage for the companies and therefore no State aid. The aim of the waste management system is to ensure that the companies that produce and sell cars also take the responsibility for a high degree of recycling of car wrecks. This measure corresponds to the polluter pays principle. Dutch government has declared that all car producers and importers have to pay charge for each car which is registered in the Netherlands. The resources are paid to car dismantling companies. As the charge for car producers and importers and premiums to

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35 MEP Stimulating Renewable Energy, N707/2002.

36 MEP Stimulating combined heat and power production (CHP), N 708/2002.

37 Case C-379/98 *Preussen Elektra AG v Schleswag AG*.

38 Directive 2003/87/EC of the European Parliament and of the Council of 13 October 2003

39 See National allocation plans for Emissions trading: http://www.europa.eu.int/comm/environment/climat/emission_plans.htm

40 *Waste disposal system for car wrecks* C11/2001 (ex N629/2000)

the dismantling companies are corresponding to the cost of recycling, the Commission found that there is no advantage and State aid for car producers nor for car dismantling companies.

Generally it is recommended to avoid **discrimination and selectivity** in state support measures, so that they can be considered as general measures and not as State aid measures. One contrary example is the Adria-Wien Pipeline GmbH case[41] concerning an Austrian legislative measure, which provides tax exemptions from energy taxes on natural gas and electricity. Although the measure was established in the context of an overall package of measures to consolidate the budget, and exemptions were based on objective automatic criteria without the administrative authorities having any discretionary power in selecting the beneficiaries, and the measure gave benefits for a very large number of undertakings, the Court of Justice found that the measure is selective. One of the main reasons for this conclusion was that the tax exemption is applied only for undertakings whose activity is mainly in the manufacturing sector. The Court of Justice found that the ecological considerations underlying the national legislation does not justify treating the consumption of natural gas or electricity by undertakings supplying services differently than the consumption of such energy by undertakings manufacturing goods, the damage to the environment is the same. The Court stated that undertakings in the services sector may, just like undertakings in the manufacturing sector, be major consumers of energy and incur high level of energy taxes and therefore they are in disadvantaged position. Based on these arguments the Court of Justice regarded these measures to be selective and to be state aid within the meaning of the Article 87(1) of the EC Treaty.

2.1.3. Market failure and justification for environmental State aid

In some instances, markets do not lead to an efficient solution, for example, in the case of negative externalities such as pollution. Such negative externalities arise when undertakings do not take into account in their production decisions the full cost of the action such as nuisance or harm to others. From the society's point of view, it is desirable to internalize such externalities, i.e. to make the price of goods reflect the real production costs, including the costs of damage to environment. Classical examples of measures to internalize externalities are environmental standards or environmental taxes. If the price of goods is increased thanks to such measures, then most probably the production and consumption of environmentally unfriendly goods and also pollution would decrease.

Member States have various possibilities to remedy the market failures. The first and most favoured one should be the use of general measures that do not constitute State aid and distort competition. If this is not possible, Member States may develop State aid measures, which are in compliance with the internal market and can be approved by the Commission. The above-mentioned prohibition to grant State aid, established by the Article 87(1), is not absolute because Articles 87(2) and (3) provide exemptions under which the granting of State aid is justified. The Commission assesses the justification and the compatibility of national environmental aid measures according to the Community Guidelines on State Aid to Environment (hereafter the 'Environmental Guidelines')[42].

The Environmental guidelines recognize two main instances where State aid may be justified. Firstly, temporary aid to help internalisation of costs. As mentioned above, the internalisation

[41] Case C-143/99

[42] Community Guidelines on State Aid for Environmental Protection, *OJ C 37, 03.02.2001, p. 3-15*

of the cost of pollution is mainly done by the introduction of environmental taxes, Emission Trading Schemes or by environmental standards. However, some undertakings, in particular SMEs, may not be able to bear the extra financial burden (environmental tax or increased investment cost to apply the standards) immediately. Therefore, the guidelines justify granting aid to SMEs in order to adapt to new Community environmental standards, for a period of 3 years from the adoption of such standards. Secondly, the Environmental guidelines foresee the possibility to grant aid to encourage undertakings to make investments to reach higher environmental standards than community standards or to undertake further investment to reduce pollution from their plants or for the development of renewable energy sources.

The guidelines also allow operating aid for specific purposes. If a Member State has introduced a high level of environmental taxes in the absence of Community harmonised tax or of a level higher than the tax envisaged by the Community legislation, then, under certain conditions ensuring an environmental counterpart, guidelines justify the awarding of environmental tax exemptions for companies for a maximum of 10 years. For further available options, see box below.

Brief summary of the Community Guidelines on State aid for Environmental Protection

The compatibility of State aid for environmental protection and energy is governed by Community Guidelines on State Aid for Environmental Protection (*OJ C 37, 03.02.2001, p. 3-15).*

Under the Environmental Guidelines Members States may, after Commission approval, grant aid for actions designed to remedy or prevent damage to our physical surroundings or natural resources or to encourage the efficient use of these resources.

The following categories of State aid are justified:

Aid for investment to adapt to new compulsory EU environmental standards or to improve on such standards

In accordance with the polluter pays principle, the Commission takes the view that aid is no longer justified in the case of investments designed to bring companies into line with new Community standards.

However, in order to address the special difficulties encountered by SMEs, it remains possible to grant them aid for adapting to new Community standards, for a period of 3 years from the adoption of such standards. Such aid may be authorized up to a maximum of 15% of eligible costs.

Investment aid may also be authorized to enable firms to improve on the Community standards, or where firms undertake investments in the absence of mandatory standards, or where they have to comply with national standards that are more stringent than the Community standards applicable. In these cases, aid may be authorised up to 30% of the eligible costs. The eligible costs must be strictly limited to the extra costs of the investments in land, buildings, equipment and intangible assets necessary to achieve the new compulsory standards and/or to meet the environmental objectives. In all cases, the eligible costs must be calculated net of the benefits accruing from any increase in capacity, cost savings engendered during the first five years of the life of the investment and additional ancillary production during that five-year period.

Aid for investment in energy saving, in renewable sources of energy and in combined heat and power installations (CHP)

The Guidelines give the Member States the possibility to grant investment aid and operating aid. Member States may grant aid to promote investments concerning renewable energy, up to 40% of the eligible costs. On the top of that, bonus of 10% may be granted to SMEs, firms located in assisted regions, and for energy installations serving all the needs of an entire community such an island.

Member States may also grant operating aid, provided it covers strictly the difference between the costs of production from renewable energy sources and the market price of that energy (i.e. does not result in overcompensation of renewable energy sources), according to 4 options:

Option 1: The aid may compensate for the difference between the production cost and the market price until the total depreciation of the plant. The aid can also cover a fair return on capital if necessary.

Option 2: Member States can also grant support by using market mechanisms such as green certificates or tendering supports.

Option 3: They can also choose to grant operating aid on the basis of the external costs avoided.

Option 4: Operating aid can be granted according the general rules for operation aid: aid for a period limited to 5 years, and in principle, "degressive".

Further general conditions on granting operating aid are described below.

Aid for the rehabilitation of polluted industrial sites

If the person responsible for the pollution is not identified or cannot be made to bear the cost, the person responsible for the rehabilitation of the land may receive aid. The eligible costs are equal to the cost of the work to repair the environmental damage less the increase in the value of the land.

Aid for the relocation of firms

Aid for the relocation of companies can be granted only if the change of location is dictated on environmental protection grounds and if it is ordered by administrative or judicial decision. In addition, the undertaking relocating must comply with the strictest environmental standards applicable in its new location. The eligible costs should be limited to the net costs of the relocation.

Operating aid

Under the Community Guidelines on State aid for environmental protection, Member States can also provide operating aid in cases where such aid is shown to make a significant contribution to protecting the environment.

The following types of operating aid may be authorised under the Guidelines:

- Operating aid to promote environmentally-friendly forms of waste management and to promoteergy saving;

- Operating aid in the form of reductions of or exemptions from taxes levied on certain activities for reasons of environmental protection (e.g. CO_2 levy);

- Operating aid to promote renewable energy sources;

- Operating aid for the combined production of electric power and heat.

Specific conditions to be respected when granting operating aid in the environmental field are set out in detail in points 42 to 67 of the Community Guidelines on State aid for environmental protection.

The eligible costs are strictly limited to the extra production costs by comparison with the market prices of the relevant products or services.

Operating aid is in principle limited to a duration of 5 years. Where the aid is "degressive", its intensity may amount to 100% of the eligible costs**.** Where the aid is "non-degressive" the intensity must be limited to 50% of the eligible costs.

For operating aid in the form of tax reductions or exemptions, specific criteria apply for new taxes and existing taxes.

2.1.4. Environmental State aid measures

Despite the need for control, in the light of the defined environmental objectives and certain market failures set out above, the Commission has traditionally adopted a rather favourable approach to aid for environmental protection. These kinds of environmental measures are normally granted in the form of schemes, not as individual aid. Certain types of environmental measures are considered to be less distortive of competition since they are undertaken in an area of Community interest. The objective of such schemes can, for example, be to support renewable energy, energy efficiency or waste management. These measures must be notified to the Commission, but are normally covered by the Community Guidelines on State aid for environmental protection. If they comply with these guidelines, which amongst others sets out limits on the aid, they can be approved under Article 87(3)(c) of the EC Treaty. In the text below, some examples of such support measures are given.

Environmental and energy measures qualifying as compatible State aid: Case studies

Support measures for renewable energy, for energy-saving, for waste management, for rehabilitation of polluted industrial sites and for improvement of production processes normally are considered to be in the interest of the Community. Relief from environmental taxes can also be of Community interest, as such taxes may not be introduced, in particular on energy-intensive companies, if no relief is allowed.

Renewable energy

In, for example, the Netherlands, the production of electricity from renewable energy sources is amongst others stimulated by a feed-in tariff[43]. The measure aims at stimulating demand for renewable energy resulting in an increase in consumption and production of renewable energy. This will contribute to the achievement of the national targets for the reduction of CO_2 emission as agreed in the Kyoto Protocol to the United Nations Framework Convention on Climate Change. The publicly owned operator of the national high-voltage grid is given the task of distributing subsidies to the producers of renewable energy. The subsidies for electricity produced from renewable energy compensates for the difference between the production cost of electricity produced from renewable energy sources and the market price of conventional electricity. The level of subsidy varies for the different forms of renewable electricity generation based on the difference of the production costs of the specific form of renewable energy (wind, solar etc) and the electricity market price of conventional electricity. The subsidy is capped at € 0.07 per kWh and is financed through a compulsory contribution by the electricity consumers, imposed by legislation. The fees, which are collected by the network controllers, are transferred each month to the grid operator, who keeps the money separately in a current account. The Commission considered that the measure constitutes State aid within the meaning of Article 87(1). The measure was found to be in line with the Environmental guidelines (in particular point 59). As the objective of the measure clearly is in the interest of the Community and there is no over-compensation, the measure was found to be compatible with the common market in accordance with Article 87(3)(c).

Energy-saving

In Spain, support[44] to promote investments in renewable energy and energy efficiency has been provided since 2001. The objective of the support is among others to achieve a contribution from

[43] N 760/95, OJ C 70, 8.3.1996, p. 6

[44] State aid No. N 188/2005 (not yet published in the OJ). That measure replaces, modifies and prolongs State aid No. N 459/2001, not yet published in the OJ, N 460/2001, not yet published in the OJ, and N 198/2002, OJ C 65, 19.3.2003, p. 23

renewable energy sources of 12 % of the demand of primary energy in 2010 and a reduction of the energy intensity by 7.2 % in 2012. As a consequence of the scheme, a reduction of 300 000 tonnes per year of CO_2 emissions is expected. Aid is provided in the form of a direct grant. Under the scheme, investments in renewable energy can receive support of between 10 and 30 % of the reference costs, while investments in energy efficiency can receive support of 40 % of the reference costs. The maximum gross aid intensity is in all cases limited to 40 % of the eligible costs (plus a regional bonus of 5 % or 10 % in certain eligible regions and a bonus of 10 % for SMEs). Eligible investments in energy efficiency can, for example, be investments in better energy saving and substitution of energy in the industry, investments in energy efficiency in buildings, energy efficiency in the public sector and public transport, non-industrial cogeneration and reuse of residuals as energy. The Commission found that the measure constitutes State aid which is compatible with the common market since it is in line with the Environmental guidelines (in particular points 30, 32, 36 and 37).

Waste management

In 2002, the French government introduced an aid scheme for the elimination of dangerous waste for the water[45]. The objective of the scheme is to preserve the water resources by promoting the elimination of waste that can pollute the subsurface and surface water or disturb the functioning of municipal purification plants. In order to achieve that objective, the scheme aims at orienting the waste pollutants, which are normally put in a disposal, in the relevant elimination procedures, successful at the technical level and optimal at the environmental level. The aid is provided to enterprises that produce the waste, when these enterprises treat the waste in appropriate procedures in order to significantly reduce the potential pollutant. It is granted in the form of grants which are calculated on the basis of the difference between the cost of the treatment of the waste in the dedicated procedure and the cost of elimination of the same waste by disposal. Each beneficiary can benefit from the aid for maximum 5 years, either as a fixed level of 50 % during that period or at an aid level which is degressive in a linear manner from 100 % to 0 % during the 5 year period. The scheme was found to be in line with the Environmental guidelines (particularly points 42 to 46). Since the scheme is covered by the Environmental guidelines and does not lead to over-compensation, the Commission approved the scheme on the basis of Article 87(3)(c).

Rehabilitation of polluted industrial sites

In May 2002, the Austrian government introduced a scheme with the objective to support the clean up and rehabilitation of polluted industrial sites[46]. The investment aid is provided in the form of grants. Aid under the scheme may amount to up to 100 % of the eligible costs, plus 15 % of the cost of the work. Eligible costs under the scheme will always be directly linked to the rehabilitation and safeguarding (including planning, etc) of polluted industrial sites. The eligible costs are equal to the cost of the work less the increase in the value of the land. Since the scheme is in line with point 38 of the Environmental guidelines and does not lead to over-compensation, the Commission approved the scheme on the basis of Article 87(3)(c).

Investment aid to improve production processes

In Germany, a measure promoting investments to create new methods of production which have special environment relevance was introduced in 2003[47]. The measure aims at resources-preservation and creation of more efficient production processes as well as a production with less environment-impairing consequences. The scheme focuses on: (1) the introduction of innovative production processes and an efficient use of natural resources and the reduction of emissions and waste, (2) the substitution and avoidance of environment-impairing materials used in the production process, (3)

45 State aid No. N 496/2002, OJ C 108, 7.5.2003, p. 5
46 State aid No. 9/2002, OJ C 164, 10.7.2002, p. 4
47 N 559/2002, OJ C 76, 28.3.2003, p. 27

limiting volatile organic compounds in the production process, (4) pilot projects aiming at reducing of the energy consumption in the production process and (5) innovative plants for the treatment and use of waste. The aid is granted in form of grants or soft loans and is limited to investments aiming to achieve significantly higher levels of environmental protection than is required by current standards. The loans run over a period of 13 years at an interest of 3 % per year. Taking into account the present reference rate of Germany of 5.06% results in an aid intensity of a loan of 13.4% gross. If the market interest changes considerably, the interest rate may be raised up to max 10% per year.The maximum aid intensity is 30% gross of the eligible costs. If the investment is carried out by SMEs, an extra 10% percentage points gross of aid is allowed which then will amount up to a maximum of 40%. Furthermore, in regions which are eligible under Article 87(3)(c), firms may receive additional aid of 5% gross. The eligible costs concerns tangible investments and spending on technology transfer. Eligible costs are only the extra investment costs which are necessary to meet environmental objectives in order to exceed existing mandatory standards. To achieve this, the beneficiaries are obliged to calculate separately, according to an objective and transparent method, those extra investment costs necessary to meet the environmental objectives. Excluded from support are costs not attributable to environmental protection as for example costs for the basic investment. The conditions of the programme were in accordance with the Environmental guidelines (in particular points 29-30 and 34-37). Therefore, the scrutiny by the Commission led to the conclusion that the trade conditions are not affected to an extent contrary to the common interest.

Relief from environmental taxes

In Sweden, there is a relatively high tax on energy, the objective of which is to increase energy saving and energy efficiency. In order, for environmental reasons, to have relatively high energy tax levels and at the same time maintain the competitiveness of the manufacturing sector, tax relief is allowed for the manufacturing industry. A lower tax rate applies for electricity used in the production of companies in the manufacturing sector[48]. The Commission has approved the relief as it was in line with the Environmental guidelines as well as with the "Energy Tax Directive"[49]. According to the guidelines, non-degressive tax exemptions covering a 10-year period from environmental taxes can in certain cases be justified when a Member State introduces a new tax in the absence of a harmonised Community tax or when the tax in a Member State exceeds that laid down by Community legislation. In the Swedish case, the lower tax rate remains higher than the applicable minimum level. Therefore, the Commission considered the notified aid scheme to be compliant with the Energy Tax Directive and with the Environmental guidelines (particularly points 51.1(b) and 51.2) and it was thus approved on the basis of Article 87(3)(c).

In addition to this general energy tax relief for electricity consumed during the production process, the Swedish authorities introduced in 2004 a system with voluntary agreements on energy saving with energy-intensive companies[50]. For these companies, a zero-tax rate on electricity used in their production processes will be applied under the condition that they participate in a 5-year programme for increased energy. The programme imposes certain obligations to be fulfilled by the companies during the programme and penalty provisions in case these obligations are not fulfilled. The obligations are considered to replace the steering effect of the energy tax on electricity used in the production processes of the undertakings. The fact that energy costs constitute an important part of these companies' total costs is an additional incentive for the companies to implement energy-saving measures. Since the scheme was found to be in line with the conditions of the Environmental guidelines (in particular point 51.1(a)) and with the Energy Taxation Directive, the Commission authorised the scheme on the basis of Article 87(3)(c).

48 State aid No. N 156/2004, OJ C 137, 4.7.2005, p. 5

49 Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity OJ L 283, 31.10.2003, p. 51

50 N 253/2004, OJ C 136, 3.6.2005, p. 43

2.1.5. *State aid expenditure on the environment*

As pointed out above, not all environmental and energy saving support measures are considered to be State aid measures. Total expenditure by Member States on State aid measures for the environment and energy saving amounted to € 11.4 billion in 2004. This figure makes up 25% of total state aid less state aid to agriculture, fisheries and transport. Table 12 shows that Member States' State aid expenditure for environment and energy objectives has increased year by year starting from €1.3 billion in 1994 to €11.4 billion in 2004.

Table 12: Trend in the level of State aid for environmental and energy saving purposes

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Environment and energy saiving aid, in million €	1247	1402	1266	1272	1370	3305	5801	6564	7256	9438	11384
Environment and energy saiving aid as % total aid less agriculture, fisheries and transport	2,1	2,5	2,2	1,7	2,8	8,6	12,6	14,0	13,8	19,3	25,1
Environmental aid granted through tax exemptions as % total aid less agriculture, fisheries and transport	0,1	0,1	0,5	0,3	0,6	5,4	8,2	9,4	9,6	14,6	19,5
Environmental aid granted through grants as % total aid less agriculture, fisheries and transport	1,9	2,2	1,6	1,3	2,0	3,0	4,0	4,3	3,8	4,2	5,3

Note: Data for 1994-1999 exclude the ten new Member States. Source: DG Competition

The three largest environmental and energy saving aid grantors in absolute terms were Germany (€6.6 billion), Sweden (€2 billion) and United Kingdom (€1.1 billion). These three countries granted more than 85% of the total aid in 2004. In relative terms, the EU environmental and energy state aid amounted to 0.1% of EU Gross Domestic Product (GDP) in 2004 (Table 13). The biggest aid grantors in relative terms were Sweden (0.7% of GDP), Germany (0.3%) and Denmark (0.28%).

Table 13: State aid for environmental and energy saving purposes

	Aid for environmental and energy saving (in million €, 2004)	Share of environmental and energy saving aid in total aid less agriculture, fisheries and transport, annual average 2002-2004	% point difference in this share (2000-2002 and 2002-2004)
EU-25	11384,1	19,1	5,6
BE	16,9	1,1	-0,4
CZ	3,2	2,2	0,5
DK	541,5	51,4	1,1
DE	6644,8	33,8	9,5
EE	0,1	0,4	-18,9
GR	25,9	3,9	3,8
ES	100,0	2,0	0,9
FR	137,5	3,7	-1,3
IE	6,6	1,0	0,7
IT	34,9	2,1	1,7
CY	1,7	1,0	0,4
LV	0,0	0,0	-0,4
LT	-	-	-
LU	0,0	0,1	-1,2
HU	2,3	3,0	-1,3
MT	-	-	-
NL	446,6	41,8	6,1
AT	94,8	20,5	4,3
PL	10,6	1,5	-2,2
PT	1,7	0,1	-0,1
SI	26,2	23,5	9,2
SK	0,0	0,0	-1,9
FI	215,4	35,1	16,2
SE	1956,9	78,4	40,6
UK	1116,6	21,9	14,5

Source: DG Competition

Around 70% of environmental and energy saving aid in Germany in 2004 was granted under the ecological tax reform[51] through tax reductions/exemptions from the mineral oil tax and from the tax on electricity. In 1999, Germany introduced a tax on the consumption of electricity and increased the mineral oil tax. In order to give transitional relief for some sectors and companies, Germany introduced also partial reductions from the eco-taxes.

Sweden granted in 2004 almost 70% of the environment and energy saving aid through two measures. First, the "Modification of CO_2 tax reduction for the manufacturing industry"[52] was introduced to maintain the present CO_2 tax level for the manufacturing industry when the

[51] See Commission decision on *Ecological tax reform* case, N249/2001.

[52] "Modification of CO_2 tax reduction for the manufacturing industry" N 484/2003

general tax rate was increased. Second, the "Energy tax on electricity used by the manufacturing sector[53]" is a tax exemption from the energy tax.

In 2004, Member States granted on average around 75% - 80% of environmental and energy saving aid through tax exemptions. Germany, Sweden, Finland and Slovenia provided 82% of environmental and energy saving aid in the form of tax exemptions. Two countries used tax deferrals as an instrument to grant environmental and energy state aid: Ireland (100%) and Netherlands (31%). Almost 20% of EU-25 environmental and energy saving aid was transferred in the form of grants. Seven countries (Austria, Cyprus, Estonia, Greece, Hungary, Italy and Spain) used only grants as an aid instrument to grant environmental and energy state aid. Other aid instruments such as soft loans, equity participation and guarantees were used by Member States to a lesser extent.

In conclusion, the underlying trend in expenditure on environmental and energy saving aid is clearly upward: the annual average increased from € 6.5 billion in the period 2000-2002 to € 9.3 billion during the period 2002-2004. While such aid is clearly directed at a commonly accepted horizontal objective, only a relatively small proportion comprises aid to make investments that reach higher environmental standards than community standards or to undertake further investment to reduce pollution or for the development of renewable energy sources. On the other hand, a large proportion of aid (accounting for around 80% of total environmental and energy saving aid in 2004) comprises tax exemptions of which the largest part had to be accepted in order to allow for certain types of environmental taxes to be introduced, e.g., to limit the impact of such taxes on the competitiveness of specific companies or sectors. Although the tax exemptions from environmental taxes do not aim at reaching higher environmental standards, such exemptions are only allowed where the taxes themselves are intended to make a significant contribution to protecting the environment and the exemptions should not undermine the general objectives pursued. Such exemptions have been used in particular by Germany, Sweden and the United Kingdom.

2.1.6. Revision of environmental guidelines

The current Environmental Guidelines are applicable until the end of 2007. The Commission has started reviewing the current guidelines in order to prepare new guidelines for environmental aid. As a starting point, the Commission published a questionnaire[54] in August 2005 and invited all Member States and other interested parties to share their experience with the current guidelines. The questionnaire included a wide range of questions, such as: whether a block exemption for environmental aid should be introduced; which categories of environmental aid should be included; should the polluter-pays principle be strengthened and less aid for polluting undertakings approved; whether the possibility to grant aid for environmental innovation should be introduced, etc. The Commission will analyse the answers and draw up the conclusions in the new draft guidelines for environmental aid, which will be discussed with Member States.

[53] "Energy tax on electricity used by the manufacturing sector" N 156/2004

[54] http://europa.eu.int/comm/competition/state_aid/others/00910_questionnaire_env_en.pdf

3. PART THREE: EXPLORING ALTERNATIVES TO STATE AID

In the context of reducing overall levels of State aid, the conclusions of various European Councils have also invited Member States to consider ways in which this may be achieved. For example, the Brussels European Council in November 2002 invited Member States in its conclusions to "consider before granting State aid whether it is targeted on a clearly identified market failures or directed at horizontal objectives of common interest … and whether an intervention in the form of State aid is the most appropriate and effective way to address these issues".

One of the best ways to reduce state aid is clearly to make better use of alternative measures such as general and regulatory measures. Before resorting to State aid, which should in general only be the "second best" option, Member States should verify whether it would represent the most appropriate solution. Some types of alternative instrument not only help to avoid distortions to competition, but also support Member States efforts to restore and maintain healthy public finances, which is also one of the main pillars of the Lisbon Strategy for Growth and Jobs.

Another approach to reducing state aid is to target it carefully to problem areas and to limit its extent to the necessary amount, time and effective means. Problem areas could in principle be situations where the market fails to produce economically efficient outcomes as set out in the State Aid Action Plan. Identifying the market failure at stake provides a better opportunity to evaluate whether state aid could be justified and acceptable. Furthermore, state aid should be designed so that it solves the market failure effectively, by creating an incentive effect and ensuring it is proportionate.

How can Member States ensure that their state aid policies are pursuing these objectives? The answer lies to a large extent in the granting procedures and practices of State aid in the Member States. With a view to developing best practices that support a "less and better targeted" state aid policy, the following questions may be worth addressing:

To what extent does a Member State assess whether or not State aid is the most appropriate form of intervention? At what stage does such an assessment take place? When and what sort of analysis is carried out to ensure that taxpayers' money in the form of State aid measures is spent effectively and efficiently? What alternatives to State aid are Member States using or developing? What kind of institutional setup supports these goals?

A number of these issues were the subject of a written questionnaire addressed to Member States by the Commission in May 2005 and discussed at a meeting with State aid experts from the Member States in July 2005. This section presents some of the replies provided by Member States as a first step towards identifying best practices in support of a "less and better targeted" state aid policy.

Exploring alternative instruments in the first place

A number of Member States referred to explicit policy efforts towards improving the general business environment such as making changes to the regulatory environment, streamlining their business support schemes and directing support away from (potentially) distortive State aid towards general measures. Among the examples of alternative instruments quoted by Member States are the following:

- The most explicit example is in Sweden with its established principle of restraint whereby subsidies to companies "should never be the first-choice solution" in dealing with different issues. Instead, alternative policy instruments should first be analysed and tested regularly. Sweden contends that there are clear indications that the policy of restraint has led to an increased use of general measures instead of State aid.

- Denmark, which has set up an inter-departmental government committee to reduce the level of aid, stressed that its industrial strategy concentrates on improving the general environment and growth conditions of firms, rather than on helping individual firms directly.

  Similar points were made by other countries such as the Slovak Republic which underlined that individual assistance to enterprises through public spending is used only in exceptional, clearly warranted cases.

- The Netherlands contends that budget constraints are forcing all aid awarding authorities to explore alternatives or grant less aid. One of the basic questions asked when aid is granted is whether or not a financial instrument is the best possible way of resolving the problem. Also related to budget considerations, Estonia referred to the use of de minimis aid as an alternative means of public support.

- In granting aid within its special economic zones, Poland considers a range of other instruments for supporting development, particular in the field of SMEs, such as business incubators, technology parks and clusters - which have a ready infrastructure - and business consultations. A further example is the funding the Ministry of Infrastructure provides for certain activities, including the financing of services provided in the general economic interest. The financing of services in the general interest by means of a special fund made up of contributions from enterprises operating within a particular sector could be considered as an alternative form of state intervention.

- Cyprus has introduced a series of legislative measures or general measures that do not constitute state aid. For example, the tax rate on company profits has been lowered to 10% and applies universally to all sectors, while, at the same time, other measures have been included in tax legislation aiming at the overall improvement of the business environment. In this way, the preferential treatment of offshore companies (which constituted state aid) has been phased out. This also made possible the elimination of a number of tax exemptions granted to specific sectors.

- Hungary and Slovenia cite specific accountancy and tax rules which qualify as general measures while the United Kingdom refers to its use of public-private partnerships in which both parties invest on equal terms and where government invests commercially.

Assessing whether a state aid measure is necessary and appropriate

Many countries also refer to the need for aid to address clearly identified market failures. For example, Slovenia indicates that proposals for state aid schemes must be based on established needs for state intervention resulting either from market failures or from a shortage of private sources of finance and the like.

The Slovak Competitiveness Strategy[55], adopted earlier in 2005, stipulates that the "State will intervene in the effectiveness of the open market only to the strictly necessary extent and for the necessary time, and only in cases where the market is failing and where, in this respect, the State can provide publicly required services more efficiently or more fairly". It goes on to say that there are plans to transfer public expenditure from those areas and programmes which do not correspond to the basic philosophy and objective of the Lisbon strategy. Therefore, when the public administration budgets are prepared, there must be a sufficient increase in public finances available for priority areas, compensated by a reduction of expenditure in other areas.

In Belgium, the Brussels Capital Region has decided to carry out a root-and-branch reform of Brussels legislation on economic expansion with a view to continuing to provide aid that has proved to be appropriate, i.e. consultancy aid, and aid for training and employment, while reducing aid that is less clearly appropriate, i.e. general investment aid.

In the Czech Republic, some providers assess aspects similar to those evaluated in the preparatory stage after the aid has been granted. Analyses of cost-effectiveness and application of the principle of sustainable development may then lead to the adjustment of measures which are being implemented or even to suspension of the aid provided. The Czech Office for the Protection of Competition (UOHS) is involved in working groups which regularly meet in order to monitor State aid. In addition to the compatibility of aid with the State aid rules, these working groups discuss efficiency and the results of evaluation of the aid provided.

Procedures and practices supporting a policy of "less and better targeted" State aid

The majority of Member States reported that they assess the appropriateness of the aid measure vis-à-vis other possible instruments at the design or preparatory phase. Although the final decision as to whether or not state aid should be used is made by the aid-granting authority, in a number of countries this authority has to demonstrate that it has explored alternatives to State aid while in other countries the various funding instruments are examined by some form of coordinating body.

Many national monitoring authorities or similar bodies with a coordination function in state aid matters seem to be taking an increasingly proactive approach towards raising awareness of and local expertise in State aid through advice, training, websites, newsletters, guides, etc. While the main focus of attention may be towards compliance with the State aid rules, the submission of State aid notifications, reporting and monitoring, etc, such interaction should also help to ensure a more consistent and coherent approach towards assessing the appropriateness of state aid vis-à-vis alternative instruments:

– In Cyprus, for the planning of a state aid measure or scheme, a technical committee - composed of representatives of all involved parties, with the participation of the Finance Ministry or Planning Office or both - is set up to examine the form of the intervention, the size of any grant, the duration of the scheme, the assessment criteria etc. The potential effectiveness of the measure in relation to the achievement of the objectives set forth is a crucial factor, as is the financial position of the State.

[55] Slovak Competitiveness Strategy until 2010, the National Lisbon Strategy' (Resolution of the Government of the Slovak Republic No 140 of 16 February 2005)

– The United Kingdom reported that all government departments and aid awarding authorities undergo a Business Planning process where each body identifies where they would focus their resources for a defined period of time and outline the strategies that will be employed to achieve the objectives set within the resources available. Formal appraisal processes ensure that before resources are granted, the rationale, objectives and proposed methodologies of all support measures have been scrutinised. This helps to ensure that the design of the instrument is such that both the likelihood of success of the instrument and value for public money are maximised. In addition, Regulatory Impact Assessments (RIA) are obligatory in the policy forming processes and are considered to be an important process to help analyse policy proposals, determine the costs and benefits of action, and decide on the best delivery method. This process applies whether or not the assistance or funding from government will constitute a State aid.

– Other Member States including Italy and Belgium referred to similar RIA exercises. For example, the Flemish Authority in Belgium described how the preparation of an RIA helps the drafters of the regulation, inter alia, to identify possible options for achieving the desired policy objectives and reflect on the anticipated costs, benefits and effects of the proposals. As soon as a problem is identified – e.g., in connection with the specific situation of a number of firms which have difficulty in investing – an investigation is carried into whether this is the result of a market failure. If this is the case, a study is made of the options available for remedying the market failure and if some form of state aid should be provided. It is explicitly laid down in the RIA that as well as the proposed solutions, alternatives must be found.

– In Finland, each individual authority in the sector concerned is responsible for assessing the appropriateness of its programme in relation to alternative instruments, e.g. when designing the taxation by tonnage the impact of alternative relief models was studied. If, as part of the assessment, public funding has been found to be the most appropriate method to influence the playing field in which companies operate, the Business Support Advisory Committee carries out an assessment of any possible overlapping of the proposed aid schemes, as well as their appropriateness, in relation to existing aid programmes.[56] The Act on the general conditions for business aid requires that before a business aid scheme is approved or fundamentally amended, the official preparing the matter must obtain a statement concerning it from the Business Support Advisory Committee. Action models are applied by the various administrative sectors. For example, the Government Institute for Economic Research (VATT) evaluates the impact of aid which is granted in the form of increased depreciation on investments that are made in development areas. This research data is exploited when the applicability of state aid as an instrument is under consideration. It is also useful when deciding on the need for the continuation of aid.

– In the Slovak Republic, an assessment takes place at the stage of the preparation and evaluation of applications for state aid. Internal and external evaluators assess projects independently in accordance with the project selection criteria, and then present a joint expert opinion to the evaluation committee in accordance with the evaluation criteria. For individual investment incentives, the Implementing Agency

[56] The Business Support Advisory Committee operates in connection with the Ministry of Trade and Industry and includes representation by all the key aid awarding Ministries.

draws up an expert opinion on the application, and the state aid grantor then assesses the application in a process which includes an examination of the company's market share before and after the investment, the investment locality, the unemployment rate in the given locality, the economic independence of the investor, and the benefit for the region.

– In Poland, when designing measures, each authority diagnoses the problems occurring on the market individually, and in seeking appropriate remedial measures, applies a variety of instruments of state intervention, including aid. The relevant authorities assess new aid, in particular, as regards its purpose and anticipated effect, at the stage of inter-departmental negotiations. For example, in relation to tax instruments, the changes made in recent years have been aimed, amongst other things, at changing the manner in which companies have received support. In the case of corporation tax, there has been a retreat from various kinds of concessions arising from things such as object-based VAT exemption for reducing taxation.

– In Spain, the preparation of any state aid scheme is carried out by the competent management centre. The Board for Economic Affairs (CDGAE) examines and discusses the proposals of the ministerial departments which affect the economy or major economic sectors (in particular, government measures amounting to over €6 million).

– At the Ministry of the Interior and Kingdom Relations in the Netherlands, a state aid coordination unit for decentralised authorities has been set up that, in addition to coordinating and providing advice on notifications by those authorities, also does a great deal to keep them informed by, inter alia, drafting guides on certain aspects, and here the development of projects without aid being provided is an important starting point.

4. PART FOUR: LEGISLATIVE AND POLICY DEVELOPMENTS

4.1. A modernized State aid policy

Commission outlines comprehensive five year reform of state aid policy to promote growth, jobs and cohesion

In June 2005, the Commission launched a State Aid Action Plan[57] outlining the guiding principles for a comprehensive reform of state aid rules and procedures over the next five years. In particular, the Commission intends to use the EC Treaty's state aid rules to encourage Member States to contribute to the Lisbon Strategy by focussing aid on improving the competitiveness of EU industry and creating sustainable jobs (more aid for R & D, innovation and risk capital for small firms), on ensuring social and regional cohesion and improving public services. The Commission also aims to rationalise and streamline procedures, so that the rules are clearer and less aid has to be notified, and to accelerate decision-making.

57 http://europa.eu.int/comm/competition/state_aid/others/action_plan/

Taking account of the comments submitted by interested parties during the consultation process that ended in September, the Commission will shortly set out detailed reform proposals.

The State Aid Action Plan is based on the following elements:

– less distortive and better targeted state aid, in line with the European Council's repeated declarations, so that public money is used effectively to the benefit of EU citizens in terms of improving economic efficiency, generating more growth and sustainable jobs, social and regional cohesion, improving services of general economic interest, sustainable development and cultural diversity.

– a more refined economic approach, so that less distortive aid, particularly where money is less easily available from financial markets, can be approved more easily and quickly and so that the Commission concentrates its resources on the cases liable to create more serious distortions of competition and trade.

– more streamlined and efficient procedures, better enforcement, higher predictability and enhanced transparency. For example, Member States currently have to notify the Commission most of the state subsidies they want to give. The Commission proposes to exempt more measures from this notification obligation and to simplify procedures.

– a shared responsibility between the Commission and Member States: the Commission cannot improve state aid rules and practice without the effective support of Member States and their full commitment to comply with their obligations to notify any envisaged aid and to enforce the rules properly.

4.1.1. Review of the regional aid guidelines

Beginning in 2003, the Commission decided to review its approach to the control of national regional state aid for the period 2007-2013, in close cooperation with Member States and other stakeholders. The review was intended to take account of enlargement, progressive deepening of the internal market, European competitiveness and demands for the reduction in overall State aid levels.

A Commission staff working document presenting the draft regional aid Guidelines[58] was transmitted to Member States in July 2005 and discussed with State aid experts from Member States in September 2005. The Commission aims to adopt a final version of the guidelines by the end of 2005, in order to leave ample time for Member States and the Commission to ensure a smooth transition by the end of 2006.

The three key features and principles of the new Guidelines are: the need to re-focus regional aid on the most deprived regions of the enlarged Union; the need to improve the overall competitiveness of the Union, Member States and regions; and the need to ensure a smooth transition of the present system of regional state aid control to the new approach.

[58] Available on DG Competition website: http://europa.eu.int/comm/competition/state_aid/regional/

4.1.2. *Communication on State aid to export-credit insurance*

The Communication on the application of the State aid rules to short-term export-credit insurance ("STEC") [59] is due to expire on 31 December 2005. Following the completion of a study on the situation of the private reinsurance market in the field of export credit insurance, and after consultation of Member States as well as of other interested parties, the Commission launched a new draft Communication to Member States on 17 October 2005.

Further to a multilateral meeting with Member States and consultations with other interested parties on the draft, the Commission is considering to leave unchanged the definition of marketable risks contained in the 2001 amendment. However, due to the fact that in most Member States there is unavailable or insufficient cover of export-credit insurance offered by private insurers to micro and small companies with a limited export turnover, the Commission services have proposed to consider their export-related risks, if and to the extent the private market in the Member States does not currently exist, as temporarily non-marketable, also in consideration of the need for the private market to adapt to the increased market size created by the EU enlargement. The Commission intends to publish the final Communication by the end of 2005. It has also decided to extend the validity of the 1997 Communication until 31 December 2010.

4.1.3. *Review of the R&D Framework*

The existing Community Framework for State Aid for Research and Development[60] will expire on 31 December 2005.[61] In the State Aid Action Plan, the Commission decided "to consider if the scope of the Framework for Research and Development should be extended to cover types of aid in favour of certain innovative activities, not already covered by existing guidelines or regulations thereby creating a Framework for R&D and Innovation".[62]

Following the Commission's adoption of a consultative document on innovation (see below), it will not be possible to have a common framework for R&D and Innovation in place before the end of 2005. Accordingly, the Commission has now decided to apply the existing R&D-framework until the entry into force of such a document, 31 December 2006 at the latest.

4.1.4. *Communication on State aid to innovation*

In September 2005, the Commission launched a public consultation on measures to improve state aid for innovation. The suggested improvements, set out for consultation in a draft Communication on State Aid for Innovation[63], include rules for aid that funds innovation, criteria to help public authorities to target aid more effectively, clarifying the rules to increase legal certainty and simplification of the regulatory framework.

The Commission makes clear in the consultation that state aid is not the response to all Europe's competitiveness or innovation problems. While the Commission recognises that, in

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[59] OJ C 281 of 17.9.1997, p. 4, as amended in OJ C 217, 2.8.2001, p. 2, and OJ C 307, 11.12.2004, p. 12.

[60] OJ C 45 of 17.2.1996, p. 5, as amended by the Commission communication amending the Community Framework for State Aid for Research and Development, OJ C 48 of 13.2.1998, p.2.

[61] OJ C 111, 8.5.2002, p.3.

[62] Paragraph 28 of the State Aid Action Plan.

[63] The Communication, press release and memo with frequently asked questions can be found under: http://europa.eu.int/comm/competition/state_aid/others/action_plan/

an effort to create growth and jobs, state aid policy can be used pro-actively to support innovation, by tackling the market failures that prevent markets from naturally delivering innovation, it also stresses that for business to embark on a more innovative path it requires, first and foremost, effective competition. Competition creates natural incentives for companies to come up with new ideas and new products; it makes them adapt to change; and sanctions those that stay put or lag behind. Ensuring competition as a driver of innovation is therefore of paramount importance.

In line with the refined economic approach laid down in the State Aid Action Plan, the draft Communication sets out a clear methodology for the elaboration of state aid measures for innovation activities. The principles are that state aid can only be authorised when 1) the aid instrument targets a well-defined market failure; 2) state aid is the most appropriate policy instrument (which is not always the case sometimes, structural policies or regulatory action may be more appropriate); 3) the aid has an incentive effect on innovation and is proportionate to the defined objective and 4) distortions of competition are limited.

The proposals for innovation aid cover six broad areas: innovative start-ups; risk capital; the integration of innovation into existing rules on state aid for research and development (R&D); innovation intermediaries; training and mobility between university research personnel and SMEs; and poles of excellence for projects of common European interest.

The Communication invited comments on a series of concrete measures for which state aid could be authorised by the Commission through ex-ante rules and criteria. On the basis of the consultation, which the Commission is currently assessing, new provisions will be integrated into the existing state aid rules. These provisions will not only give Member States who apply them more speedy approval of state aid for innovation but also help Member States target public money more effectively. A first exchange of views with Member States should take place at the end of 2005/beginning of 2006, with a view to adoption of the future R&D and Innovation Framework in the first half of 2006.

4.1.5. Revision of the Communication on State aid to risk capital

As mentioned above, the draft Communication on innovation is proposing additional flexibility for state aid to risk capital, notably for the very early project stages (where private investors are extremely reluctant to invest), and for the development phase (where additional funding is often missing to help start-ups grow).

The Commission intends to propose a new draft Communication on State aid to risk capital in early 2006, to replace the current version[64] which expires in August 2006. In preparing the review, the Commission will take account of the replies to the questionnaire sent out for public consultation in January 2005.

4.1.6. Services of General Economic Interest (SGEI)

A package of measures providing greater legal certainty to the financing of services of general economic interest and public service compensation was adopted by the Commission in July 2005.

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[64] Communication on State aid to risk capital OJ C 235 of 21.8.2001. See: http://europa.eu.int/comm/competition/state_aid/legislation/aid3.html#risk

The measures ensure that companies can receive public support to cover net costs incurred, including a reasonable profit, in carrying out public service tasks as defined and entrusted to them by public authorities, whilst ensuring that there is no over-compensation liable to distort competition. Member States are able to grant compensation to small-scale public services, hospitals and social housing without notifying the Commission. The package consists of a Commission Decision based on Article 86 of the Treaty, a Framework and a modification of the Commission Directive on financial transparency.

The Commission Decision (based on Article 86(3) of the EC Treaty) specifies the conditions under which compensation to companies for the provision of public services is compatible with state aid rules (a clearly defined public service mandate and no over-compensation) and does not have to be notified to the Commission in advance.The Decision is applicable to compensation of less than €30 million per year provided its beneficiaries have an annual turnover of less than €100 million. Compensation granted to hospitals and social housing for services of general economic interest also benefits from the Decision irrespective of the amounts involved, as does compensation for air and sea transport to islands as well as airports and ports below specific thresholds defined in passenger volumes.

The Commission Framework specifies the conditions under which compensation not covered by the Decision is compatible with state aid rules. Such compensation will have to be notified to the Commission due to the higher risk of distortion of competition. Compensation that exceeds the costs of the public service, or is used by companies on other markets open to competition, is not justified, and is incompatible.

Finally, the package modifies the existing Transparency Directive to ensure clear separation of the operators' public service costs and costs for commercial services, to enable clear assessment of the costs of public services.

See also article in the autumn 2005 edition of the DG Competition Newsletter.[65]

4.1.7. Revision of Environmental aid Guidelines

As mentioned in section 2.1.6, the Commission has, as part of the revision process for the Guidelines on state aid for environmental protection, which will expire at the end of 2007, invited Member States and other interested parties to share their experience with the current guidelines. In this context, in August 2005, the Commission published a questionnaire[66] addressing some of the issues currently under consideration. The Commission is currently examining the replies to the questionnaire with a view to preparing a draft set of guidelines to be circulated to Member States during the course of 2006.

4.2. Recovery of unlawful aid

Article 14 (1) of Council Regulation 659/1999 states that "where negative decisions are taken in cases of unlawful aid, the Commission shall decide that the Member State concerned shall take all necessary measures to recover the aid from the beneficiary."

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65 EC Competition Policy Newsletter - 2005 Number 3 Autumn (forthcoming): "Public Service Compensation in Practice – Commission Package on State Aid for Services of General Economic Interest" - http://europa.eu.int/comm/competition/publications/cpn/

66 http://europa.eu.int/comm/competition/state_aid/others/00910_questionnaire_env_en.pdf

As of 30 June 2005, there were 84 pending recovery decisions, compared to 94 at the end of 2004.[67] During the first six months of 2005, 14 cases were closed while a further four new recovery decisions were taken (Table 14). The geographical distribution of pending recovery cases remains relatively stable: Germany accounts for the largest number of pending recovery cases (42%) followed by Spain (24%), Italy (14%) and France (8%). There are no pending cases in sixteen of the EU-25 Member States.

Table 14: Pending recovery cases by Member State, first semester 2005

	Situation 31/12/2004	New cases in first semester 2005	Cases closed in first semester 2005	Situation 30/06/2005
DE	44	1	10	35
ES	20	0	0	20
IT	11	2	1	12
FR	10	0	3	7
BE	3	0	0	3
NL	2	1	0	3
EL	2	0	0	2
PT	1	0	0	1
SW	1	0	0	1
TOTAL	94	4	14	84

Source: DG Competition.

Table 15 provides data on the amounts of aid to be recovered under the 96 recovery decisions adopted since 2000[68]. For 72 of these decisions, relatively accurate information exists on the amount of aid involved. This information shows that the total amount of aid to be recovered on the basis of decisions adopted between 1.1.2000 and 30.6.2005 is € 9.4 billion[69]. Half of this amount is due to decisions taken in 2004 (Landesbanken, France Télécom, Spanish shipyards).

67 Excluding any recovery cases in the agriculture, fisheries or transport sectors.

68 On 30.6.2005, there were still a further 16 recovery decisions pending that were adopted before 1/1/2000.

69 The spring 2005 Scoreboard reported a total of €9.7 billion. The reasons for the discrepancy are due to the annulment of the Credit Mutuel decision by the CFI and to the use of some estimated figures for which final data are now available.

Table 15: Trend in the number of recovery decisions and amounts to be recovered, 2000-2005

	Date of Decision						
	2000	2001	2002	2003	2004	First sem. 2005	Total
Nr.of decisions adopted	16	21	22	10	23	4	96
Nr of decisions for which the aid amount is known	15	12	17	8	18	2	72
Total aid to be recovered (million €) (1)	**362.1**	**1828.5**	**1089.8**	**1015.9**	**5104.2**	**10.4**	**9410.9**
Amounts recovered (in million €)	**108.2**	**797.9**	**1441.4**	**1228.2**	**4396.3**	**0**	**7972.0**
Of which:							
(a) Principal reimbursed/in blocked account	17.1	797.9	1038.0	892.5	3135.1		5880.6
(b) Aid lost in bankruptcy	91.1		1.2	0.7			93.0
(c) Interest			402.2	335	1261.2		1998.4
Amount outstanding (2)	253.9	1030.6	50.6	122.7	1969.1	10.4	3437.3
% still pending to be recovered	**70.1%**	**56.4%**	**4.6%**	**12.1%**	**38.6%**	**100.0%**	**36.5%**

(1) Only for Decisions for which the aid amount is known. (2) Amount excluding interest. Source: DG Competition.

For 24 of the recovery decisions adopted since 2000, the Member State concerned has not yet submitted reliable information on the aid amount involved. The availability of information on amounts to be recovered is particularly limited in the case of aid schemes, especially tax or quasi-tax aid measures, and aid measures involving guarantees. The Commission continues its efforts to obtain information from the Member States on the aid amounts involved.

Of the € 9.4 billion of aid to be recovered under decisions adopted since 2000, some € 7.9 billion (a principal amount of € 5.9 billion plus almost € 2 billion interest) had been effectively recovered by the end of June 2005. Excluding interest, this represents 63.5% of the total amount to be recovered.

Recovery of incompatible state aid is a lengthy process: 16 of the recovery decisions still pending at the end of June 2005 were adopted before the year 2000. Of the 96 decisions adopted between 2000 and June 2005, only 29 were closed by the end of June 2005 (Table 16).

Table 16: Trend in the closure of recovery cases

	Date of the decision						
	2000	2001	2002	2003	2004	First semester 2005	Total
Number of recovery decisions adopted	16	21	22	10	23	4	96
Number of recovery cases closed on 30/06/05	9	2	9	4	5	0	29

Source: DG Competition.

As underlined in the State Aid Action Plan (SAAP), the effectiveness and credibility of state aid control presupposes a proper enforcement of the Commission's decisions. The Commission therefore announced in the SAAP that it will seek to achieve a more effective and immediate execution of the recovery decisions, which will ensure equality of treatment of all beneficiaries. To this effect, the SAAP announces that the Commission will monitor more closely the execution of the recovery decisions by Member States. Where Member States do not take all measures available to implement such decisions, the Commission will more actively pursue non-compliance under Articles 88(2), 226 and 228 of the Treaty.

See also article "Enforcement of State aid recovery decisions" in the Competition Policy Newsletter[70].

4.3. State aid to the agricultural sector

In accordance with Annex IV, part 4, point 4 of the Accession Treaty the new Member States could communicate to the Commission all schemes and individual aid granted before accession and still applicable after accession in order to have them approved by the Commission as "existing" aid within the meaning of Article 88(1) of the EC Treaty. Until the end of third year from the date of accession the new Member States shall, where necessary, amend these measures in order to comply with the guidelines applied by the Commission. After that date any aid found incompatible with those guidelines shall be considered as new aid.

The Accession Treaty obliges the Commission to publish a list of aids it has approved as existing aid. The Commission has not only published a list of existing aid measures in the Official Journal[71] but has also put the full text of all existing state aid measures notified by the ten new Member States on-line. A total of 451 measures have been made accessible. This is a big step towards creating more transparency in the field of state aid. Nothing similar has been done for previous enlargements. Since these existing state aid measures are not subject to a full assessment by the Commission, it would otherwise be difficult for the public to know the

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70 Competition Policy Newsletter, Number 2, Summer 2005: http://europa.eu.int/comm/competition/publications/cpn/cpn2005_2.pdf

71 OJ C 147, 17.6.2005, p. 2

substance of the state aid measures that are in place in the new Member States. This transparency notably improves legal certainty for the farmers in the new Member States in the sense that they (and farmer representatives) can now easily check whether state aid they receive is covered by an existing aid regime.

The number of measures submitted per new Member State is:

Czech Republic	63
Lithuania	30
Latvia	33
Slovakia	32
Estonia	23
Malta	19
Hungary	108
Cyprus	70
Poland	51
Slovenia	22

The Commission has published the full texts of these existing measures on the Internet at the following address: http://europa.eu.int/comm/agriculture/stateaid/newms/index_en.htm

By the end of November 2005, Member States have communicated to the Commission services the summaries of around 80 different measures under the procedure laid down by art. 19 of Regulation N° 1/2004 granting exemption for certain types of state aid accorded to small and medium-sized agricultural enterprises. The Commission has published these summaries on the Internet at the following address:

http://europa.eu.int/comm/agriculture/stateaid/exemption/index_en.htm.

4.4. State aid to the transport sector

One of the main objectives of the common transport policy is the promotion of environmentally friendly modes of transport in order to achieve a reduction of road transport. In this sense, the revitalisation of the railway sector is considered as a key element in the Community's common transport policy. Rail transport has to be made, once again, competitive enough to remain one of the leading players in the transport system in an enlarged Europe. By 2007, the entire European freight network, both internationally as nationally, will have been opened up completely to competition. The arrival of new railway companies should make the sector more competitive and encourage the national companies to restructure. In this context, specific guidelines for the railway sector will be developed in 2006. The main objective of these guidelines is to establish a common approach with regard to public contributions to the railway sector. It is necessary from both a legal and a political point of view that national authorities, companies and individuals are made aware, in a clear and transparent way, of the rules applicable to the railway sector in this new more competitive environment. This initiative will significantly increase transparency and legal certainty.

Further as regards legislation, the Commission published in June 2005 its draft proposal of 3 March 2004 amending the de minimis Regulation by including in its scope the transport sector. Observations from all interested parties were transmitted as of July 2005.

In July 2005 the Commission also adopted a revised proposal for a Regulation on public passenger transport services by rail and by road, designed to modernise Regulation 1191/69, which is still in force today. This proposal gives national, regional and local authorities the possiblity of defining the public service missions of inland transport (bus, train, tram, underground railway) and to give financing or exclusive rights to the operators responsible for such services, if this is necessary for the operation of these public services. The Regulation also sets a framework for the choice by the local authorities of the undertakings to provide these public transport services. It is stipulated that even though from a legal angle the financing granted in accordance with this Regulation as compensation for the public service constitutes State aid, it need not be notified to the Commission and is considered compatible with the internal market rules.

Concerning the air sector, the Commission adopted on 6 September 2005 a Communication on Community guidelines on financing of airports and start-up aid to airlines departing from regional airports[72]. Following a wide-ranging public consultation, the Commission has adopted new rules which will encourage the development of regional airports. These rules lay down the conditions under which start-up aid can be granted to airlines to operate new routes from regional airports. New regional air services will encourage mobility in Europe and regional development. The clear rules adopted guarantee equal treatment for public and private airports and ensure that airlines receiving aid are not unduly favoured. These guidelines also give airports and Member States guidance on the public financing of airports establishing a firm legal framework for agreements between airports and airlines. The new guidelines will increase transparency and prevent any discrimination in the agreements concluded by regional airports and airlines on start-up aid.

4.5. Enlargement

On 25 April 2005 the Accession Treaty with both Romania and Bulgaria was signed. A series of safeguard clauses were included in the Accession Treaty, in the event the acceding countries fail to implement commitments undertaken in the context of the accession negotiations, as well as a provision for the possible postponement of the date of accession by one year in the event of either state being manifestly unprepared to meet the requirements of membership. In the case of Romania, the Treaty specifies that the Council may, on the basis of a Commission recommendation and after a detailed assessment decide on such a postponement, if it finds shortcomings in Romania's fulfilment of specific conditions in the competition area.

According to the Commission's comprehensive monitoring report on the state of preparedness for EU membership published in October 2005, both Bulgaria and Romania have continued to make progress in adopting and implementing EU legislation and have reached a considerable degree of alignment. Romania was called to make increased efforts in the area of competition policy as regards in particular the enforcement of state aid rules. The Commission will continue to monitor progress intensively up to accession and intends to present a monitoring report to the Council and Parliament in April/May 2006. At that moment, the Commission may recommend that the Council postpone the accession of Bulgaria or Romania until 1 January 2008 if there is a serious risk of any of those states being manifestly unprepared to meet the requirements of membership by January 2007 in a number of important areas.

[72] http://europa.eu.int/comm/dgs/energy_transport/state_aid/doc/2005_09_06_aviation_guidelines_en.pdf

No existing aid measures have been attached to the Accession Treaty of Romania, nor will the interim procedure be applied until the Commission concludes that Romania's state aid enforcement record has reached a satisfactory level. In the case of Bulgaria, three measures have been annexed to the Accession Treaty that shall be thus regarded as existing aid upon accession. In October 2005, Bulgaria submitted its first request to the Commission under the interim procedure pursuant to Annex V § 2.1(c) of the Accession Treaty.

EU Member States decided in Luxemburg on 3 October 2005 to launch accession negotiations with Croatia and Turkey. The advancement of the negotiations will be guided by the candidate countries' progress in preparing for accession. Progress will be measured in particular against the Copenhagen criteria, which includes among its requirements for membership "the existence of a functioning market economy and the capacity to cope with competitive pressure and market forces within the Union". For each chapter of the negotiations, the Council must lay down benchmarks for the provisional closure of negotiations, including a satisfactory track record on implementation of the acquis. Existing legal obligations relating to alignment with the acquis must be fulfilled before negotiations on the chapters concerned are closed. Long transition periods may be necessary. Issues relating to competition and state aid will be dealt in a separate chapter during the negotiations.

5. ONLINE STATE AID SCOREBOARD, REGISTER AND OTHER REPORTS ON STATE AID

The online Scoreboard contains electronic versions of this and previous Scoreboards as well as a set of key indicators and a wide array of statistical tables: http://europa.eu.int/comm/competition/state_aid/scoreboard/

Any queries or requests for data should be sent to the scoreboard mailbox at Stateaid-Scoreboard@cec.eu.int

State aid Register – a second transparency tool

The Commission's State aid Register has been online since 2001. The Register provides detailed information on all State aid cases which have been the object of a final Commission decision since 1st January 2000 as well as block exemption cases published in the Official Journal. It is updated daily and thus ensures that the public has timely access to the most recent State aid decisions. It is available on the homepage of the Competition Directorate General's Internet site:

http://europa.eu.int/comm/competition/state_aid/register/

Following an extensive review, a major revamp of the Register is foreseen and should be fully operational in early 2006.

Annual Competition Report and Competition Policy Newsletter

The Commission publishes an Annual Report on Competition Policy which summarises the most important legal developments and case-law of the year as well as statistical data on the Commission's work during the relevant year.
http://europa.eu.int/comm/competition/annual_reports/
A Competition Policy Newsletter is also published three times a year by the Competition Directorate-General of the European Commission. It aims at describing and discussing in

more detail legislative developments as well as interesting case-law and covers generally the preceding four months.
http://europa.eu.int/comm/competition/publications/cpn/

6. METHODOLOGICAL NOTES

The Scoreboard covers State aid as defined under Article 87(1) EC Treaty that is granted by the EU-25 Member States and has been examined by the Commission. Accordingly, general measures and public subsidies that have no affect on trade and do not distort or threaten to distort competition are not dealt with in the Scoreboard as they are not subject to the Commission's investigative powers. For example, a general tax break for expenditure on research and development is not considered as State aid although it may well appear in Member States national budgets as public support for research and development. Furthermore, Community funds and instruments are also excluded. See also box on "What is a State aid" on page 11 of the spring 2005 update of the Scoreboard.

All State aid data refer to the implementation of Commission decisions and not cases that are still under examination. There may be discrepancies with figures published in previous Scoreboards for a number of reasons: first, provisional or estimated figures may now be replaced by final data; second, when the Commission takes a decision on a non-notified aid measure, the aid in question is attributed to the year(s) in which it was awarded. In cases that result in expenditure over a number of years, the total amount is attributed to each of the years in which expenditure took place. All data are provided in million (or billion where appropriate) euro at constant 1995 prices but have been re-referenced on the year 2004.

This autumn 2005 edition of the Scoreboard focuses largely on the year 2004. This is the first time that the Commission, thanks to the efforts of the Member States in responding to the new reporting requirements set out in Commission Regulation 794/2004, has been able to publish data for the preceding year. Another improvement concerns the inclusion of recent decisions, taken between January and August 2005, during which the Commission reached a final decision following a formal investigation procedure.

As in previous years, State aid data collected for the Scoreboard are grouped according to primary objectives which may be either horizontal or sector-specific. Information on the objective of the aid, or, the sector to which the aid is directed, refers to the time the aid was approved and not to the final recipients of the aid. For example, the primary objective of a scheme which, at the time the aid was approved, was exclusively earmarked for SMEs is classified as aid for 'SMEs'. In contrast, aid granted under, say, a regional development scheme may ultimately be awarded to SMEs, but is not regarded as such if, at the time the aid was approved, the scheme was open to all enterprises.

The following symbols have been used in the Scoreboard:

n.a. not available

- real zero

0 less than half the unit used

Further information on methodological issues may be found on the online Scoreboard:

http://europa.eu.int/comm/competition/state_aid/scoreboard/conceptual_remarks.html