



Deloitte Legal Newsflash

Public, Regulatory and Permits

What remains of the EU State Aid regime after the EU-UK trade deal?

The transition period that started on 31 January 2020, when the UK officially left the EU, came to an end on 31 December 2020. And while it looked certain that both sides were not going to come to an agreement regarding the trade relationship going forward, a deal came through at the final hour. Both parties concluded a “*Trade and Cooperation Agreement*” (TCA) setting out the economic relationship as of 1 January 2021.

It is no secret that the level playing field was one of the more challenging issues during negotiations. The UK wanted to break free of the EU State aid regime and ‘take back control’ of its subsidy policy. The EU demanded certain conditions in return for tariff-free access to their single market. It is thus no surprise that there is a specific section devoted to the subsidy control of both the UK and the EU in the agreement.

Substance

Scope

Title XI Chapter 3 of the TCA sets out bilateral commitments on subsidy regulation. At first glance, much of the terminology did not survive the transition from State aid regime to new trade arrangement.

Substantively however, the differences are not as significant as one would think. The definition of an ‘economic actor’ is identical to the definition of ‘undertaking’ under EU State aid law. Namely “*an entity or a group of entities constituting a single economic entity, regardless of its legal status, that is engaged in an economic activity by offering goods or services on a market*”.

What is and is not a subsidy also closely mirrors the definition of State aid. A subsidy must originate from state resources, it must confer an advantage, be specific (which in essence is equal to the selectivity criterium under State aid law) and have an effect or potential effect on trade or investment between the Parties (being the UK and the EU).

It is also expressly laid down that tax measures can be subsidies, encapsulating the three-step test of the Court of Justice of the European Union (CJEU). It can thus be expected that whenever the EU State aid rules apply to tax measures, the subsidy regime will equally be applicable.

Exceptions

Article 3.2 expressly limits the scope of what should be understood as a subsidy. Here again, there are many similarities to the EU State aid regime, with subsidies compensating for natural disasters or exceptional occurrences excluded from subsidy regulation, as well as subsidies with a social character.

As is the case under EU State aid rules, there is also a *de minimis* threshold built into the Agreement. What is noteworthy however is that it is set almost twice as high. The *de minimis* threshold under EU State aid is set at EUR 200,000 across three years. The threshold under the TCA agreement is set at SDR 325,000, which converts to approximately EUR 383,500.

Regarding Services of General Economic Interest (SGEI's), which are defined as 'Services of Public Economic Interest' under the Agreement, the threshold for *de minimis* subsidies is also higher than its counterpart under EU State aid rules. (SDR 750,000 or EUR 885,000 compared to EUR 500,000); as is the reporting threshold for SGEI's (SDR 15 million or EUR 17.65 million, compared to EUR 15 million under State aid regime). Apart from these differences, the rules regarding SGEI's set out in Article 3.4 strongly resemble State aid rules.

It is thus important to take into account that the TCA Agreement sets out monetary limits that give more freedom to the UK than what it was allowed under the current EU State aid regime. More aid can be given to an undertaking without falling under the subsidy control regulation.

Also noteworthy is the explicit exclusion of subsidies to the audio-visual sector, meaning that the film industry and broadcasters such as the BBC will not be hamstrung by limits of the Agreement. In addition, there is also an exclusion for temporary subsidies in response to a national or global economic emergency. What should be understood here is currently unclear, as it is not further defined in the Agreement.

Principles to take into account

In article 3.4, it is set out that no subsidy will be granted if it has a "*material effect on trade or investment*". What should be understood as a material effect is however unclear at the time of writing. The article further sets out the principles that need to be adhered to when granting subsidies. Attentive readers will notice that these principles closely resemble the basic principles developed by the European Commission to decide whether aid is compatible with article 107(3) TFEU.

The principles are:

- subsidies pursue a specific public policy objective;
- subsidies are proportionate and limited to what is necessary to achieve the objective;
- subsidies are designed to bring about a change of economic behaviour of the beneficiary that is conducive to achieving the objective;

- subsidies should not normally compensate for costs that beneficiaries would have funded themselves;
- subsidies are appropriate and that the objective cannot be achieved through other less distortive means;
- subsidies' positive contributions to achieving the objective outweigh any negative effects.

In interpreting these principles, the Joint Declaration on Subsidy Control Policies is noteworthy. It lays down how subsidies for the development of disadvantaged areas, subsidies to transport and subsidies to research and development can be accomplished within the framework of the TCA Agreement.

Prohibited subsidies and subsidies subject to conditions

Article 3.5 prohibits certain subsidies if they have a material effect on trade. These prohibited subsidies are unlimited state guarantees, export subsidies and subsidies stipulating the use of domestic products.

Article 3.5 also lays down special conditions for certain types of subsidies. Subsidies for rescuing and restructuring an ailing or insolvent economic actor will only be allowed if a realistic restructuring plan is drawn up. Bigger economic actors will also need to contribute to costs of the restructuring. An ailing or insolvent actor is defined as one that would almost certainly go out of business in the short to medium term without the subsidy. This more or less resembles the rules for rescue and restructuring aid under EU State aid rules, albeit not as detailed.

There are further special rules laid down for subsidies to banks, credit institutions and insurance companies. These subsidies must only be granted based on a credible restructuring plan, or not exceed what is needed to secure an orderly exit from the market.

Subsidies to regional airports and air carriers for new routes also have special rules, as well as subsidies for energy and environment, and subsidies for large cross border or international cooperation projects.

Immediate impact

Enforcement

The biggest impact of the transition to the new subsidy control system lies in its enforcement. Under EU State aid law, a mechanism of *ex-ante* control is used establishing that no aid may be distributed until it is notified and cleared by the European Commission, whereas the provisions of the TCA do not demand such a mechanism to be put in place.

However, this does not mean that there is no system of review in place to establish whether or not distributed subsidies are compliant with the commitments. Article 3.7 explicitly sets out a mechanism for transparency. The UK (and the EU) must publish information with respect to any subsidy granted or maintained within its territory, within 6 months after granting (or one year after tax declaration due date for tax measures). This would allow possibly interested parties to assess compliance with the principles set out in Article 3.4. Said parties also have the possibility to request further information through a letter, before taking action.

Should an interested party disagree with the granting of a subsidy, it will have the possibility to apply for a review conducted by a UK tribunal or court. It will then be up to the court to decide whether a granting authority has acted in compliance with the principles set out in Article 3.4 when granting the subsidy.

This mechanism creates more uncertainty for beneficiaries of subsidies, as they must take into account the possibility of a court declaring the subsidy's granting as incompatible with subsidy control rules. Article 3.9 sets out the commitments of Parties to establish an independent authority that must play "*an appropriate role*" in the subsidy control regime. Although what should be understood as an appropriate role is not defined, it is possible that this authority will in the future provide granting authorities and beneficiaries with some sort of clearance, providing them with certain assurances as to the compatibility of a subsidy. This however is not demanded in the Agreement.

Recovery

Article 3.11 lays down the obligation for the EU and the UK to put in place an effective recovery mechanism for incompatible subsidies, if an interested party has challenged the grant before a court in a timely manner.

Specificities

Remedial measures

In the new subsidy control regime, compatibility is thus enforced by UK courts instead of the European Commission and the CJEU. Should the EU not agree with the granting of a subsidy by the UK, it can appear as an intervening party in an ongoing court action in the UK, in accordance with Article 3.10.2 of the TCA Agreement.

Article 3.8 also foresees the possibility for the EU to request an explanation of how the Principles referred to in Article 3.4 have been respected with regard to a certain subsidy. The UK then has 60 days to provide the requested information.

Should any disagreement persist as to the possibility of a subsidy having a negative effect on trade or investment between the Parties, then the EU may request a consultation with the Trade Specialised Committee on the Level Playing Field, which will try to come up with a mutually satisfactory resolution within 30 days.

If this consultation does not produce a solution to the alleged problem, the EU will be able to take remedial measures against the UK, only if it can provide evidence that a UK subsidy risks causing a significant negative effect on trade. However, such remedial measures must be limited to what is strictly necessary and proportionate. Should the UK in turn not agree with the remedial action taken by the EU, it will be able to put the matter before an arbitration panel, which could eventually lead to the UK having to take remedial action itself.

It should be noted that these remedial measures are reciprocal. The UK has the same abilities to challenge subsidies granted within the EU should it find them problematic.

A more general disagreement as to the other Party's subsidy policy, or a failure to comply with what is set out in the TCA Agreement will be addressed through the general dispute resolution procedure.

Northern Ireland Protocol

A last point that should be taken into account, is that with the entry into force of this new subsidy control regime within the UK, there will now be two parallel systems applicable to certain subsidies granted in the UK.

Article 10 of the Northern Ireland Protocol established that EU State aid rules applied in full to measures with an actual or potential effect on trade between Northern Ireland and the EU. Such measures will thus still need to be notified to the European Commission, with the CJEU having the power to exercise judicial control. In the Agreement, there is no reference made to the Northern Ireland Protocol; it can therefore be assumed that this remains in effect.

Given the traditionally low threshold used by EU courts to establish an effect on trade, many UK subsidy measures can still be caught by the EU state aid regime, albeit indirectly through the Northern Ireland Protocol.

The exact application and scope of the Northern Ireland Protocol has been a contested issue since its inception, and will likely remain so for the foreseeable future. The fact that two separate subsidy regimes are now applicable will only make the issue more complicated and therefore more disputed.

Conclusion

With the transition period at an end, the UK will no longer fall under the EU State aid regime. Substantively however, the rules remain rather similar, and the possibility of this changing in the future is hard to predict given the uncertainty surrounding the scope of the Northern Ireland Protocol.

For now, the biggest difference is found in the procedure to establish whether subsidies are compatible, with the UK (for the time being) not using a system of *ex-ante* control but rather an *ex-post* mechanism through its own courts. This means that, in checking whether there is a case to be made before the courts, it will now be up to any possibly interested parties to monitor information made available in a public database to be set up.

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