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State Aid in the Enlarged European Union. An Overview

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**State Aid in the Enlarged European Union
An Overview**

Jens Hölscher, Nicole Nulsch, Johannes Stephan

November 2010

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IWH Discussion Papers

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State Aid in the Enlarged European Union

An Overview

Abstract

In the early phase of transition that started with the 1990s, Central and Eastern European Countries pursued economic restructuring of the enterprise sector that involved massive injections of state support. Also foreign investment from the West and facilitation of the development of a market economy involved massive injections of state support. With their accession to the European Union (EU), levels and forms of state aid came under critical review by the European Commission. This inquiry investigates whether the integration of the new member states operates on a level playing field with respect to state aid. Quantitative and qualitative analysis is relied upon to answer this key, as well as other, related questions. Findings suggest that in recent years a level playing field across the EU has indeed emerged. State aid in the new EU member countries is rather handled more strictly than laxer compared to the 'old' EU countries.

JEL Classification: H25, L50, P20

Keywords: competition policy, economic transition, EU enlargement, state aid

Staatliche Beihilfen in der erweiterten Europäischen Union Ein Überblick

Zusammenfassung

Als die Frühphase der Transformation in den neunziger Jahren begann, haben die Länder Mittel- und Osteuropas (MOEL) den Unternehmenssektor durch massive staatliche Unterstützungen restrukturiert, wobei der Fokus auf der Privatisierung und Liberalisierung traditioneller Industrien lag. Aber auch ausländische Direktinvestitionen und die Schaffung einer Marktwirtschaft erforderten massive staatliche Unterstützung. Mit dem Beitritt der MOEL zur Europäischen Union (EU) kamen die Höhe und auch die Form der gewährten staatlichen Unterstützung unter die kritische Beobachtung der Europäischen Kommission. Der vorliegende Beitrag untersucht, wie sich die europäische Beihilfekontrolle auf die Ausrichtung der nationalen Beihilfepolitiken der MOEL nach dem Beitritt in die EU ausgewirkt hat. In einer quantitativen Analyse werden daher Beihilfeniveaus und -ziele der MOEL denen der westeuropäischen EU-Länder gegenübergestellt. Darüber hinaus werden in einer qualitativen Untersuchung Entscheidungen der Kommission in Bezug auf nicht genehmigte Beihilfen analysiert, um etwaige Unterschiede in den Beihilfepolitiken der ost- und westeuropäischen Länder herauszustellen. Die Resultate zeigen, dass in den letzten Jahren ein einheitliches *level playing field* in Bezug auf staatliche Beihilfen entstanden ist. So zeigte sich nach dem EU-Beitritt der MOEL eine rasche Annäherung der staatlichen Beihilfen an den Durchschnitt der westlichen EU-Länder in Bezug auf die Gesamtausgaben. Hinsichtlich der Verwendung staatlicher Beihilfen zeichnen sich zwar Unterschiede ab, allerdings nicht allein gegenüber den westeuropäischen EU-Ländern, sondern auch innerhalb der MOEL.

JEL-Klassifikation: H25, L50, P20

Schlagworte: Wettbewerbspolitik, ökonomische Transformation, EU-Osterweiterung, staatliche Beihilfen

Introduction¹

In the early 1990s, and towards the start of the transition phase, Central and Eastern European countries (CEECs)² relied upon public sector outlays to promote industrial restructuring. State aid included tax incentives for investors, establishment of special economic zones, and the like, with an additional focus designed to support flows of foreign investments from the West. Some of these CEECs are now fully integrated in Europe's common market and their integration has come under critical review by the European Commission. This inquiry investigates whether the integration of the new European Union (EU) member states operates on a level playing field with respect to receiving various forms of public sector aid.

An earlier analysis (Hölscher and Stephan, 2009) reveals that effectiveness of implementation of competition law and policy and intensity of competition run lower for CEECs compared to the EU-15 countries. This inquiry aims to clarify whether this comparatively lower level of performance results as state aid is granted more generously (with less supervision, scrutiny, and lower levels of accountability) in the CEECs. And also do funds tend to be targeted at individual firms or industries? Röller and Hirschhausen (1996) expected major implications regarding the assessment of state aid measures in former socialist countries having in mind the experience from East Germany. Thus, we consider how state aid policy in the CEECs has developed over recent years since full EU membership and whether indeed their industrial policies during and after transition challenged the European state aid regime.

CEECs have a strong tradition of government intervention resulting from the planned economy system. Even at the dawn of EU accession their level of public support to certain industries and individual firms was significantly higher than in the EU-15 member states. Three years after accession a study by Hashi et al. (2007, p. 51) found that “the general philosophy [regarding state aid policies] does not appear to have changed fundamentally since the accession”. The authors inquire: Does government intervention in the form of state aid influence industrial competitiveness? They find that competitiveness is not improved by state aid policies but by the firms' efforts themselves. Another related work compares state aid at an international level. The authors find differences between European countries and the US where the amount of subsidies is markedly lower (Buigues and Sekkat 2010). However, that paper fails to include the CEECs.

¹ This research project was supported by the Halle Institute of Economic Research (IWH). We especially thank *John Hall* and *Marina Gruševaja* for reviewing the paper and providing critical comments and helpful suggestions. We have benefited from comments from the audience at the EACES Conference 2010 and the Research Seminar 2010 given at IWH. We assume responsibility for all errors.

² In the context of this article, Central and Eastern European countries are the following ten most recent member states of the European Union: Bulgaria, the Czech Republic, Hungary, Estonia, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia.

State aid takes numerous forms. For example, state aid would include those public funds that a national government allocates to its own domestic firms and industries, taking the form of subsidies, tax reductions, guarantees and the like. State aid is monitored and controlled by the European Commission by requiring member states to notify in principle the Commission in advance. This study compares justifications for state aid in theory and also in practice. This inquiry considers the question: are CEECs treated differently in terms of the kind of justifications used, or the kind of state aid notifications (e.g. biases on particular kinds of state aid, in particular industries, stages of value chain, technology, knowledge, education)? If “yes,” how does that affect the playing field across the European economic space? The Commission has the right to approve or refuse to approve proposed state aid; aid that is not notified to and tested by the Commission is defined as unlawful. Under the present procedural rules, the Commission is under obligation to order the recovery from the beneficiaries of any unlawful aid that is found to be incompatible with the common market.

This study is structured into five sections. Section two places state aid into the context of economic theory and EU competition policy, and then proceeds to the accession negotiations with the new EU member countries. This section concludes with an overview of the development of a competition culture compared with the average of the ‘old’ EU-15 member countries. Relevant literature is also reviewed. Section three provides stylised facts of state aid in comparative perspective. For this quantitative analysis statistics and data provided by the European Commission and national authorities are used. Section four presents selected exemplary cases in which state aid delivered to selected CEECs was declared unlawful. In this qualitative analysis court cases are used to identify the rationale for the decisions made by the Commission. This delivers an assessment of the effectiveness of state aid control in the EU common market with particular reference to the CEECs. Finally, this study evaluates the adequacy of current procedures with a view on a level playing field for doing business in the European Union.

Economic Theory and the EC Treaty

The main economic justification for state aid is to enhance efficiency in order to optimise total welfare. However, as there are several different types of aid, their motivation varies as well. Accordingly, state aid is used to correct market failures, like externalities, asymmetric information or market power and coordination problems and in respect of public goods. A very common example of positive externalities are R&D activities. Private companies face the difficulty to internalize the spillovers of R&D which leads to an under-investment by private firms. Thus, most governments provide public funds to support R&D activities.

Another justification for public subsidies are information asymmetries. Companies, especially SMEs might face difficulties in acquiring loan capital as the information about the potential of an SME to return a loan or on the risk of its projects are unknown.

In the case of industry or even firm specific aid besides market failure justifications additional arguments are needed, since there is a cost of public funds, optimization of government resources may call for intervention in specific sectors or industries in which externalities can have a larger impact on total welfare. First, bankruptcy of a large enterprise may lead to market power concentration and a possible reduction of total welfare. Second, in terms of restructuring firms, which have been crucial in the transition Central and Eastern Europe economies, state aid smoothes the process of restructuring and therefore mitigates negative social externalities (Nitsche and Heidhues 2006, 21). Third, agglomeration externalities might justify state aid measures for specific industries. The notion of cluster denotes the necessity of firms devoted to similar or related activities in a well defined region due to the costly transmission of tacit knowledge over increased geographical distance. Industrial policy may foster the creation of clusters by possibly subsidizing firms generating these externalities. On the other hand, governments may not have all the necessary information to determine which industries are capable of generating these agglomeration effects (Gual and Jodar-Rosell, 2006). A fourth possible justification for sector-specific aid lies in the market failure of imperfect competition, constituting the basis for strategic trade policy developed first by Brander and Spencer (1983). In an imperfect, oligopolistic market subsidising local companies will increase welfare of the subsidising state as the profit of foreign companies will be directed to the local company as the latter could reduce costs and thus also prices. A classical example in a European context is the Airbus case, documented in Neven and Seabright (1995).

Besides economic considerations also equity concerns may justify the provision of state aid in order to correct social inequalities, e.g. training for employees in a specific industry. Total welfare will be increased if the benefits in terms of social and cohesion goals outweigh the negative effects of distorting competition.

Some forms of state aid involve a mix of efficiency and equity justifications. Regional aid presents such a mix. To the social and cohesion goals, Rodrik (2004) argues that there is a market failure in the process of discovering activities that can be profitably adapted to local conditions: social value of experimenting with new activities is high whereas private costs for entrepreneurs are significant and benefits, if they exist, would be shared with followers. In such cases, a partnership between government and private firms would be desirable.

Aside from economic and social justifications and on the other side of the coin, intervention in the market to overcome 'market failure' may be associated with the danger of 'government failure'. Centralised institutions are 'doomed to choose', have the problem of 'picking winners'. The complex and constantly changing nature of interdependence of markets and the information problems associated with this led the EU to adopt a rather pragmatic, horizontal approach to industrial policy. With regard to state-aid, however, "[t]he idea that the government can disengage from specific policies and just focus on providing broad-based support to all activities in a neutral way is an illusion..." (Hausmann and Rodrik 2006, p. 24).

Yet, since the enactment in 1958 the EC Treaty ever contained rules regulating industrial policies and the provision of state aid. The primary function of such a control is to ensure a free competition between enterprises from different member states on the Common market. European state aid control is based on Articles 107 to 109 of the Treaty on the Functioning of the European Union (TFEU) and its interpretation by the European Commission (laid down in decisions and regulations) and the judgements of the European Courts.

Article 107 (1) TFEU broadly defines:

“Save as otherwise provided in this Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between Member States, be incompatible with the common market.”

Thus, in general state aid is prohibited if the aid measure is granted through state resources and might distort competition in the internal market. However, Article 107 (2) TFEU and Article 107 (3) TFEU list the exemptions from the prohibition in order to balance competition and trade considerations against the wider objectives of the EU (e.g. economic and social cohesion). These two paragraphs build the foundation for several exemptions which are mainly codified in the Commission's soft law. One of these regulations is the general block exemption regulation (GBER) which was introduced in 2008 regarding exemptions for several horizontal objectives of aid (e.g. aid for research and development, environmental aid).

The European state aid control system finds a justification in several economic theories. In the reasoning of the traditional foreign trade theory the reduction of trade barriers between countries will generate welfare effects due to the exploitation of absolute and comparative economics. Foreign trade theory however, does not show distortionary effects of state aid measures as it uses a static model assuming perfect competition. State aid measures would have no short term effect on capacities in the market but would only increase profit of the benefited company. In contrast, the Strategic Trade Theory assumes an imperfect, oligopolistic market: to subsidise a local company which would increase welfare of the subsidising state: profit of foreign companies would be directed to the local company as the latter could reduce cost and thus reduce prices. As every state has the same incentive to subsidise a subsidy race would follow. Thus, in the reasoning of the Strategic Trade Theory state aid regulation is fundamental to ensure a level playing field across the EU. Therefore, the aim of state aid control would be to prohibit state aid in order to prevent such a subsidy race. Another perspective is identified by the New Political Economics. Subsidising firms, especially rescuing large firms, is often a politically attractive option in order to increase popularity and the chance to win elections.

2.a Enforcement of State Aid Control in the European Union

Based on Article 108 TFEU (ex. Art. 88) the power of state aid regulation in the EU is firmly allocated to the European Commission in the Directorate General Competition. All state aid measures have to be notified to the Commission and can only be put into effect until having been approved by the EU. If the Commission regards a measure as not compatible with state aid rules it comes to a negative decision. Firms that already received aid without EU consent may be liable to paying back if the aid was disapproved of ex post. Such a recovery of unlawful aid is not explicitly mentioned in primary legislation but was won by the Commission in case law. In its *Kohlengesetz* decision in 1973 the European Court of Justice (ECJ) established the Commission's power, in order for a negative decision 'to be of practical effect', to 'require repayment of aid granted in breach of the Treaty' in addition to requiring the member state concerned to abolish or modify any aid found to be incompatible with the common market (Santa Maria 2007, p. 5 and European Commission 2007).

The enforcement of European state aid rules is sometimes denoted to be "subdued" (Santa Maria, 2007, p. 3). In the 1950s to 70s most countries pursued an industrial policy which saw in public subsidies a panacea for growth and development leading to a non-compliance with European state aid rules (Zuleeg 1978). It took the Commission years to establish and enforce the simple rule of notification for state aid schemes. For many years the member states were reluctant to honour the Commission's decisions or rulings of the ECJ in such cases (Slot 1990, Lasok 1990). The first negative decision regarding state aid was published in 1964 (Ford Tractor) and until 1980 only 13 negative decisions have been taken. This changed only gradually with the introduction of the common market from the 1980s onwards. However, prior to enlargement it has been widely acknowledged that European state aid control enjoys a good level of compliance and can be regarded as a success story (Wolf 2005, p. 88, 90; Lavdas and Mendrinou 1999). Furthermore, the Commission nowadays takes a strong stance against unlawful aid. In recent years, the Commission has been more and more willing to reach negative decisions and to enforce decisions with recovery payment where aid has already been paid. In 1993, *British Aerospace* was the first case of aid repayment involving reimbursement of the interest advantage on the granted aid.³ Yet, the repayment of unlawful aid is still a rather difficult task as it depends on national authorities. Former Competition Commissioner Kroes has noted that only a small percentage of aids banned by the Commission are ever recovered and has stressed the duty of the member states to act to improve compliance (Wishlade 2006, p.237). Even though Art. 228 TFEU gives the Commission the power to seek penalties against a party ignoring a court order this provision has not been used in the realm of state aid control. At least the Commission now

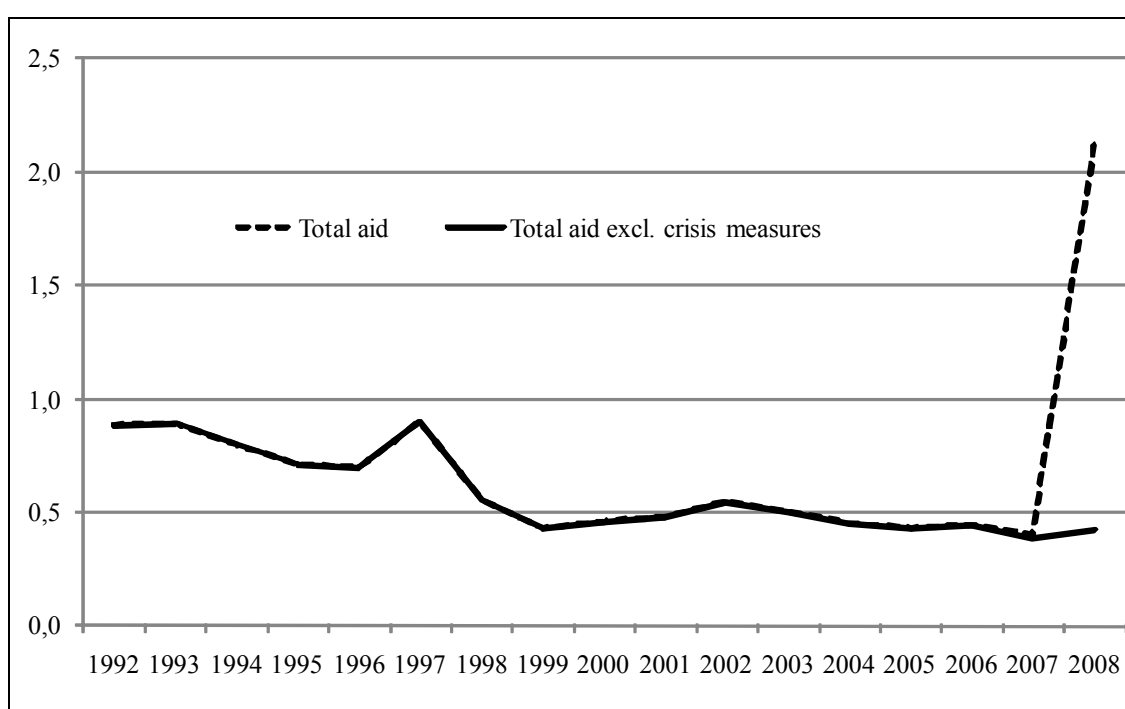
³ Case C-294/90: *British Aerospace Public Ltd Company and Rover Group Holdings plc v Commission of the European Communities*, Judgement of 4.2.1992, ECR 1992, p. I-00493. See also: Press Release (IP/93/405, 26.05.1993) and <http://commercial.practicallaw.com/7-100-4046> (accessed 18.6.2010).

initiates infringement proceedings against a member state that does not take all the measures available to implement the recovery of unlawful aid. In this respect the number of pending recovery decisions has been reduced (from 94 in 2004 to 43 in 2009). Yet, half of the pending decisions were adopted more than four years ago (European Commission 2009). While the Commission is not always in a position to act promptly to safeguard the interests of third parties in state aid matters, national courts may be better placed to ensure that breaches of the rules (in particular Article 108 (3) TFEU) are dealt with and remedied (Jestaedt et al. 2006).

In 2005, the Commission published a so called State Aid Action Plan (SAAP) with the objective of 'less and better targeted state aid'. It shall encourage member states to reduce their overall state aid levels, whilst redirecting state aid resources at objectives having a clear community interest. The attitudes towards state aid were influenced by the Lisbon Agenda, with the Council of Ministers taking a growing interest in the scale and efficiency of government intervention, which is reflected in the objective of 'Less aid, but better' (Wishlade 2006, p.233).

Figure 1:

Total State Aid, Less Agriculture, Fisheries and Transport, for the EU-27, 1992 – 2008, as Percentages of GDP



Source: State Aid Scoreboard, Autumn 2009 (one case in 1997, Credit Lyonnais, responsible for kink)

The amount of state aid in Europe has steadily declined over recent decades. And, mainly because it used to reflect nationally-oriented industrial policies that, with the deepening of European integration in the common market, became increasingly untenable (level playing field). It is only in the most recent past and effected by the outbreak of the

current financial crisis and the economic policy-reactions of most European governments, that state aid (in the broadest sense) jumped markedly in 2008 (see Figure 1).

2.b State Aid in the Central Planning System

In a centrally planned economy, state aid has been an essential instrument: budgetary subsidies were necessary to compensate firms for the losses incurred by producing under a distorted price system. At the beginning of the transition period, these subsidies could be reduced with the price liberalization. However, the decline of budgetary subsidies was followed by the emergence of a series of indirect and less transparent forms of state support to inefficient firms and sectors; state aid has become an important instrument during the process of economic transformation in most CEECs (Atanasiu 2001, p. 263ff). Even though facilitating the development of a market economy involves massive injections of state support (Hashi 2004), the bulk of aid measures to enterprises was not connected to any long term development policy but to rescuing enterprises in difficulty in order to ‘speed up the adjustment process and rescue as many enterprises as possible’. This was motivated to a large extent by political and electoral considerations (Hashi 2004). Rescue and restructuring policies of the early transition period may be described as unplanned, reactive and non transparent and had a strong ‘crisis management’ feature: “[o]pen and hidden subsidies flowed to some enterprises and sectors even when it was established that many of them had no future in a competitive market economy and had to exit anyway.” (Hashi 2004, p.3). Thus, there has been a tremendous misfit between post-communist state aid policies and the state aid policy of the European Union (Blauberger 2007) and a tremendous need for adjustment of state aid rules according to the *acquis communautaire* in the pre-accession period.

The policy change was initiated with the beginning of the accession negotiations to the EU. The CEEC’s commitment to adapt national state aid policies according to European rules dates back to the entry into force of the Europe Agreements. In order to finalise accession negotiations in competition (chapter 6), candidate countries had to fulfil three criteria:

- administrative capacity (i.e. national monitoring authorities)
- sufficient legislative alignment (i.e. application of the state aid *acquis*)
- credible enforcement record

The Europe Agreements contain state aid provisions that closely followed the model of the EC Treaty (general ban), which instruct the CEECs to eliminate state aid if it distorts trade with the EU and to make their state aid expenditures transparent (Atanasiu, 2001, p.259). Between 1997-2001, all CEECs adopted national state aid laws [see reports in the ESTAL] and established national authorities, the Commission was not authorized to

decide on state aid issues until accession of the CEECs. Those national state aid rules and enforcement authorities served also as test for the time after EU accession:

‘Harmonisation in this context takes on a specific character, one that is more about learning to play the game than about borrowing rules’ (Cremona, 2003, p.287)

2.c Accession Negotiations and ‘Existing Aid’

According to the general EC rules on state aid, all aid which is granted by acceding countries before accession to the European Union qualifies as ‘existing aid’ (Regulation 659/1999). Legal consequences of such a qualification as existing aid are i.e. that the Commission can modify an existing aid only with effect for the future and cannot order recovery of aid which has been disbursed in the past under existing aid measures. However, the Commission was concerned that the CEE acceding countries would not learn fast enough ‘to play the game’ as they would not dispose of sufficiently independent state aid control authorities. Thus, different to any prior accession, also all aid granted prior to accession qualified as new aid, unless it was specifically qualified as existing aid in Annex IV to the Accession Treaty (Rapp 2005). The latter refers to the following categories (Dias 2004):

- Aid measures put into effect before 10 December 1994 are per se deemed to be existing aid.
- Measures submitted by CEECs until November 2002 were examined by Commission in the light of the state aid acquis. If those measures were considered to be in line with EC state aid rules, they were qualified as existing aid and listed in an Appendix to the Accession Treaty (320 measures were submitted by CEECs, 222 measures were approved).
- Measures submitted before 1 May 2004 and approved by the Commission under the ‘interim-procedure’ are also considered as existing aid (559 measures were submitted).

The interim mechanism is legally unprecedented. It added a second layer on the filtering process of pre-accession aid in as much as the Commission examined the national authorities’ assessments. The acceding countries were under no obligation to notify their aid measures under the interim-procedure. However, in order to benefit from the classification as ‘existing aid’ and in order to obtain legal certainty, it has been in the CEECs own interest to notify all pre-accession state aid. The Commission strongly encouraged the candidate countries to follow the interim procedure and as a result, the Commission received a notification by the CEECs for 559 measures.

Finally, a number of transitional rules resulted from rather lengthy and complicated negotiations in the competition policy chapter of the *acquis communautaire*. These meas-

ures follow a different regime and do not fall under the treatment of Annex IV.⁴ The transitional framework included: temporary rules on incompatible fiscal aid for Poland, Hungary and Slovakia as well as sector specific exceptions regarding the restructuring of the steel industry in Poland and the Czech Republic. Poland additionally achieved a number of exemptions regarding state aid for environmental protection. Only the Baltic States and Slovenia did not conclude transitional agreements. Hence, these transitional rules mark one point, where aid in the CEECs is more targeted at individual firms or industries. However, the transitional rules phase out (even though at different dates) and all member states have to adjust their industrial policies according to the same rules (Känkänen 2003).⁵

Although the Commission could exert its control function via the interim-procedure already before accession, the year 2004 marks a crucial turning point for the CEECs as the national state aid laws became obsolete and the exclusive competence to control state aid measures has been transferred to the European Commission. Since then, state aid policies in most of the CEECs have changed significantly. Since then, state aid monitoring authorities have only an advisory function. However, this function may differ in the CEECs. The Polish advisory system does not expressly prohibit the granting of aid before the competition authority issues its opinion. Based on the available information, this appears to be different in Estonia, where the authority may not grant aid before receiving an opinion from the Ministry of Finance, which is the competent state aid authority in Estonia.⁶

2.d Developing Competition Culture

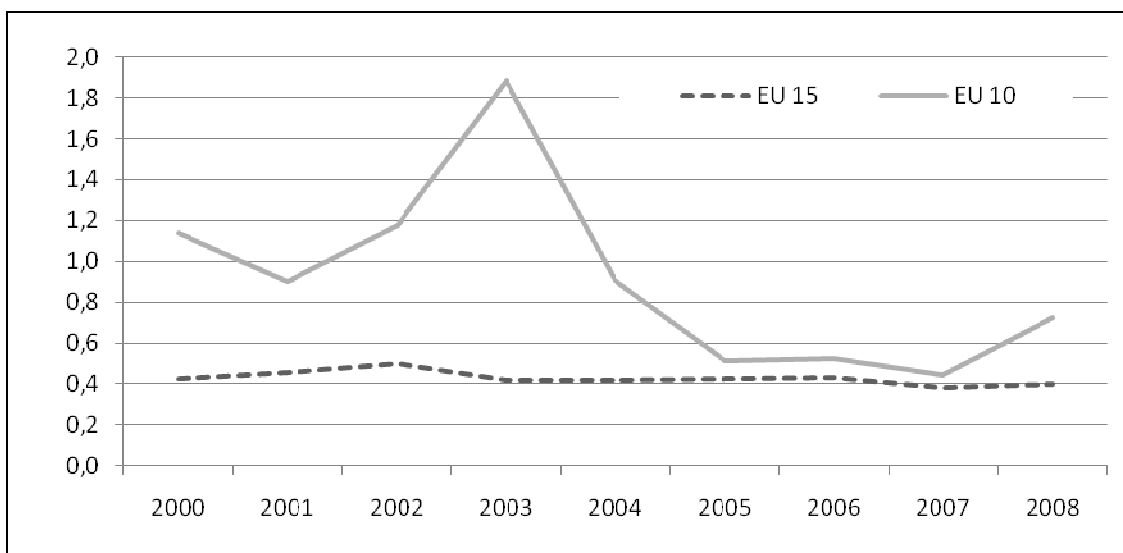
Whilst by 2001, all acceding countries had adopted national competition laws; this did not necessarily result in a competition culture already comparable to the old EU member states. In fact, the amount of state aid granted in the CEECs surpassed the intensity that was common amongst the EU-15 member states: in 2000, total state aid amounted to some 1.1 per cent of GDP (measured in purchasing power standard) amongst the CEECs against only 0.4 per cent amongst the EU-15 (Figure 2). The difference became even larger in 2003 with 1.9 per cent versus 0.4 per cent respectively. In the most recent past, the aid level among the CEECs has nearly reached West European levels and yet it is still somewhat higher (0.7 per cent in 2008) than in the EU-15 countries (0.4 per cent in 2008).

4 Additionally, aid measures in the agricultural and transport sector do not fall under the procedure of Annex IV.

5 Those temporary arrangements may have been particularly important for the new EU members: as formally centrally planned economies, the criterion of competition obviously was absent for decades. The CEECs as catching up economies only started to generate a small and medium sized enterprise sector and competed with fellow transition countries to attract foreign direct investment.

6 § 34 (5) of the Estonian Competition Act. See also *Kuik* 2008.

Figure 2:
Total State Aid, Less Agriculture, Fisheries and Transport, 2000 – 2008,
as Percentages of GDP (excluding crisis measures)



Source: State Aid Scoreboard, Autumn 2009

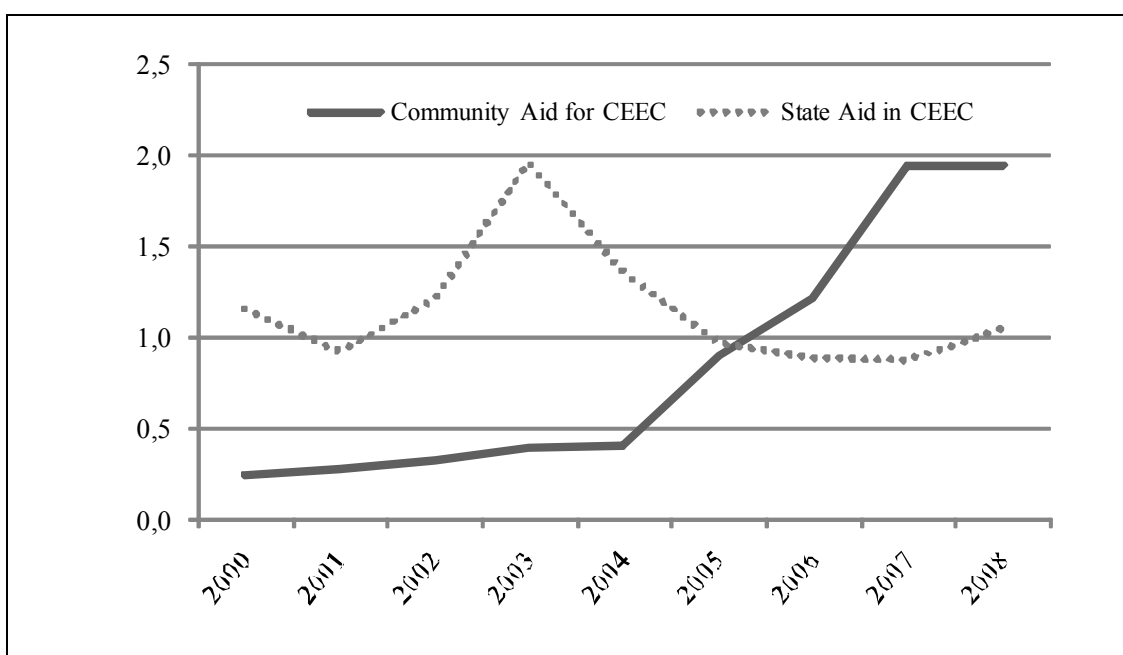
However, parallel to the decline in state aid the amount of aid deriving from EU funds (including agriculture and structural funds) to the CEECs increased rapidly (Figure 3). The EU structural funds are the financial instruments of the European Union's regional policy. In order to narrow the development disparities among member states, i.e. to resolve structural economic and social problems, financial assistance is granted. Therefore, community aid can be used to co-finance projects concerning R&D, employment, training, regional development etc. Thus, it can be concluded that to some extent, former state aid measures have been substituted by community means.

Anyway and returning to state aid, over time, the average differences were not especially striking, and large country-variations exist with Hungary, the Czech Republic, Slovakia, Poland, and Slovenia at the higher end of the spectrum and Estonia, Bulgaria, and Lithuania at the lower (Figure 4). The CEECs are hence not at all homogeneous with respect to their spending for state aid.

These differences may already raise the preliminary expectation that state aid policy in Central East Europe is, in general, more lenient than in the West: institution-building, importance attached to FDI for swift and budgetary relevant privatisation with the expectation of international technology transfer, the apparent difficult negotiations with the EU over the *acquis communautaire*, and a playing field with respect to competition policy slightly tilted towards the East (Hölscher and Stephan 2004 and 2009), all serve to nourish this assumption. Further, the intensity of use of state aid in industrial policy will in general tend to be more pro-active in economies with larger productivity gaps, lower sectoral diversity or adjustment to international division of labour, and structural flexibility in general. Whilst this comparative issue is rather underrepresented in the li-

terature (Blauberger 2009), and no clear answer can be derived so far, the compliance literature in other policy-fields does maybe surprisingly suggest that there is no significant lag in institutional enforcement amongst the CEECs (see e.g. Falkner and Treib 2008): they find a good pattern of transposition of EU law into national law in the four investigated CEECs but rather flawed enforcement (which incidentally could also be observed in two old member states, namely Italy and Ireland).

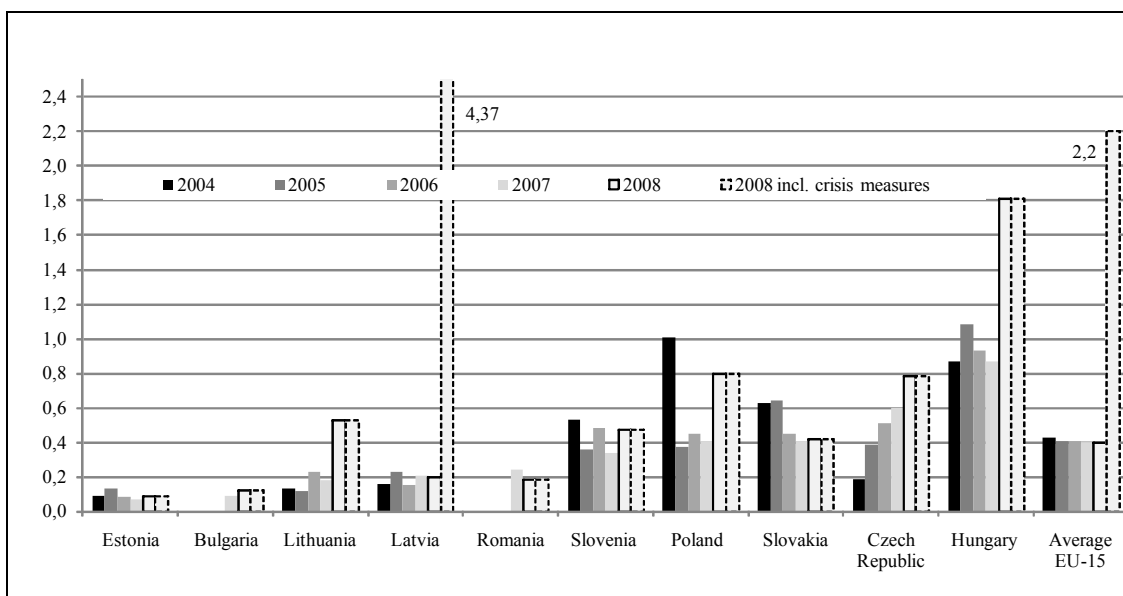
Figure 3:
State Aid and Community Aid in CEEC, 2000 – 2008,
as Percentages of GDP



Source: State Aid Scoreboard, Autumn 2009; EU Financial Report 2008

On the other side, evaluations of innovation policies in Central East Europe suggest that their emergence after EU accession largely followed the same assumption as in Western Europe, i.e. that the countries do generate very good basic research, alas lack results in terms of commercialisation of research results or inventions (see e.g. Kattel et al. 2009, p. 25). Furthermore, the application of instruments produced a much stronger horizontal bias than was common in Western Europe at the same time. This is attributed both to the way that policy makers in the East apparently understood EU state aid regulations (Reid and Peter 2008), and to a general neo-liberal perspective and macro-policy bias of policy makers during the early 2000s (see e.g. Kattel et al. 2009, p. 25). Both interpretations tend to suggest a tendency towards a level playing field. This issue hence remains open, and it is the task of the analytical chapter 3 to test this hypothesis by providing a quantitative overview, by way of qualitative analysis, and by reviewing example representative cases.

Figure 4:
Total State Aid for CEECs, Less Agriculture, Fisheries and Transport, 2004 – 2008,
as Percentages of GDP



Source: State Aid Scoreboard, Autumn 2009

3 Comparative Analysis of State Aid: Stylised Facts

Looking more closely into state aid as discussed above, we start with analysing differences in the application of broad instruments and objectives of state aid and then refer to particularly insightful cases to shed some more specific light on the particularities of state aid in CEECs.

3.a *The Choice of State Aid Instruments in East and West*

One clear difference between East and West in the choice of instruments lies in a strong bias on tax exemptions and social security contributions in the East. This may be rooted in a laxer execution of such commitments (they were often not treated as a form of state aid) and because the possibility of state aid via direct grants was still widely unknown (Biegunski 2008). Further, the rather low share of direct grants might have been due to tighter budgetary positions amongst the transition economies (Schütterle 2004). By 2007, the most favoured aid instruments in 20 member states including CEECs had been direct grants followed by tax exemptions. We no longer find a difference between East and West regarding the choice of instruments. Yet, Slovenia and Estonia provided more than 90% of their aid in the form of grants, while Bulgaria granted more than 80% of their aid through tax exemptions (European Commission 2008).

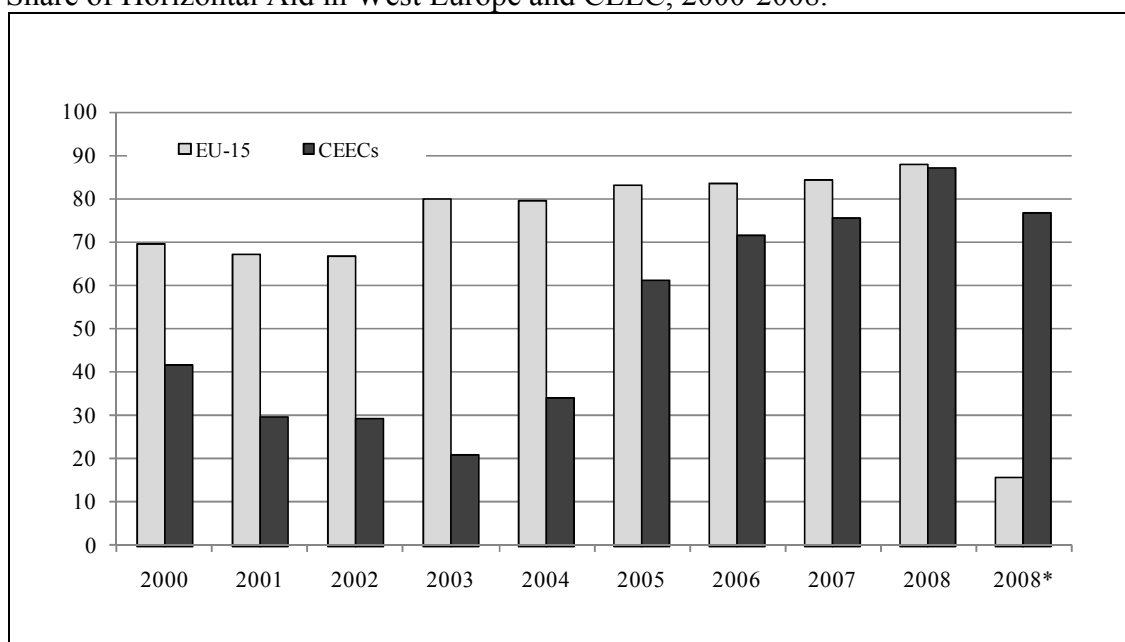
3.b *State Aid Objectives in East and West*

In terms of objectives of state aid, the European Commission distinguishes two broad categories: horizontal and sectoral state aid, the former being largely synonymous with ‘well-targeted’ state aid (European Commission 2005). Sectoral aid is considered to be an important instrument in the course of restructuring and privatizing state-owned enterprises (Ellison 2005, p.26). The Commission’s *State Aid Scoreboard* classifies regional aid as ‘horizontal’, suggesting such aid is in line with the shift to more broadly-based objectives. However, much of regional state aid ends up in the hands of individual firms and investors (ibid., p.25). State aid for horizontal objectives, i.e. not granted to a certain industry sector, is considered as being better suited to address market failures and thus less distortive than sectoral aid. In the mid Nineties, only around 50% of aid was granted for horizontal objectives in the old member states. As it was one of the key Lisbon purposes to redirect state aid towards horizontal objectives, the share increased rapidly in the EU-15 countries. In the CEECs, data only exists from the year 2000 onwards: here, the share of horizontal aid decreased prior to accession. After accession, the share increased rapidly and reached the same level as in the old member states by 2008 (Figure 5). Moreover, the share of horizontal aid is even larger in CEECs when crisis measures are included. Due to the financial crisis and the following aid measures especially to the financial industry, the share of horizontal aid in the EU-15 countries fell to 16 percent.

However, the distinction of aid between horizontal and sectoral objectives is not always exact. This holds especially for the CEECs as prior to accession their national authorities were the sole source of information (e.g. aid to the national railway companies have been reported as sectoral or, in order to act in line with EU policies and make it more acceptable, as horizontal for employment aid). Furthermore, there are concerns that not all aid was reported, especially tax and social contribution arrears (Hashi 2004, p. 12).

Disparities between East and West before accession can be explained in part by the restructuring of industries in order to reach viability and to complete privatization. Furthermore, CEECs took advantage of the transitional rules and the rules on existing aid, agreed upon in the accession negotiations. The previous more lenient treatment of state aid became more difficult after accession as the CEECs had to comply with the European state aid rules. Thus, in several member states, the last chance for sectoral aid was exploited. After accession, the speed of adjustment of national state aid policies however differed between CEECs. Horizontal policies in general did not generate much interest in Poland as compared to other countries prior to accession. State aid in Poland had a bias on large enterprises with a share of around 60% (Blauberger 2009, p.163). The Polish government seemed to give national policy goals precedence over European state aid policy (most prominent examples include the shipyards, see case study in the following section and Blauberger 2007, p. 25). Other CEECs, as Estonia and Slovenia, showed already in the year 2000 a share of horizontal aid above 75%. The government in Estonia always spent public support solely for horizontal measures (Table 5, Annex).

Figure 5:
Share of Horizontal Aid in West Europe and CEEC, 2000-2008.



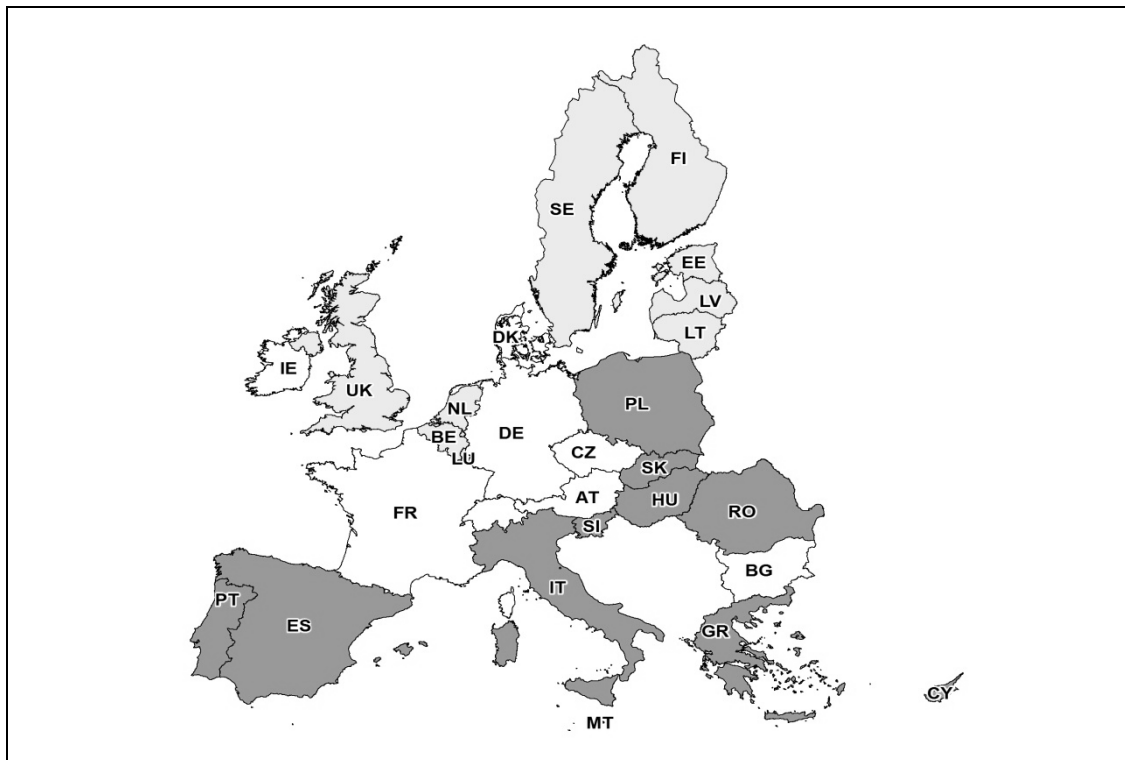
2008* includes crisis measures.

Source: State Aid Scoreboard, Autumn 2009 and Autumn 2004.

However, the last Scoreboard of Autumn 2009 no longer shows clear disparities between old and CEECs regarding the shares for sectoral aid (see Table 3 and 4, Annex). Nearly all member states have reduced their level of sectoral aid to a minimum, with the exception of Malta, Portugal and Romania.⁷ However, large disparities between member states remain in the share of aid awarded to various horizontal objectives. The predominant objective for horizontal aid in the 10 CEECs is aid for regional development (34% in 2006, 44% in 2008), followed by employment aid (17% in 2006, 19% in 2008). Aid for R&D (6%), environmental objectives (6%) and SME (4%) play only a minor role. In comparison, the most favoured objective in the EU-15 countries has been aid for environment and energy saving, to which 27% of aid were granted. However, differences in the allocation of aid measures among the member states do not clearly exist between CEECs and the EU-15 but rather between North-West and South-East Countries. Whereas the Nordic countries (including the Baltic State) spend nearly 100% of all aid to horizontal measures like R&D and environmental protection, the Southern countries allocate a large proportion of aid to sectoral or regional objectives (Figure 6).

⁷ The low share of horizontal aid in Malta can be explained by a tax relief measure under the Business Promotion Act 37, while in Portugal it is due to a large regional aid tax scheme (being phased out) in Madeira which in practice benefits a limited number of sectors. In Romania, a significant proportion of aid continues to be granted to the manufacturing sector as well as to the mining industry.

Figure 6:
Differences in the allocation of aid measures between North-West and South-East member States



Light grey member states: only horizontal measures, these mainly attributed to R&D and environmental objectives.
Dark grey member states: a large proportion of sectoral aid and horizontal aid mainly used for regional development or employment measures.

Source: State Aid Scoreboard: Autumn 2009; own presentation.

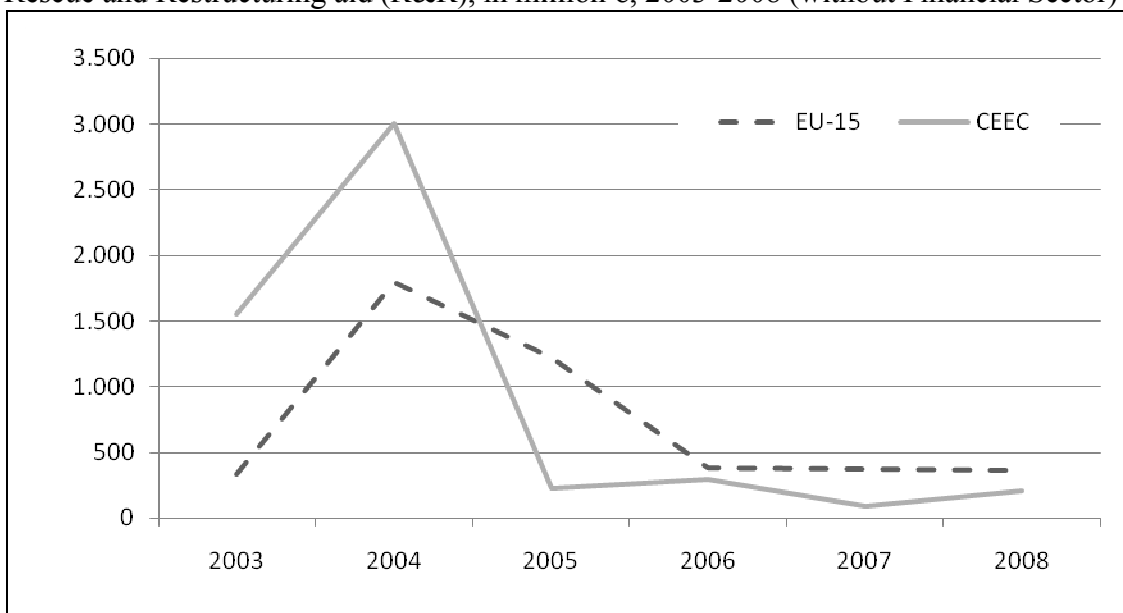
After accession, aid granted in CEECs in support of regional development and cohesion reached the highest shares in all years, the entire territory of each CEEC is eligible for regional aid under Article 107(3)a TFEU (ex 87(3)a TEC). This is particularly pronounced in the cases of Lithuania and the Czech and Slovak Republics and particularly low for Montenegro (not yet a member state) and Cyprus and Estonia.

SME programmes drew the attention of all post communist governments, as SMEs are key players in a market economy as they respond quickly to market signals and promote competitiveness (OECD 1992). However, SME support programmes have attracted only a small amount of resources. Contrary, the share of aid regarding rescue and restructuring (R&R) of companies started high (Hashi (2004) reports that in Poland 20% respectively 23% of all aid in 2001 and 2002 were used for this objective) and fell to a level similar to EU-15 member states (Figure 7). However, often R&R aid is supposed to be reported under employment schemes, e.g. in Poland in 2000: R&R aid amounted to only 7% whereas employment aid levelled at 24% (Hashi 2004, p. 16). Thus, the total amount of aid related to rescue and restructuring will be even higher. From a country

perspective, in the period 2004 to 2009 Poland showed the most cases with the objective to rescue or restructure an individual company or implement a scheme to do so.

Figure 7:

Rescue and Restructuring aid (R&R), in million €, 2003-2008 (without Financial Sector)



Source: State Aid Scoreboard: Statistical Tables, Autumn 2009

3.c Formal Investigation Procedures

Another indicator for the establishment of a state aid level playing field is the number of decisions to open a formal investigation, because such decisions must already summarise the relevant issues of fact and law. It further must include a preliminary assessment as to the aid character of the measure and set out the commission's doubts as to the compatibility with the common market.

Table 1:

Formal Investigation Procedures in CEECs, Years 2004 - 2009

	2004	2005	2006	2007	2008	2009	Total
State Aid Proceedings	32	146	176	119	107	111	691
No objections	27	134	161	110	101	103	636
Formal Investigation	5	12	15	9	6	8	55
Share of formal investigation	15,6%	8,2%	8,5%	7,6%	5,6%	7,2%	8,0%

Source: State Aid Register (Online Database).

The share of state aid cases, in which a preliminary assessment was followed by a formal investigation procedure, significantly fell after 2004 and in 2009 reached a mere eight per cent in comparison to over 15 per cent in 2004 (Table 1). Yet, huge differences among the CEECs exist: whereas the share in Poland, Rumania, and Hungary is above average (11, 28 and 10%), other member states were not yet confronted with a formal investigation procedure at all (Estonia, Lithuania).

3.d Final Decisions:

The existence of pre-accession state aid enforcement in the CEECs has not stopped the Commission from initiating formal investigation procedures into certain measures adopted before accession (Kuik 2004). Those pre-accession measures are not directly regulated by Article 107 and 108 TFEU, but by separate Protocols listed in the particular Accession Treaties.

Table 2:

Share of Positive and Negative Decisions, Share of Un-notified Aid, Years 2004 – 2010

	Positive*	Negative	Un-notified aid
EU-27	97.65%	2.35%	9.9%
EU-15	97.49%	2.51%	10.4%
CEECs	98.09%	1.91%	8.1%

* This figure includes not only “positive decisions”, but also all other decisions with a positive outcome (e.g. Art. 4(3) decision not to raise objections)

Source: State Aid Register, own calculations.

As Table 2 shows, the share of un-notified aid is lower in the case of the CEECs as compared to the old EU-15. As it can be assumed that the EU commission and not least competitors will keep a close eye on state aid granted, this does indicate that the governments in CEECs play by the rules. This is mirrored in the share of negative decisions, which is also lower in CEECs than in the EU-15 countries (1.91% compared to 2.51%).

We should not expect the EU commission to take a more permissibly stance towards state aid in the CEECs: since accession, the Commission released 15 negative decisions regarding state aid measures in CEECs. Thereof, nine cases required recovery of unlawful aid. The 15 decisions concerned aid measures in Poland (6), Hungary (5), Romania (1), Slovakia (3). Most of these cases concern the restructuring of companies (6) or a sectoral development (4), both objectives which are assumed to cause most distortionary effects on competition (See Table 6, Annex). A detailed discussion of selected state aid cases will be given in the following section.

4 Selected State Aid Cases

For this exemplary analysis we chose to analyse negative decisions as these are the cases most critical in order to reach a level playing field among all member states. In order to sketch some of the differences in EU state aid control between East and West, we compare a small selection of state aid cases in CEECs and in EU-15 countries. We take it that these examples are quite insightful with respect to our general conclusion that EU state aid control in the East is in fact strict: the gloves are off. The first case study relates to decisions in the steel industry being a very common subject to state aid proceedings. Furthermore, the case of ‘Huta Czestochowa’ has been the first negative decision requiring recovery in the CEECs. Another prominent sector in terms of state aid investigations is the shipyard industry. Two negative decisions in the CEECs regard state aid measures in favour of Polish shipyards, including the highest recovery amounts among the CEECs and thus an assumed large economic and social impact. In contrast, the last case study was chosen, because it regards a measure in an industry not traditionally affected by state aid proceedings as the affected company ‘Frucona Kosice’ produces consumer goods. Regarding the sample from EU-15 countries we selected cases from Germany and Greece that are to some extent comparable to the cases in CEECs and compare the decisions taken by the EU – again in support of our general conclusion.

4.a *Steel Industry*

The first negative decision that also required repayment of aid in a CEEC concerned aid in favour of the second largest Polish steel producer ‘Huta Czestochowa’ (HC). Restructuring aid in the steel sector is generally prohibited. However, the Polish government negotiated transition rules regarding state aid for the steel industry. HC could not take an advantage of the transitional rules as it was not listed in Protocol No. 8 of the Accession Treaty. This document, however, listed companies active in the Polish steel industry to receive restructuring aid. Initially, it was the aim of the Polish government to liquidate the company (Saryusz-Wolska 2010). However, the government decided in 2003 to restructure the company in view of a subsequent privatisation.

In 2004, the Commission opened a formal investigation concerning state aid granted by Poland to HC starting from 1997 onwards under the “interim-mechanism”. Albeit the final decision of 5th July 2005 found that measures taken for the restructuring process between 2002 and 2005 did not constitute state aid (the restructuring plans included a partial write-off of public and commercial debt claims), certain measures in the period prior to the restructuring (1997-2002) were found to be incompatible with the internal market: Poland had, in anticipation of the national restructuring plan, provided HC with restructuring aids amounting to approximately four million Euro. The Commission ordered recovery of these four million Euro.

The case has been novel as it concerned a pre-accession aid measure. And even though an exhaustive list of companies in the Polish steel sector were allowed to receive state aid and listed in Protocol No. 8 to the Accession Treaty, HC was not on the list. In fact, the company was taken off the list of beneficiaries in the last minute due to its financial difficulties. The parties argued before the General Court that the Commission did not have the power to investigate, as the state aid was granted between 1997 and 2002. The Commission on the other side argued that Protocol No. 8 is a *lex specialis* and extends monitoring to any aid granted for the restructuring of the Polish steel industry between 1997 and 2006. The Court agreed with the Commission and thus Protocol No. 8 builds the legal basis for the Commission to order recovery.

Further on, the parties challenged the way the commission had set the recovery interest. However, the commission was under no obligation to indicate the recovery rates in the decision itself. As the recovery interest had been set in close cooperation with Polish authorities, the order of the parties has been dismissed. Thus, Poland had to recover the four million Euro from HC. It is further worth mentioning that the amount thereby deemed unlawful has already been repaid. Out of the eight negative decisions in the CEECs that required recovery only the aid in favour of ‘Huta Warszawa’, another Polish steel producer, has already been repaid.

Under the national restructuring programme for the Polish steel industry and the special steel rules for Poland, Polish steel producer ‘Huta Warszawa’ (HW) received about 50 million Euro of state aid mainly in the form of a state guarantee for a loan to pursue its investment plan. However, HW had used around 30 million Euro of the loan in 2004 to pay off some old debts. The Commission found that this measure was neither indicated in the restructuring plan nor necessary for the restructuring, but, on the contrary, endangered the company's return to viability. The Commission therefore concluded that, that part of the aid had been misused and was incompatible with the Single Market. In 2005 Arcelor had taken over the company (AHW) and repaid the guaranteed loan and updated the business plan of the company in order to ensure long term viability. The Commission considered that the advantage stemming from the guarantee during one year was an interest subsidy for the loan amounting to around €2 million. In order to settle the case AHW agreed to repay this amount.

In Western Europe, especially companies in Spain and the German New Länder were subject to state aid proceedings regarding state aid measures for rescuing and restructuring companies in difficulties. One example is the ‘Eisenguss Torgelow GmbH’ (EGT) in Germany which received aid measures between 1998 and 2000 that were not prior notified to the Commission as it is required. After privatization in 1993 the company filed for bankruptcy in 1997. The company was sold to a group of investors but restructuring failed and the company filed again for bankruptcy in 2001. On 1 May 2001 EGT was declared bankrupt. While for the second time bankruptcy proceedings were under way, the firm was maintained as a going concern and the assets were sold to a new investor, CHL. In these two restructuring periods EGT received state aid measures total-

ing 9 million Euro, whereof 1.5 million are in question.⁸ The Commission concluded in its decision that the initial restructuring plan was not efficient in order to restore viability. This argument is supported by the second insolvency in 2001. Thus, aid in the height of 1.5 million Euro had to be recovered. The second restructuring and another sale of the company in 2004 brought the change. The number of employees increased from 64 in 2003 to 700 in 2008. Turnover rose from 5 million Euro in 2003 to 82 million Euro in 2007 and 140 in 2008.

Besides the East German example, also companies in the Western part of Germany have been found of having received unlawful aid. Two examples are the ‘Salzgitter AG’ (SAG) and the ‘Hamburger Stahlwerke’ (HSW). The Cases were decided 1995 and 2000. SAG received tax allowances according due to their special location close to the GDR border. However, the Commission found that SAG was not able to profit from the tax allowances as SAG is a steel company and, as such, subject to the stricter rules of the ECSC Treaty and the Steel Aid Code. The aid granted was incompatible with that legislation. HSW has been in financial difficulties and received a loan which the Commission found to be incompatible with the rules of the ECSC Treaty and the Steel Aid Code. In both cases, Germany has been ordered to recover the aid. However, in both cases the recovery has been delayed, also due to long court proceedings. Yet, both cases still belong to the list of pending recovery cases were the unlawful aid measures have not been recovered yet (State Aid Scoreboard 2009, Statistical Tables).

4.b Shipyards

The largest attention of all state aid cases was probably received by the Polish shipyards, not least due to its political implications (birthplace of Solidarnosc). On 1st June 2005, the Commission published its decision to open a formal investigation examining state aid measures in favour of three Polish shipyards in Gdynia, Gdansk, and Szczecin. Since 2002, the shipyards have benefited from several aid measures such as capital injections, guarantees, loans, and tax write-offs totalling several billions of Euros. Contrary to other sectors (and unlike Malta), Poland, with its relatively large shipbuilding industry, did not negotiate any transitional arrangements for the application of State aid rules to this sector. The investigation lasted more than three years; the case was meanwhile also negotiated between Commissioner Kroes and the Polish prime minister (Blauberger 2009). In November 2008, the Commission published its first two decisions coming to the conclusion that the aid granted to Gdynia and Szczecin constitute unlawful aid and subsequently have to be repaid.

⁸ The company site has received further 14 million Euro aid from the local government which does not fall under the European state aid rules as it derives from funds for investment in low developed regions, partly co-financed by European Fund for Regional Development and the European Social Fund. <http://freierjournalist.wordpress.com/2007/12/06/alles-giest/>

The two yards have been in difficulties since the 1990s. In April 2004, Poland notified restructuring aid for the two yards whereupon the Commission opened formal investigations in June 2005 (see IP/05/644). As EU state aid rules concerning the shipbuilding industry require aid to be based on far-reaching restructuring plans, the Commission required Poland to submit such restructuring plans, which occurred with substantial delays only in September 2005 and September 2006. The Commission came to the conclusion that none of the plans would have ensured long-term viability of the yards and the restructuring would have been financed entirely by state aid (also private capital is necessary in order to be in line with state aid rules). In December 2006, Poland decided to privatise the shipyards, a process, delayed several times, that finally led to potential investors submitting restructuring plans for the two yards on 12 September 2008. However, despite further large amounts of state aid and substantial job losses foreseen in these plans, the Commission found that the yards would still not have been commercially viable. Hence, the subsidies received by the Gdynia and Szczecin shipyards did not comply with the guidelines on rescue and restructuring aid but rather constituted illegal operating aid. The Commission decision required repayment of the illegal aid totalling 3.3 billion Euros. Poland committed that the recovery will be implemented by way of a sale of assets. The existing companies owning the yards, with the remaining assets and liabilities, will be liquidated. However, no investor was found and only a few assets of the shipyards could be sold. Thus, the repayment of unlawful aid could not have been complied with and the two shipyards had to declare bankruptcy at the end of 2009.

In contrast, in July of 2009 the European Commission has authorised the various support measures in favour of the Gdansk shipyard worth 251 million Euro. The company had been successfully privatised in 2007 to a Ukrainian industrial group (ISD). Initially, the new owner attempted to merge the shipyards in Gdansk and Gdynia, but the Commission rejected this plan, mainly because it was not sufficient to ensure a return of the yards to long-term viability. Subsequently, ISD presented a restructuring plan solely for the shipyard in Gdansk that has been financed to a large extent from private resources. The Commission concluded that the plan will ensure the viability of the yard and that the distortions of competition, caused by years of subsidised operations, will be adequately reduced by production capacity closures. The Commission decision of 2009 has authorised state aid granted to Gdansk Shipyard since 2004 when Poland entered the EU in order to finance the yard's restructuring. The decision also authorised production guarantees. As the continuous subsidies for the yard's production since 2002 caused a significant distortion of competition on the shipbuilding market, the yard's shipbuilding capacity has to be reduced substantially. According to the restructuring plan, the yard will close two of its three slipways.

The Commission investigation in the Polish shipyard cases may have been protracted due to strategic considerations. The Commission might have thought that it is disadvantageous to launch a potentially negative decision prior or parallel to the ongoing negotiations regarding the Treaty of Lisbon. The Commission released its negative decision one month after Poland had signed the treaty in October 2009.

Most negative decisions of the EC regard state aid measures in order to rescue or restructure companies. In most cases they fail the formal investigation due to a missing or unrealistic restructuring plan and a missing private investor financing the majority of the restructuring. Many decisions regarding state aid in East Germany during the 1990s concluded that without a private investor permanent losses are made or more state aid is necessary. In contrast, in cases where a private investor was found and a realistic restructuring plan was presented, the Commission came to a positive decision.

This is also reflected in the Polish shipyards cases. The Commission came to a positive decision in the case of the shipyard in Gdansk: the yard presented a restructuring plan and the restructuring has been financed to a large extent from private resources. Thus, the Commission concluded that viability of the yard will be given. Furthermore, distortions of competition, caused by years of subsidised operations, will be adequately reduced as production capacity will be reduced substantially. The situation is different in the other two cases: according to the EC none of the submitted restructuring plans would have ensured long-term viability to the yards and restructuring would have been financed entirely by state aid and not by a private investor. The Commission therefore concluded that the subsidies received by the Gdynia and Szczecin shipyards did not comply with the guidelines on rescue and restructuring aid but rather constituted illegal operating aid.

The shipyard sector in Europe is consistently subject to formal investigation procedures regarding the legality of state aid measures.⁹ Another European case concerns a shipyard in Greece: Hellenic shipyard (HSY). The Commission authorised aid measures in benefit of HSY in 1997 and 2002. However, in 2008 the Commission found, that conditions attached to the aid were not respected. HSY had not fully implemented the investment plan necessary to modernise the yard and exceeded the specified capacity limitation. Thus, the Commission came to the conclusion that aid measures totalling 230 million Euro constituted unlawful aid and have to be recovered.

4.c Consumer Goods

A third case in the CEECs regards state aid in favour of Frucona Kosice (FK), a medium-sized company in Eastern Slovakia, that used to be one of the major producers of distiller spirits and spirit-based beverages in Slovakia and currently operates as a distributor. In 2004, Frucona's accumulated tax debts amounted to nearly 17 million Euros. The company asked for an arrangement under the applicable insolvency legislation. In July 2004, the tax office agreed to write off 65% of its debt (11 million Euro). The

⁹ Currently, the European Commission discusses whether the framework for aid to the shipbuilding sector should be prolonged, revised or repealed. The current framework expires at the end of 2011. The Commission therefore also released a consultation in order to receive the opinions by the stakeholders. See Press Release IP/10/1280 from 4th October 2010.

Commission found that the tax office had not behaved as would be expected of a normal commercial creditor in a market economy. However, a state intervention must be made on the same conditions that a private creditor would have accepted, without taking account of socio-political considerations (such as regional or social policy). The Commission concluded that the tax office would have obtained a higher repayment of its claims through a bankruptcy procedure, in which the company would have been sold and the tax execution procedure would have allowed direct sale of the company's assets. The debt write-off therefore constituted state aid.

Such aid would have only been compatible with the Commission's guidelines on restructuring aid, if it were linked to a sustainable restructuring plan. Moreover, such aid can only be granted on the condition that the restructuring plan is properly implemented. Where this is not the case, the company is considered to have received operating aid, which has given it an unfair advantage vis-à-vis its competitors.

The Commission initiated the formal investigation procedure in July 2005. In June 2006, the final decision was published, ordering repayment of the unlawful aid. As Slovakia did not comply with the decision and the aid awarded to FK was not recovered, the Commission referred Slovakia to the European Court of Justice in May 2009 (Case-507/08). Even though the Slovak Republic vowed to recover the unlawfully granted aid in legal proceedings, the aid has still not been repaid yet. The first instance court dismissed the action *inter alia* because FK's obligation to pay its debt to the tax authorities arose *ex lege*. The appeal court upheld the judgment of the first instance court *inter alia*, because it was not possible to review the order concerning the arrangement. This was the case, because it must be respected by all bodies, including the appeal court and, also, because the Commission in the decision failed to respect the provisions of national law governing conflicts between bankruptcy and enforcement proceedings. The judgments of both courts prevent the immediate and effective execution of the Commission decision. It is not sufficient that the Slovak Republic made use of all means at its disposal. The application of those means must result in the immediate and effective enforcement of the decision, which the Slovak Republic must be considered as having failed to fulfil its obligations. A member state fails to fulfil its obligation to recover, if the steps taken by that member state have no impact on the actual recovery of those amounts.

Pending recovery decisions have a long 'tradition' in EU state aid enforcement¹⁰. However, in recent years the number of such cases is decreasing. The CEECs have besides FK four other pending recovery decisions (three in Poland and one in Hungary). The figures for EU-15 countries show that by December 2009 for 54 cases the recovery of the aid was still pending whereof the oldest not enforced recovery decision dates from 1997.

¹⁰ See chapter 2a Enforcement of State Aid Control in the European Union, page 9f.

One of the pending cases in the EU-15 countries regards an aid measure in France in favour of an American paper company. The case has been initiated by a complaint in 1996. The Commission concluded in its decision that the state aid in form of a preferential land price and a preferential rate of water treatment levy granted by France amounting to more than 18 million Euro is incompatible with the common market. The decision has been released in the year 2000. The last figures of the State Aid Scoreboard show that this case is still pending. Therefore in the year 2009 the Commission brought also this case to the ECJ.

In summary, these cases are exemplary in the sense that they show, that the Commission does not hesitate to enforce strict state aid recovery even for the period before EU membership, neither for large amounts, nor through involvement of the European Court of Justice.

5 Conclusions

For the new European members states, state aid is a sensitive issue in particular for politicians and society: large employers, for which previously the state was responsible, carry not only the largest burden in the industrial restructuring process during transition to a market economy but also over a much longer period of time than smaller privatized firms. The call to assist them by way of extending previous state subsidies is hence politically pressing.

Still, once having entered the EU as full members, those countries appear to be converging into the competition cultures: state aid may well be slightly higher than in the old member states, but comparative analysis does suggest that enforcement may be gradually becoming as effective and strict in the East as is the case in the West: Our quantitative analysis has shown that state aid does assume an increasingly horizontal character, in particular with regional cohesion objectives. The share of formal investigation procedures has fallen sharply in CEECs and the share of negative decisions is much lower than in the West, as is notably the share of un-notified aid.

The cases reviewed highlight in detail the strict enforcement of state aid policy in the CEECs. It became apparent in all cases that the EU commission executes strict state aid control in CEECs that even extends to the period before accession to the EU and adoption of the EU *acquis communautaire*. No special treatment is granted to the CEECs with their particular needs for industrial restructuring – the gloves are off. In fact state aid enforcement has been rather draconic: The first Polish example where unlawful aid was in fact paid retrospectively for a period before EU membership and the shipyard example where the inability of repayment led to bankruptcy and unemployment could hardly have been more drastic. The Slovak example shows that the commission uses its full arsenal of weapons, in this case a law suit against an EU member's government before the European Court of Justice.

We would hence conclude that state aid in the new member countries of the European Union is today not granted more generously than amongst the old members, it appears not to be more targeted at individual firms or industries. Our initial suspicion that state aid enforcement may be rather more lax in the East could not be verified, instead state aid policy has become at least as strict as in the West and a level playing field can today be assumed.

The current financial crisis has had a significant impact on state aid policy, and it will be particularly interesting for future research to test any differences emerging between CEECs and EU-15 countries in recent years. So far, we find no indication that the level playing field tends to tilt.

Annex

Table 3:
Share of Primary Objectives of Horizontal Aid in 2008 in CEECs, (as Percentage of Total Aid)

	CEECs	CZ	EE	LV	LT	HU	PL	SI	SK	BG	RO
Sectoral	13	6	0	0	0	19	7	11	16	9	47
Horizontal	87	94	100	100	100	81	93	89	84	91	53
Environment	6	1	15	21	13	5	8	15	13	0	6
Regional	44	68	6	47	73	41	39	47	64	13	15
R&D	6	18	23	2	0	4	1	12	1	15	26
SME	5	6	13	14	1	3	4	1	4	61	0
Training	3	1	5	2	10	3	4	1	1	2	0
Employment	19	0	1	1	3	18	7	11	16	9	47
Others	4	6	0	0	0	19	93	89	84	91	53

Source: State Aid Scoreboard, Autumn 2009

Table 4:
Share of Primary Objectives of Horizontal Aid in 2008 in EU-15 countries, (as Percentage of Total Aid)

	BE	DK	DE	IE	GR	ES	FR	IT	LX	NL	AT	PT	FI	SE	UK
Sectoral	1	6	13	16	2	21	4	15	0	2	1	84	2	0	9
Horizontal	99	94	87	84	98	79	96	85	100	98	99	16	98	100	91
Environment	11	16	40	5	2	12	2	2	15	65	42	0	38	86	41
Regional	10	0	23	17	76	40	41	18	10	1	8	7	6	6	10
R&D	48	9	17	15	2	19	25	19	36	18	23	1	29	4	19
SME	19	0	5	18	16	3	19	26	24	6	20	5	7	0	3
Training	4	0	1	10	0	1	0	7	0	0	2	0	1	0	2
Employment	4	66	0	4	0	1	2	7	0	3	1	4	6	0	0
Others	4	3	2	16	2	3	7	5	14	4	2	0	10	4	15

Source: State Aid Scoreboard, Autumn 2009

Table 5:
Share of Horizontal Aid 2000-2008 in EU-27 countries, (as Percentage of Total Aid)

	2000	2001	2002	2003	2004	2005	2006	2007	2008
EU-15	70	67	67	80	79	83	83	84	88
CEEC	41	29	29	21	34	61	71	75	87
Belgium	100	100	100	100	100	100	98	100	99
Bulgaria	-	-	52	36	65	73	79	92	91
Czech Republic	14	19	12	12	85	100	100	100	94
Denmark	98	98	95	94	89	98	97	94	94
Germany	64	61	51	74	77	80	85	82	87
Estonia	100	100	98	100	100	100	100	100	100
Ireland	36	43	48	65	72	76	80	82	84
Greece	97	91	84	94	97	98	98	98	98
Spain	44	38	70	68	64	65	73	70	79
France	75	68	73	77	64	90	97	95	96
Italy	89	96	93	95	94	83	72	86	85
Cyprus	28	26	32	22	46	45	96	95	95
Latvia	6	48	74	65	100	96	100	100	100
Lithuania	3	7	5	18	58	84	100	95	100
Luxembourg	100	100	100	100	100	100	100	100	100
Hungary	28	43	53	39	54	48	48	50	81
Malta	7	5	4	8	6	1	3	3	2
Netherlands	94	95	95	94	91	93	94	96	98
Austria	84	98	97	98	99	99	54	99	99
Poland	69	31	39	15	24	69	85	87	93
Portugal	35	23	17	19	19	12	12	10	16
Romania	-	-	42	35	23	48	45	43	53
Slovenia	75	56	84	81	69	87	88	85	89
Slovakia	78	43	50	72	61	60	95	76	84
Finland	85	97	97	97	97	98	97	96	98
Sweden	100	100	100	100	100	99	99	99	100
United Kingdom	84	91	77	99	99	90	91	92	91

Source: State Aid Scoreboard, Autumn 2009

Table 6:
State aid cases in CEECs with negative Commission decision, 2004-2010.

CASE CODE	CASE TITLE	MS	AID INSTRUMENT	NOTIFICATION DATE	DECISION DATE	DECISION	OBJECTIVES	PUBLICATION OFFICIAL JOURNAL
Steel Industry:								
C51/2006	Huta Warszawa	PL	Interest subsidy	06.12.2006	11.12.2007	negative decision with recovery	Restructuring firms in difficulty	JOCE C/35/2007, JOCE L/143/2008
C20/2004	Huta Czesochowa	PL	Debt write-off	19.05.2004	27.06.2006	negative decision with recovery	Restructuring firms in difficulty	JOCE C/204/2004, JOCE L/366/2006
C23/2006	Technologie Bucek	PL	Reduction of social security contributions	07.06.2006	23.10.2007	negative decision with recovery	Restructuring firms in difficulty	JOCE C/196/2006, JOCE L/116/2008
Shipyards:								
C17/2005	Gdynia Shipyard	PL	Debt write-off, Guarantee, Soft loan, Tax deferment	01.06.2005	09.09.2009	negative decision with recovery	Restructuring firms in difficulty	JOCE C/220/2005, JOCE L/33/2010
C19/2005	Szczecin Shipyard	PL	Debt write-off, Soft loan, Tax deferment	01.06.2005	09.09.2009	negative decision with recovery	Restructuring firms in difficulty	JOCE C/222/2005, JOCE L/5/2010
Automobile Industry:								
C46/2007	Privatisation of Automobile Craiova	RO	Debt write-off, Guarantee	10.10.2007	27.02.2008	negative decision with recovery	Sectoral development	JOCE C/248/2007, JOCE L/239/2008
Energy Sector:								
C41/2005	Hungarian Stranded costs	HU	Guarantee	09.11.2005	04.06.2008	negative decision with recovery	Sectoral development	JOCE C/324/2005, JOCE L/225/2009
C43/2005	Polish Stranded costs	PL	Direct grant	23.11.2005	25.09.2007	negative decision without recovery	Other	JOCE C/052/2006, JOCE C/063/2006, JOCE L/83/2009

CASE CODE	CASE TITLE	MS ^a	AID INSTRUMENT	NOTIFICATION DATE	DECISION DATE	DECISION	OBJECTIVES	PUBLICATION OFFICIAL JOURNAL
Financial Industry:								
C35/2004	Postabank	HU	Guarantee	20.10.2004	21.10.2008	negative decision without recovery	Sectoral development	JOCE C/068/2005, JOCE L/62/2009
Consumer Goods:								
C25/2005	Frucona Kosice	SK	Debt write-off	05.07.2005	07.06.2006	negative decision with recovery	Restructuring firms in difficulty	JOCE C/233/2005, JOCE L/112/2007
Others:								
C12/2007	Glunz&Jensen (Manufacturing of Machinery)	SK	Tax allowance	24.04.2007	11.12.2007	negative decision on notified aid not put into effect	Regional development	JOCE C/189/2007, JOCE L/178/2008
C57/2007	ALAS Slovakia s.r.o (Mining and Quarrying)	SK	Tax allowance	11.12.2007	04.06.2008	negative decision on notified aid not put into effect	Regional development	JOCE C/30/2008, JOCE L/248/2008
C21/2007	Ibiden Hungary Ltd (refractory products)	HU	Direct grant, Tax allowance	10.07.2007	30.04.2008	negative decision on notified aid not put into effect	Regional development	JOCE C/224/2007, JOCE L/295/2008
C1/2009	Alleged aid to MOL (Mining and Quarrying)	HU		13.01.2009	09.06.2010	negative decision with recovery	Sectoral development	JOCE C/74/2009
C29/2007	Short term export credit guarantee to SMEs	HU	Guarantee	18.07.2007	16.04.2008	negative decision on notified aid not put into effect	SMEs	JOCE C/234/2007, JOCE L/239/2008

^a MS = Member State

Source: State Aid Register

Table 7:
State aid cases compared to the CEEC case studies.

CASE CODE	CASE TITLE	MS	AID INSTRUMENT	NOTIFICATION DATE	DECISION DATE	DECISIONS	OBJECTIVES	PUBLICATION OFFICIAL JOURNAL
Steel Industry								
C77/2001	Eisenguss Torgelow GmbH	DE	Direct grant, Guarantee, Soft loan	30.10.2001	05.06.2002	negative decision with recovery	Rescuing and Restructuring firms in difficulty	JOCE C/063/2002, JOCE L/300/2003
C10/1999	Salzgitter AG	DE	Tax rate reduction	03.02.1999	28.06.2000	negative decision with recovery	Regional development	JOCE C/113/1999, JOCE L/323/2000
96/236/EGKS	Hamburger Stahlwerke	DE	soft loan	06.07.1994	31.10.1995	negative decision with recovery	Restructuring firms in difficulty	JOCE L/078/1996
Shipyards								
C18/2005	Gdansk Shipyard	PL	Debt write-off, Guarantee, Soft loan, Tax deferment	01.06.2005	22.07.2009	positive decision	Restructuring firms in difficulty	JOCE C/220/2005, JOCE L/81/2010
C16/2004	Hellenic Shipyard	GR	Debt write-off, Direct grant, Guarantee, Soft loan	20.04.2004	13.08.2008	negative decision with recovery	Restructuring firms in difficulty	JOCE C/202/2004, JOCE C/236/2006, JOCE L/225/2009
Consumer Goods								
C38/1998	Kimberly Clark/Scott	FR	Other: preferential land price, preferential rate of water treatment levy	20.05.1998	28.02.2001	negative decision with recovery	Regional development	JOCE C/301/1998, JOCE L/012/2002

^a MS = Member State

Source: State Aid Register

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