WHITE & CASE

# Commission launches long-awaited consultation on revised guidelines on State aid for rescuing and restructuring firms in difficulty

November 2013

On 5 November 2013, the European Commission launched a consultation on its proposed new guidelines on State aid for rescuing and restructuring firms in difficulty ("the draft R&R guidelines") which will replace the current R&R guidelines adopted in 2004. The revision of the 2004 guidelines was postponed a number of times as a result of the financial crisis, during which the Commission applied a special R&R regime for the financial sector. At the time, the Commission was still considering adopting new R&R rules applicable to both the financial sector and the real economy. In the end, the draft R&R guidelines will only apply to non-financial firms in difficulty. However, the Commission has drawn on its experience from the financial crisis in the preparation of the draft R&R guidelines, which would considerably tighten the conditions under which R&R aid may be approvable.

The main proposed changes are the following:

## Temporary Restructuring Support

First, the draft R&R guidelines introduce a new category of temporary restructuring support designed specifically for SMEs. Its aim is to promote the use of less distortive types of aid, such as liquidity assistance in the form of loans or guarantees which are limited in amount and time. Under the proposals, liquidity support would be possible for ailing SMEs as rescue aid for periods beyond 6 months (either 12 or 18 months depending on the outcome of the consultation). This is a welcome new tool, which is an eminently appropriate form of assistance for the real economy. Obtaining extended liquidity support is a major concern for ailing companies. Temporary restructuring support addresses this and enables companies to get liquidity assistance in a flexible way. However, its scope is unfortunately very limited since it only applies to SMEs, and for a very short term. In our view, this should be extended to the benefit of larger companies and for a longer period.

## Additional eligibility criteria/Counterfactual scenarios

Second, the draft R&R guidelines contain additional eligibility criteria to ensure that aid clearly serves a "common interest objective". In order to be deemed compatible with the Internal Market, the Member State will need to show that the granting of the aid will prevent social hardship or address severe market failures. The draft R&R guidelines provide a list of what situations are deemed to comply with these criteria. According to the draft, SMEs are to benefit from a less stringent standard when proving social hardship and market failure.

To establish the eligibility aid, the notification will have to be supported by a counterfactual scenario not involving State aid (this is not applicable to


For more information on the topics discussed in this alert, please contact:

**Mark Powell**
Partner, Brussels
mpowell@whitecase.com

**Kai Struckmann**
Partner, Brussels
kstruckmann@whitecase.com

**James Killick**
Partner, Brussels
jkillick@whitecase.com

**Christoph Arhold**
Counsel, Berlin
carhold@berlin.whitecase.com

rescue aid or temporary restructuring support).[1] The Commission's objective behind the counterfactual scenario is for the Member State to show that "the aid is truly in the public interest in a given case".

Our concern is that these high evidentiary requirements will in fact make it more difficult for many companies to be eligible for State aid, putting in jeopardy their objective, which was to simplify the rules. It is debatable whether it is actually the Commission's role to be dictating how Member States spend taxpayers' money.

## Burden Sharing

Third, in line with the current approach under the financial crisis regime, the draft R&R guidelines develop a concept of "burden sharing", under which the Commission will look not only at how much investors contribute but also at who contributes. This is intended to shift losses onto shareholders as much as possible.

Concretely, the Commission proposes two options. Under the first "broader" option, contributions would be required from incumbent shareholders and creditors, since they would be the ones to support the losses in a case of insolvency. Under the second "more precise" option, all past losses would have to be borne as a priority by shareholders and then, if need be, subordinated creditors would also have to contribute.

The notion of burden sharing is not new: it exists in the current R&R guidelines as a requirement for the company to make an "own contribution" which has been further developed in the financial crisis regime. While the draft guidelines go some way to clarifying this notion, some questions remain. For example, it is not clear how the burden sharing requirement would play out if the principal shareholder is the State itself (common in restructuring cases), and whether minority shareholders would also be implicated.

A potential consequence of applying this concept to the real economy is to make it more difficult for companies to be eligible for R&R aid. It may also make it harder for companies - not yet technically in difficulty - to have access to external financing. At the very least, it may be liable to increase the costs of financing due to the higher risks involved for creditors. Rigorous application of "burden sharing" may therefore prove to be counterproductive for the objectives pursued.

In addition, the proposal would considerably tighten the rules concerning the own contribution required from the aid beneficiary. While the current guidelines differentiate between minimum own contributions for small (25%), medium (40%) and large (50%) undertakings, the draft R&R Guidelines request an own contribution at least as high as the aid amount ("broader burden sharing option 1") or in an amount of at least 50% of the restructuring costs (option 2). This is further aggravated by the condition that contributions by the State in its capacity as shareholder or creditor would no longer be taken into account for the calculation of own contribution, even if they pass the Private Investor or Private Creditor Test. It is doubtful whether this approach is in line with the principle of equal treatment of public and private companies.

The situation for SMEs will be further complicated by their new obligation to provide a full-scale restructuring plan.

## Definition of "Firm in Difficulty"

The Commission is also seeking comments on the definition of "undertakings in difficulty". Under the current rules, this definition contains both so-called "hard" (objective) criteria and "soft" criteria which require a broader and more subjective assessment of the undertaking's situation. This over-reliance on

[1] It should be interesting to see if the Commission will use some of the findings of the study it commissioned from economics consulting firm Oxera on counterfactuals in restructuring aid.

the subjective criteria has been particularly criticised in recent years for creating much legal uncertainty. Therefore, in response to these concerns, the draft R&R guidelines now seek to shift the emphasis from soft to hard criteria to improve clarity and to align with other legislation, such as the *de minimis* Regulation. The soft criteria will continue to be taken into account, albeit in a residual way and only in exceptional circumstances. While such a definition is naturally welcome, the main challenge will be to use sensible indicators to define what constitutes hard criteria.

## Other proposed changes

- An increase in the minimum level of remuneration for rescue aid and incentives for beneficiaries to repay the aid as soon as possible;

- More detailed provisions on the required content of a restructuring plan;

- Measures to limit distortions of competition replacing the "compensatory measures" that apply under the existing guidelines, focusing less on protecting competitors and more on preserving competition in the market: the draft R&R guidelines now explicitly request that structural measures shall take place in the markets where the undertaking will have a significant market position after restructuring; in other words, divestments in order to focus on the core business may no longer be considered sufficient compensatory measures;

- Special provisions for SGEI providers;

- Eligibility for aid under R&R schemes extended to cover undertakings that fail to qualify as SMEs only because they are 25% or more State-owned. The maximum amount of aid that any one undertaking can receive under a scheme is reduced from €10 million to €5 million.

- Provisions on transparency and on *ex post* evaluation.

## Conclusion

By and large, the draft R&R guidelines contain some useful new concepts and clarifications such as temporary restructuring support and the definition of “undertakings in difficulty”. However, one of the practical implications of the new rules if they are adopted would be to make it more difficult to be eligible for rescuing and restructuring aid, and to comply with the compatibility criteria for its approval by the Commission. While further clarification is naturally welcome, the main challenge will be to use sensible indicators to define what constitutes hard criteria and allow for sufficient flexibility for taking into account specific circumstances of a given case.

## Next steps

As the Commission’s proposals are only in the context of a consultation, these are not yet final. The consultation is primarily targeted to institutions, public authorities, citizens, companies and organisations. Interested parties have until 31 December 2013 to submit their comments.

Should you have any further queries concerning the draft R&R guidelines, or would like to participate in the consultation, we would be happy to assist you.

Worldwide. For Our Clients.

**Brussels**
**White & Case LLP**
Avocats-Advocaten
rue de la Loi, 62 Wetstraat
1040 Brussels
Belgium
Telephone: +32 2 239 16 20
Facsimile: +32 2 219 16 26

www.whitecase.com