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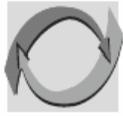


9th ASCOLA Conference Warsaw 2014 on
PROCEDURAL FAIRNESS IN COMPETITION PROCEEDINGS

State Aid and Fundamental Human Rights: State Aid Procedure and Procedural Fairness – A Contribution to the Right to Participate Debate

Luboš Tichy & Petra Joanna Pipková

CENTRE FOR ANTITRUST AND REGULATORY STUDIES, UNIVERSITY OF WARSAW
Warsaw, 26 – 28 June 2014



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State Aid and Fundamental Human Rights: State Aid Procedure and Procedural Fairness – A Contribution to the Right to Participate Debate

Luboš Tichy¹ & Petra Joanna Pipková²

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I. Introduction – problem definition and purpose of the contribution

It is commonly acknowledged that the beneficiaries and other interested parties have significantly less procedural rights than interested parties in other EU competition law proceedings, as the proceedings is meant to be bilateral (i.e. between the Commission and the Member State concerned) only.³This perception of the proceedings remains unchanged, although interested parties, especially the beneficiary, may be – as will be further shown – strongly affected by the Commission’s decision but also by the proceedings itself.

The subject of this contribution is, thus, the analysis of the question how far the European legal framework for the state aid procedure before the European Commission (i.e. the Regulation No. 659/1999, as amended, laying down detailed rules for the application of article 108 of the Treaty on the Functioning of the European Union – the regulation will be further referred to as the “Procedural Regulation”) complies with the fundamental procedural rights with regard to the position of the beneficiary of the state aid. The authors of this contribution have strong doubts regarding the question whether the position and procedural rights of the state aid beneficiary are adequate to his importance in the process of ascertaining of the distortion of competition, especially before the Commission, and, most importantly, whether they comply with the fundamental procedural rights he should enjoy according to the

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³ See e.g. Sinnaeve A., in: Heidenheim M. (ed.), *European State Aid Law*, C.H.Beck/Hart/Nomos 2010, 682, no. 1.

European law in force (i.e. with the European Convention on Human Rights and the Charter of Fundamental Rights of the European Union) and case law of the Court of Justice of the European Union. The authors first analyse the position of the state aid beneficiary and evaluate the current regulation of his procedural rights (chapters II and III). Further, the negative impacts of the current situation are described (chapter IV). Here, the authors derive from their own experience that, due to the rules in force, a range of problems arises, particularly with regard to transaction costs, and, therefore, that the current situation (i.e. the legal rules contained in the Procedural Regulation) needs to be reformed. The reform of the Procedural Regulation performed in July 2013 did not improve the beneficiary's position in any way. Thus, there is still need for a further reform. Consequently, the authors analyse how the fundamental procedural rights of the beneficiary are violated (chapter V). The authors present such a reform proposal at the end of this contribution (chapter VI).

2. Current position of the state aid beneficiary

According to the Procedural Regulation, the beneficiary has very limited procedural rights in proceedings relating to unlawfully granted state aid; albeit, the previous regulation was even more meagre in this direction. The Procedural Regulation contains a “whole” chapter on the rights of interested parties. This chapter consists of one single article summarising the rights granted to the interest parties throughout the regulation: the right to submit comments in the procedure on notification of state aid, the right to inform the Commission of an unlawful aid (which does not have the same consequences as a right to a formal complaint) and the right to obtain a copy of a decision of the Commission. It contains no right to an oral hearing, to access to the file or to obtain further information. Of course, the Commission may, if it deems it necessary, give the interested parties, including the beneficiary, an oral hearing or ask them to submit further information or comments. This is, however, on a facultative basis and may be used by the Commission arbitrarily.

The rights of the beneficiary are limited to the possibility of presenting statements expressing his opinion. However, there is no right of the beneficiary that would correspond to the Member State's right in art. 11 of the Procedural Regulation to submit comments. Thus, formally, the Commission is not bound to take into consideration the beneficiary's opinion or the relevant facts presented by him when issuing a decision on whether the aid was unlawful and has to be recovered by the Member State. In practice, the Commission usually allows the beneficiary to present his opinion but this has not the same status as submitting formal

comments. Thus, this informal practice cannot guarantee the beneficiary's procedural protection.

The beneficiary is not a party to the proceedings and he has no rights to access the proceedings files. He is, thus, completely unaware while it is, actually, being decided on him. It is the beneficiary who will have to pay the alleged unlawful aid back but he is unable to see what he should be defending himself against and, thus, cannot present any evidence to his advantage.

Not being party to the proceedings, the beneficiary has no genuine possibility to claim facts to support the dispensation of state aid recovery under art. 14 para. 1 sentence 2 of the Procedural Regulation. This provision provides for a dispensation from the obligation to recover if this would be contrary to a general principle of EU law. However, the beneficiary has no possibility to plead before the Commission that in his particular case the recovery of the state aid granted to him would be contrary to the general principles like fundamental rights or proportionality.⁴

Hence, the beneficiary has to rely on the Member State and confide his case into its hands, although he will be the one that will be burdened. The fact that the beneficiary has the possibility to challenge the Commission's decision before the EU courts does not alleviate his position, as many misunderstandings may be clarified already at the stage of the Commission's decision-making. The right to submit an appeal to the EU courts may only remedy a wrong that has already occurred. The ability of the beneficiary to participate in the proceedings before the Commission can prevent the emergence of the wrong. Probably everybody will agree that preventing a wrong from occurring is always better than its remedying.

The beneficiary's procedural rights are limited not only in the proceedings relating to the unlawful aid (contained in the arts. 10 and following of the Procedural Regulation) but also in the proceedings relating to notified aid (contained in the arts. 2 and following of the Procedural Regulation). Here, contrary to the unlawful aid proceedings, the beneficiary – as one of the interested parties – has the right to submit comments. However, his procedural rights are strictly limited to this one right as the Court of Justice of the European Union stated in his *Sytraval* judgement⁵ overruling the General Court's judgement⁶ who thought otherwise.

⁴ For more on general principles of EU law, please, see Tridimas T., *The General Principles of EU Law*, OUP 2006, 2nd ed.

⁵ Judgement of the CJEU C-367/95 P of 2 April 1998, *Commission v. Sytraval*, ECR [1998] I-1719, para. 59.

⁶ Judgement of the General Court T-95/94 of 28 September 1995, *Sytraval v. Commission*, ECR [1995] II-2654, paras. 53 and, especially, 78.

In its judgement, the General Court held that the Commission has, in certain circumstances, an obligation to exchange views and arguments with interested parties in order to justify to the requisite legal standard its assessment of the nature of a measure characterized as state aid. The Court of Justice opined that the rights of interested parties are limited merely to submit comments and that, consequently, the imposition on the Commission of an obligation requiring it to conduct an exchange of views and arguments with the interested party lead to conflict with the procedural regime laid down by art. 108.

On the other hand, since July 2013, the beneficiary is burdened with the obligation to reply to the information request. The non-compliance with this obligation is sanctioned as all the others procedural infractions in competition law with a fine that can amount up to 1% of the annual turnover. Hence, the beneficiary is burdened on one hand and does not acquire any real rights on the other. It is obvious that this imbalance of procedural obligations and procedural rights needs to be tackled.

However, the authors would like to focus preferentially on the procedural rights of the state aid beneficiary in the proceedings relating to unlawful aid in their contribution. The violation of fundamental procedural right here is far more acrid because these proceedings may be equalized with sanctioning proceedings within the meaning of the art. 6 of the European Convention on Human Rights given to it by the European Court for Human Rights, as we will see shortly.

3. Strict liability of the Member State and of the state aid beneficiary and its impact on the beneficiary

The whole philosophy of competition law shows that the infringer of competition rules (with the *de minimis* exception) is strictly liable. His mental attitude to his act or its result is irrelevant. A mistake is irrelevant either. It is solely taken into account when considering aggravating and extenuating circumstances and only in the area of arts. 101 and 102 of the Treaty on the Functioning of the European Union. The state aid category is completely free of subjective aspects. The good faith principle and the protection of legitimate expectations have only a limited application scope.

In state aid proceedings, the Commission examines only (i) whether there has been an intervention by the State or through State resources; (ii) whether the intervention gives the recipient an advantage on a selective basis; (iii) whether competition has been or may be distorted; and (iv) whether the intervention is likely to affect trade between Member States.

The Commission inquires only into the question of the unlawfulness of the aid granted by the Member State and determines whether the Member State has an obligation to recover the unlawful aid. The Commission never inquires into the beneficiary's attitude towards the aid it has received and the ability to return it. It just orders the Member State to recover the unlawful aid from the beneficiary who has nothing to say to its advantage, regardless of the means and of the Member State's ability to do so.

Even if it would be possible to claim subjective aspects of the beneficiary's relation to the aid granted he has no possibility to plead it.

From this results that it is the state aid beneficiary who shall be eventually strictly liable and compelled to return the received state aid entirely. In other words, there are no liberation (or exoneration) grounds on the side of the beneficiary. He cannot rely on the principle of legitimate expectation that the benefits he received from the Member State were compatible with the EU law. Such an assumption leads to the fact that the beneficiary is required to question any benefits it receives from the Member State, from its public authorities or even from individuals if their payments are founded on a legal act issued by the Member State or its authorities. Such a thorough analysis, including probably the private investor in a market economy test, constitutes a significant burden for the beneficiary. If the beneficiary is already required to conduct such an analysis, he should also be allowed to present the results of it in the proceedings before the Commission and rebut on its basis the Commission's evidence.

It should be further noted that the obligation to reimburse the unlawful aid to the Member State does not only cover the "granted" amount but also interests. These interests have to be "repaid" by the beneficiary even if he relied on the fact that the state aid was granted lawfully to him. Sometimes, he doesn't even have to consider the granted state aid as an advantage. It may be a measure that is activated *ex lege* and the beneficiary has nothing to say about it. He did not ask for it, he did not apply for it. Reimbursing the interests to the Member States may, thus, be considered not only as paying back of an advantage but also as a severe sanction.

In the authors' opinion, this means that the procedure regarding the recovery of the unlawful state aid fulfils the *Engel*-criteria of the European Court for Human Rights and constitutes criminal proceedings within the meaning of the art. 6 of the European Convention on Human Rights. According to the *Engel*-criteria,⁷ proceedings relating to an offence

⁷ See judgement of the European Courts for Human Rights nos. 5100/71; 5101/71; 5102/71; 5354/72; 5370/72 of 8 June 1976, *Engel and others v. The Netherlands*, para. 82.

represents criminal proceedings if either, (i) the provision(s) defining the offence charged belong to criminal law, (ii) the very nature of the offence classifies the proceedings as criminal, or (iii) the degree of severity of the penalty is of a specific intensity (i.e. the weight of the potential negative effects of the impending sanction is considered). These criteria are alternative. The authors consider the third criterion to be fulfilled. It is not the actual scope of the sanction but the abstract impending penalty (i.e. the maximum penalty) that is being considered.⁸ In state aid recovery cases, the sanction as defined above may be severe. Hence, the beneficiary needs to defend himself against it efficiently.

4. Negative effects – a practical example

The procedural provisions of the state aid law currently in force, including the possibly defective provisions in the Member States' internal legal systems, may lead, and in reality have already many times led, to enormous transaction costs. This may be observed on the example of the proceedings initiated on the basis of the initiative of the Slovak government (!) in the *Frucona* case. By a decision of the Commission, a Member State (Slovakia) was compelled to recover unlawful state aid (consisting in forgiving a fiscal debt in the framework of an insolvency procedure). The beneficiary filed an action seeking to overturn the Commission's decision to the General Court, which was dismissed by the latter. It was for the Court of Justice to acknowledge the beneficiary's claim the Commission and the General Court have not sufficiently evaluated the beneficiary's objections and to quash the General Court's judgement. It is now again for the General Court to decide on the case for a second time. The judgement was quashed by the Court of Justice because the General Court failed to establish whether the Commission had taken into account certain facts concerning the beneficiary. Obviously, the situation would be substantially clearer if the beneficiary had been able to participate fully already in the proceedings before the Commission.

At the same time as the EU courts were deciding on the Commission's recovery decision, Slovakia initiated civil proceedings to recover the unlawful state aid on the national level by filing an action in private law. The proceedings ended negatively for the claimant (i.e. Slovakia) up to the Supreme Court with dismissing judgements. The judgements of the Slovak courts were justified by the fact that *Frucona* went bankrupt and its obligation to pay the debt expired *ex lege* with the conclusion of the insolvency procedure. Hence, Slovakia was not in a position to comply with its obligation to recover. Consequently, the Commission

⁸ See Grabenwarter C., Europäische Menschenrechtskonvention, C.H.Beck/Manz 2005, 2nd ed., 291, no. 20.

initiated proceedings for infringement of the Treaty. The Commission obtained a positive Court of Justice judgement and Slovakia pursued new national proceedings; this time before the Slovak Supreme Court and the Slovak Constitutional Court.

In the end, in spite of the Slovak President's veto, a law had to be enacted that has changed the hitherto existing regulation in Slovakia. However, the initial proceedings regarding the Commission's decision on the unlawfulness of the state aid is still pending at the General Court after the annulling decision of the Court of Justice of the European Union. The entire proceedings take already almost ten years. The beneficiary's arguments acknowledged by the Court of Justice concerned primarily its bankruptcy situation and its evaluation in the light of the granting of state aid. These questions could be solved already on the Commission's level of decision-making if the beneficiary in general was entitled to participate genuinely on the proceedings before the Commission.

5. Fundamental procedural rights and the Procedural Regulation

Already the description of the state aid beneficiary's position in chapter II shows that his position under the current regulation is inadequate with regard to two aspects.

First, his position does not correspond with the importance of his role in the state aid proceedings. The beneficiary's importance for the proceedings is twofold. He, as the participant to the competition on the relevant market, can bring the relevant information necessary for the evaluation of the question whether the measure under scrutiny is indeed a selective advantage or whether competition was or is likely to be distorted. Further, it is eventually the state aid beneficiary who will assume the final liability for the unlawful state aid. It is him who will have to pay back the benefit including interests.

Second, the Procedural Regulation violates the European provisions on fundamental procedural rights that the European Union has pledged to abide to.

Above all, it violates the art. 6 of the European Convention on Human Rights. As has been already argued above, the procedure regarding unlawful state aid may be considered as criminal proceedings within the meaning of the art. 6 of the European Convention. As such, it must by all means abide to the imperative of fair trial. The fair trial principle is an umbrella notion for several procedural principles, like the principle of equality of arms, right to access to the case files, right to be heard or right to a justification of a decision.⁹ All of these principles or guarantees presuppose that the individual or legal entity against who will be

⁹ See e.g. Grabenwarter, 309, no. 60.

decided is party to the proceedings. This is not the case in the proceedings under the art. 10 of the Procedural Regulation.

The fair trial imperative requires “*a reasonable opportunity to present his case - including his evidence*”.¹⁰ The statements and the evidence have to be taken into consideration in the decision on merits. The Procedural Regulation does not contain even a hint of a guarantee of such an opportunity for the beneficiary.

The right to present his case presumes unambiguously the right to access to the case files. Only the full access to the evidence that the public authority has against the party to the proceedings guarantees that he knows which further evidence and statements need to be submitted to make the picture complete and veridical. For this reason, art. 6 of the European Convention requires that the prosecution authorities disclose to the defence all material evidence in their possession for or against the accused.¹¹ In spite of such a requirement, the state aid beneficiary has no possibility to access the case files of the Commission during the proceedings relating to unlawful state aid or during any other proceedings, although he should clearly have the status of a party to the proceedings. His only right is to obtain the issued decision, which is too late to exercise his fundamental rights guaranteed to him by the European Convention and taken away from him by a hierarchically lower legal act.

However, the beneficiary’s position under the Procedural Regulation is not only violating the European Convention but it is also in breach of the EU’s own fundamental rights provisions, i.e. the fundamental EU procedural rights guaranteed by the Charter of Fundamental Rights of the European Union. Art. 48 of the Charter states that “*respect for the rights of the defence of anyone who has been charged shall be guaranteed.*” The current Procedural Regulation does not respect this prerequisite.

The fact that the beneficiary has not even the possibility to access the files is a flagrant violation of the art. 48 and especially of art. 47 para. 2 of the Charter of Fundamental Rights of the European Union, constituting breach of the principle of due process and fair trial guaranteed by the EU itself.

One of the fundamental principles of procedural law in all legal systems is that if it is decided on the rights and obligations of a person this person is a party to the proceeding. The rule of law imperative requires the authority deciding on an individual’s rights and obligations to give this individual the possibility to explain the facts, to bring forward evidence, to

¹⁰ Judgement of the European Court for Human Rights no. 14448/88 of 27 October 1993, *Dombo Beheer B.V. v. The Netherlands*, para. 33.

¹¹ Judgement of the European Court for Human Rights no. 39482/98 of 24 June 2003, *Dowsett v. United Kingdom*, para. 41.

examine and question the evidence brought against him, to submit depositions or attenuating evidence that the authority has to take into consideration and deal with when issuing a decision on the merits.

The respect of fundamental procedural rights is not an objective of its own, it is means. It is an instrument of the protection of unjust decisions of public authorities. Sometimes, the respect of procedural rights helps the guilty ones; however, even those have the right to be protected against the public arbitrariness. What makes a state to a state abiding to the rule of law is the fact that a sanction proceedings does not amount to arbitrary retribution but that even the guilty party is granted the ability to defend oneself and justify its deeds. The law is not moral, it is value-free. Its objective is to protect the moral; thus, it cannot be morally just but it has to be procedurally fair. This fairness is characterized by the fact that even the party to be sanctioned has the opportunity to defend oneself effectively. The nature of proceedings is irrelevant. Thus, this principle applies also to procedures regarding unlawful state aid.

The negative effect of the violation of the fundamental procedural rights does not stop at the mere fact of a breach of a general principle, which is unfortunate on its own, but it spreads even further. The violation has impact on the outcome of the proceedings and burdens heavily not only the state aid beneficiary, but also the Member State who granted the state aid and the European institutions that have to deal with the subsequent proceedings aiming at rectifying the preceding potentially wrong decision.

It is obvious from chapter IV that had the state aid beneficiary in the *Frucona* case been able to fully participate in the proceedings before the Commission it would be possible to shed light on several aspects of the case in the proceedings' phase before the Commission. The fully-fledged participation would certainly have prevented the errors that were not discovered and taken into account until the Court of Justice had to decide which led to the case being returned back to the General Court. Thus, the fully fledged participation would most certainly have prevented the substantial transaction costs.

While all institutions, national or European, are trying to find measures that would reduce transaction costs both on the public and on the individuals' side, it is hard to understand why the European Union has not taken any steps that would reduce the transaction costs in this area. Proceedings the beneficiary has fully participated in will not only observe his fundamental procedural rights but will also increase the probability of his accepting the Commission's decision and, thus, by some amount decrease the number of appealed decisions.

6. Solution: reform proposal

Therefore, the authors propose to grant the state aid beneficiary the position of a party to the state aid proceedings before the European Commission and to amend the Procedural Regulation accordingly. The authors make this proposition in spite of their knowledge of the Council's and Commission's belief that a significant expansion of the rights of interested parties (to which category the beneficiary belongs) would neither be in accord with the system of state aid control under the Treaty, nor would it serve to improve the efficiency of such control.¹² The authors reject this opinion for several reasons.

First of all, as was already shown above, involving the beneficiary in the proceedings would help clarify a number of questions already in the "Commission's phase" of deciding. Further, the refusal to grant the beneficiary a status of a party to the proceedings is based on the assumption that the art. 108 para. 1 of the Treaty on the Functioning of the European Union lays down bilateralism of the state aid procedure as it speaks only about the Commission and the Member States. However, it does not speak explicitly about proceedings conducted by the Commission on particular cases; it just states that "*the Commission shall, in cooperation with Member States, keep under constant review all systems of aid existing in those States*" and that "*it shall propose to the latter any appropriate measures required by the progressive development or by the functioning of the internal market.*" Thus, in the authors' opinion, this provision does not oppose granting the beneficiary the right to take part in the proceedings. It only states, which parties should definitely be involved in the control procedures.

As for the argument that art. 108 para. 2 of the Treaty provides for an exhaustive list of rights of interested parties (the Treaty speaks of parties concerned), under this provision, the interested parties have the right to submit their comments before the Commission decides whether the aid granted by a Member State or through State resources is compatible with the internal market or not, or whether such aid is being misused, whether the Member State concerned shall abolish or alter such aid. In the authors' opinion, this provision only stipulates the minimum of procedural rights that must be granted to the interested parties. It does not lay down the maximum. Hence, it may not be considered as an exhaustive list of procedural rights of the interested parties, especially of the state aid beneficiary who will be burdened most by the Commission's decision.

¹² Sinnaeve, 682, no. 2.

In the authors' opinion, the state aid beneficiary should have the same or similar procedural position and same or similar procedural rights and obligations as the Member State who granted the unlawful state aid has. This should not only concern the proceedings relating to unlawfully granted state aid but also to proceedings relating to notified state aid to be granted. However, in the latter procedure, it must be considered that in many cases the particular beneficiary is not known until the state aid was granted as it is based upon a general legal act that affects a category of undertakings. In such a situation, it should be required from the undertaking claiming the status of a party to the proceedings on a notified state aid to prove that he is indeed an "actual beneficiary to be" within the meaning of the recent *Telefónica* judgement.¹³

Thus, in the proceedings on unlawful state aid, the beneficiary should be entitled to submit comments in the same manner as the Member States can under the art. 11 of the Procedural Regulation, and, further, to access the files or to submit evidence to his advantage. As for the procedure regarding notified aid, the Commission does not impose sanctions directly on the beneficiary; however, the decision relates to his interests and, further, the Commission has now the right to impose obligations on the beneficiary and sanction him for not complying with them. Therefore, the Procedural Regulation should balance the rights and obligations of the beneficiary and grant him at least some procedural rights next to the right to submit comments. For example, the beneficiary should be granted the right to access the comments of the Member State and of the other interested parties likewise the notifying Member State has (art. 6 para. 2 of the Procedural Regulation). The beneficiary may be in a position to dispel competition concerns referred to by the other interested parties. The beneficiary or the beneficiaries will of course not be subject to any sanctions; thus, their procedural position may be weaker than the position of the beneficiary of the state aid already granted. Nevertheless, granting him some genuine procedural position would be desirable, be it a position of a sort of an accessory party/notifier.

On the basis of the aforementioned, the authors have to stress that it is highly advisable to follow this proposal and to amend the Procedural Regulation once more in the described manner as the fundamental procedural rights need to be observed in all proceedings and the observance would significantly help to reduce transaction costs both on the side of the European institutions and on the side of the Member States and beneficiaries.

¹³ Judgement of the CJEU C-274/12 P of 19 December 2013, *Telefónica SA v. Commission*, ECR [2013], para. 46 ff.