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For further information please contact
Jan Schinner at: info@lexxion.eu
Tel.: +49 30/81 45 06-0 · Fax: +49 30/81 45 06-22

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Proportionality of the Sectoral Application of the Covid-19 Temporary Framework

*Sofie Holtan Lakså**

This article is adapted from the author's College of Europe Master's Thesis which was awarded the Lexxion Publisher prize for the Best Thesis on EU State aid.

One of the measures put in place to mitigate the effect of the Covid-19 pandemic on the European economy was the Covid-19 Temporary Framework. Adopted on 19 March 2020, it granted Member States flexibility under the State aid regime to support their national economies from their own pockets. While the relaxed rules were deemed necessary, the Framework was introduced with a known caveat: it is well-established that the granting of State aid distorts competition on the internal market. It is for the same reason that certain criteria have to be met for the Commission to approve the granting of aid, amongst them the principle of proportionality. This article argues that a large share of the aid approved under the Temporary Framework was in fact not proportionate to the shock caused by the Covid-19 pandemic, and should therefore not have been approved by the European Commission. The results demonstrate that the aids granted under the Temporary Framework cannot be considered proportionate in nature: of the 19 sectors analysed, the aid was found not to be disproportionate to the shock caused by the pandemic in only one sector.

Keywords: Temporary Framework; proportionality; subsidy race; COVID-19

I. Introduction

The first Coronavirus case in the European Union (EU) was reported already on 24 January 2020.[1] Not even two months later, the Coronavirus crisis was a fact and a wide range of measures were set in motion to dampen its impact on the continent. One of these was the State Aid Temporary Framework (Temporary Framework), adopted by the European Commission (Commission) on 19 March 2020. With it, Member States were granted flexibility under State aid rules to support their economies from their own national budgets.

The underlying principles of the Temporary Framework are the same as those of conventional State aid. A key criterion was that the aid amount and intensity must be limited to what was strictly necessary in order to reduce any distorting effects on the internal market.[2] In the context of the Temporary Framework, aid should therefore not exceed what was needed to offset the losses or damages caused by the Covid-19 virus outbreak.[3]

The ability of Member States to make use of the Temporary Framework depended on a range of factors, amongst others the mere fiscal capacity of the Member States and the practical and political ability to implement general protection measures to limit

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* Sofie Holtan Lakså, graduate, European Law and Economic Analysis, College of Europe, Bruges, and Analyst at Oxera Consulting LLP, Brussels.

1 Commission, 'Timeline of EU action in the context of the Coronavirus response' (Strategy and Policy, 2023) <https://commission.europa.eu/strategy-and-policy/coronavirus-response/timeline-eu-action_en> accessed 28 November 2023.

2 Commission, 'Staff working document: Common principles for the economic assessment of the compatibility of State aid under Article 87(3)' (2009).

3 Phedon Nicolaides, 'Application of Article 107(2)(b) TFEU to Covid-19 Measures: State Aid to Make Good the Damage Caused by an Exceptional Occurrence' (2020) 11(5-6) Journal of European Competition Law & Practice 238-243.

the spread of the Covid-19 virus, as well as the strategies chosen to do so.[4]

It is well-established that the Covid-19 pandemic had a significant impact on the European economy. In 2020 alone, the real GDP in the European Union contracted by an average of 4.5%, and while the Covid-19 pandemic hit the Member States' economies differently, also the initial conditions for the economies differed greatly. Germany, for example, was one of the economies in the Union that was less adversely affected by the pandemic, and still experienced a GDP contraction of 4% in 2020. However, Germany was by far the largest grantor of aid under the Framework, with aid budgets amounting to EUR 640 billion - more than three times larger than runner-up France. Greece, on the other hand, experienced the 2nd worst GDP contraction in 2020, of 9%, but granted 'only' EUR 21 billion under the Framework, around 30 times less the amount of Germany's approved aids.

This uneven distribution of aid has raised concerns about the effects of the Framework and its distortion of the level playing field of the internal market, both from scholars and the Commission itself.[5] Against this backdrop, one natural question is whether the Member States and the Commission, in its aids adopted and approved under the Temporary Framework, adhered to the principle of proportionality.

In its 2022 State Aid Scoreboard, the Commission assessed the proportionality of the aids implemented under the Temporary Framework.[6] While an ex-ante quantification of the damage suffered by each Member State was not performed before the Commission's authorisation to grant aid was given, this is now possible to undertake ex-post, even on a sectoral level.

This article sets out to explore whether the budgets of the aids approved across sectors were proportional to the actual economic disturbance.[7]

In the following, the term *aid* or *aid measure* is used to refer to separate grant packages authorised by the Commission. While one aid measure may contain several separate schemes, this analysis is however performed on the *aid* level. In other words, each aid package is considered as a whole, as opposed to the separate schemes it may contain.

The remainder of the article is organised as follows: the next section will present the Temporary Framework, Section III will then outline the methodology used, before the findings are presented in Section IV and further discussed in Section V.

II. The Temporary Framework

The Commission in its Communication of 13 March 2020 established that the pandemic affected all Member States and had an impact on all undertakings through the various containment measures adopted to limit the spread of the virus.[8] This led to the possibility of State aid being granted under the legal bases in Articles 107(2)(b) and 107(3)(b) TFEU, allowing aid to remedy damages caused by the Covid-19 pandemic as an exceptional occurrence and a serious disturbance to the economy respectively.[9]

The Temporary Framework, which was introduced on 19 March 2020, allowed for additional State aid measures to be found compatible under Article

4 Niccolò Battistini and Grigor Stoevsky, 'The impact of containment measures across sectors and countries during the COVID-19 pandemic' (ECB Economic Bulletin, 2/2021); Carole Maczkovics, 'How Flexible Should State Aid Control Be in Times of Crisis?' (2020) 19(3) European State Aid Law Quarterly.

5 See, for example, G Cannas, S Ferraro, A Mathieu Collin and K Casteele, 'Competition state aid brief' (Directorate-General for Competition (European Commission), 2022); Massimo Motta and Martin Peitz, 'State Aid Policies in Response to the COVID-19 Shock: Observations and Guiding Principles' (2020) 55(4) Inter economics 219-222; Jan Van Hove, 'Impact of state aid on competition and competitiveness during the COVID-19 pandemic: an early assessment' (Policy Department for Economic Committee on Economic and Monetary Affairs, Scientific and Quality of Life Policies, European Parliament, December 2020) <https://www.europarl.europa.eu/thinktank/en/document/IPOL_STU(2020)658214> accessed 28 November 2023.

6 European Commission, 'State aid Scoreboard 2022' (2023) <https://competition-policy.ec.europa.eu/state-aid/scoreboard_en> accessed 28 November 2023.

7 Acknowledging that the exact and projected size of the shocks were unknown at the time. Note that the 2022 State Aid Scoreboard (n 6), including an assessment of the State aids granted under the Temporary Framework, was published after the empirical work of this article was completed. The data provided by the Scoreboard has therefore not been included. Note also that the analysis and work of this article solely focus on the Temporary Framework adopted in connection with the Covid-19 virus outbreak, and not the Temporary Crisis and Transition Framework.

8 Kevin Kasser and Maria Claudia Solarte-Vasquez, 'Neutrality and Equality Aspects in the EU State Aid Temporary Framework 2020: The Case of the Airline Industry' (2022) 12(1) TalTech Journal of European Studies 99-122; Commission, 'Communication from the Commission to the European Parliament, the European Council, the Council, the European Central Bank, the European Investment Bank and the Eurogroup on Coordinated economic response to the COVID-19 Outbreak' (Communication) COM 2020/112.

9 Commission 'Coordinated economic response to the COVID-19 Outbreak' (n 9).

107(3)(b) TFEU and thus enabled the Member States to further support their economies with a base in their own national budgets.[10] The relaxed State aid rules were put in place under TFEU Article 107(3)(b) to remedy and prevent any further disturbance to the economy caused by the Covid-19 outbreak.[11] Alleviating a situation of sudden shortage or unavailability of liquidity for undertakings was the main aim under the initial version of the Framework.[12] Measures were foreseen in the form of direct grants, selective tax advantages, guarantees, loans and insurance schemes.

Any aid to be granted under the Framework had to be notified by the Member State and approved by the Commission as per the normal procedures, with a promise on the Commission's side of rapid processing. In its notification to the Commission, the Member State had to demonstrate that the measure in question was 'necessary, appropriate and proportionate to remedy a serious disturbance in the economy of the Member State concerned',[13] as the latter is a requirement for Article 107(3)(b) TFEU and thus also for the Framework to apply.

Measures were originally set out to be applied no later than 31 December 2020.[14] It was later amended on seven instances, the latest on 28 October 2022.[15] The end date of measures under the framework was extended to 30 June 2022 with the October 2021 amendment. Member States were however still allowed to grant certain investment and solvency support measures until the end of 2022 and the end of 2023.[16]

The aid measures in the Framework list specific conditions which had to be fulfilled for each category of aid to be found lawful. One example is that the beneficiary cannot have been in financial difficulty before 31 December 2019.[17] A requirement to quantify the actual loss suffered by the undertaking, however, is absent from the Framework.[18]

Although the Temporary Framework was put in place to ensure a level playing field, while providing Member States with the tools to mitigate the effects of the Covid-19 outbreak, it was acknowledged that the Framework both could and would have adverse effects on the internal market. The propensity, willingness and capability to grant aid vary across Member States and depend on a range of factors,[19] which again would have an impact on how much aid each Member State was fiscally able to grant under the Framework.

III. Methodology

The proportionality of the granted aid is assessed by comparing the budgeted amount of aid approved by the Commission with the negative shock experienced in terms of the contraction of GDP. The same approach was followed by the Commission in its own assessment of the proportionality of the Temporary Framework.[20]

The analysis is based on data made available by the European Commission in its Decisions under the Temporary Framework,[21] as well as from Eurostat on

10 Commission, 'State aid: Commission adopts Temporary Framework to enable Member States to further support the economy in the COVID-19 outbreak' (19 March 2020) <https://ec.europa.eu/commission/presscorner/detail/en/ip_20_496> accessed 28 November 2023.

11 Nicolaides (n 3).

12 Commission, 'Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak' (19 March 2020) <https://competition-policy.ec.europa.eu/state-aid/coronavirus/temporary-framework_en#:~:text=The%20State%20aid%20Temporary%20Framework%20was%20adopted%20on%2019th,context%20of%20the%20coronavirus%20outbreak> accessed 28 November 2023.

13 Commission 'Commission adopts Temporary Framework' (n 10) 19.

14 Commission 'Temporary Framework for State aid measures' (n 12).

15 Commission, 'Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak' (19 March 2020) <https://competition-policy.ec.europa.eu/state-aid/coronavirus/temporary-framework_en#:~:text=The%20State%20aid%20Temporary%20Framework%20was%20adopted%20on%2019th,context%20of%20the%20coronavirus%20outbreak> accessed 28 November 2023.

16 Commission, 'Amendment to the Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak' (Communication) COM 2022/C 423/04; Commission, 'State aid: Commission will phase out State aid COVID Temporary Framework' (20 May 2022).

17 Aid was naturally foreseen and permitted for undertakings facing financial difficulty because of the Covid-19 pandemic.

18 Michael Honoré, 'State Aid and COVID-19 – Hot Topics' (2020) 19(2) European State Aid Law Quarterly; Commission, 'Temporary Framework For State Aid Measures To Support The Economy In The Current Covid-19 Outbreak (Consolidated Version)' (Communication) COM 2021 8442.

19 Hussein Kassim and Bruce Lyons, 'The New Political Economy of EU State Aid Policy' (2013) 13(1) Journal of Industry, Competition and Trade 1-21.

20 Commission 'State aid Scoreboard 2022' (n 6).

21 Commission, 'Competition Policy: Search competition cases (all policy areas)' (2023) [Database] <https://ec.europa.eu/competition/elojade/isef/index.cfm> accessed 28 November 2023.

the economic activity across the different economic sectors in the Member States.[22] It is based on decisions running up to and including 18 February 2023. Subsequent updates and amendments to decisions have not been included.

1. Constructing the Database

Data about the State aid decisions was extracted from the European Commission's official list of State Aid Decisions.[23] Because of technical limitations, all decisions since the Temporary Framework was adopted on 19 March 2020, and until 18 February 2023, were extracted from the database and then filtered and sorted. Key parameters from the database included the case number, the granting Member State, the aid budget, the economic sector, and the decision date.

The decisions were first screened with the aim of filtering out those which had not been adopted under the Temporary Framework.[24] Note that decisions from the United Kingdom were also excluded, as were decisions with no aid budget amount available, those with indefinite aid amounts, and those without a publicly available version of the relevant Commission decision.

Next, all Commission decisions were read to refine and complete the dataset. First, original decisions were distinguished from amendments to existing decisions. Budget amounts of original decisions were then updated on the basis of subsequent amendments and reintroductions.[25] When the budgeted aid amounts were missing from the extract from the database, these were updated. Information on sectors were added when missing. These were determined based on Eurostat's Nomenclature of Economic Activities framework (NACE Rev 2), following the existing data from the Commission.

In the last and final step, the date of granting each aid was established and approximated by applying a three-month lag to the date of the Commission's decision.

Note that this resulted in a final list of 712 original decisions taken under the Temporary Framework, and 551 amendments. The budgeted aid amounted to a total of EUR 1.502 trillion. There is a discrepancy between these numbers and those provided by the European Commission in its various publications, whereas the Commission presents numbers close to EUR 3 trillion.[26] A handful of factors have an influence on this, but it is important to note that the distribution of aid granted per Member State in the data is consistent with the numbers reported by the Commission.[27] Moreover, all decisions listed as adopted under the Temporary Framework as of late December 2022 by the Commission itself are included.[28] The database is therefore considered to reasonably reflect reality.

Note also that the database, and thus also the analysis, does not differentiate between the *form* of aid granted by the Member States, and neither is the *actual* aid amount calculated. This is an important caveat, as it implicitly assumes that the aid component of a loan is equal to that of, for example, a grant.

A descriptive summary of the resulting data on adopted aid is presented in Section IV.

2. Sectoral Developments Absent the Covid-19 Pandemic

The sectoral and overall shocks, proxied by contraction in GDP, are estimated as the difference between the actual output and the projected output, the counterfactual, without the Covid-19 outbreak. GDP data was obtained from Eurostat.[29]

The shocks to the overall GDP in a Member State, are calculated based on each Member States' 2019 GDP combined with the last EU-wide economic fore-

22 Eurostat, 'National accounts aggregates by industry (up to NACE A*64)' (6 April 2023) <https://ec.europa.eu/eurostat/databrowser/view/NAMA_10_A64__custom_5813275/default/table?lang=en> accessed 28 November 2023.

23 Commission 'Competition Policy: Search' (n 21).

24 For example, aid granted under the Temporary Crisis Framework, Regional Guidelines, and so on.

25 Reintroductions were treated as amendments.

26 Commission, 'Report on Competition Policy 2021: Commission Staff Working Document Accompanying the document Report from The Commission to the European Parliament, the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions' (26 August 2022) <https://competition-policy.ec.europa.eu/publications/annual-reports_en> accessed 28 November 2023.

27 ibid 26.

28 Commission, 'Coronavirus Outbreak - List of Member State Measures approved under Articles 107(2)b, 107(3)b and 107(3)c TFEU and under the State Aid Temporary Framework' (last modified 20 December 2022) <https://competition-policy.ec.europa.eu/system/files/2023-05/State_aid_decisions_TF_and_107_2b_107_3b_107_3c.pdf> accessed 28 November 2023.

29 Eurostat (n 22).

cast and projections for each Member State's economy prior to the onset of the COVID-19 pandemic.[30]

The sectoral shocks are obtained by linear projection based on data from 2009-2019 in order to forecast the GDP of the respective sectors in 2020 and 2021, absent Covid-19. While this implicitly assumes a linear growth in all sectors, it facilitates an initial analysis based on the trends in the various sectors over the decade prior to the COVID-19 pandemic.

IV. Results

The descriptive characteristics of the database and the Commission's decisions under the Temporary Framework are presented first. Next, the non-specific aid will be presented, ie those with no specific sectors targeted by the measures. Finally, the different sectors will be presented, focusing first on the hardest hit, being those related to transport, hospitality, retail, culture and tourism,[31] before a summary of the remaining sectors is given. The findings are further discussed in Section V.

1. Descriptive Summary

A total of 712 decisions were adopted under the Temporary Framework in the period between 19 March 2020 and 18 February 2023. One third of these were granted by three Member States only: Italy, Belgium, and Czechia. Italy alone provided for almost 90 aid measures by itself. Spain had eight aid measures cleared, the fewest under the Temporary Framework.

The majority of the absolute aid amounts authorised under the Framework relates to Germany. With more than EUR 640 billion budgeted, Germany granted the largest amount under the Framework, with the second and third largest France and Italy budgeting for a more modest EUR 200 billion each. With a total of EUR 1.502 trillion budgeted under the Temporary Framework, this implies that over two thirds of the aid was granted by three Member States alone. Next are Spain, Poland and Belgium with EUR 92, 70, and 67 billion respectively, leaving the remaining 15% to the other 21 Member States.

Germany also dominates on the average budget per measure, with almost EUR 42 billion per aid measure adopted. This is almost fourfold Spain, which ranks second with an average of EUR 11 billion per aid measure. Most Member States' averages were well below also this, and in fact, most even below EUR 2 billion.

Among the sectors worst hit by the Covid-19 outbreak were transport, tourism, culture, hospitality, and retail.[32] Observing the aids granted to these in connection with the trends outlined above, with large and fiscally strong countries such as Germany, France, and Italy granting the majority of the aids under the Framework,[33] may give an indication as to whether the concerns around the impact of the Temporary Framework on the level playing field of the internal market are well-founded or not.

2. General Aids Granted Under the Temporary Framework

Of the 712 decisions adopted under the Temporary Framework, 271 were of a general nature, that is, aid with no specific sector targeted by the measure. These are summarised on Member State level in Figure 1.

The dotted line represents the proportionality threshold, that is, where the aid granted is equal to the GDP contraction, or the shock, that the aid is to remedy for. Any observation below the threshold is to be considered proportional, meanwhile any above is considered disproportional in the sense that the amount of aid granted is overcompensating the shock.

As seen in Figure 1, many Member States granted aid in both 2020 and 2021 which was significantly larger than the GDP contraction experienced in the associated years. This means that the aid was overcompensating and therefore in breach of the principle of proportionality. Examples of this are especially Germany, Hungary, Ireland, Italy, Belgium, Czechia, Poland, Spain, and Sweden. In 2020, the non-sector specific aid granted by these Member States were many times higher than the actual shock. In Germany alone, the difference between the aid granted and the shock in the economy amounted to

30 Commission Directorate-General for Economic and Financial Affairs, 'European Economic Forecast. Autumn 2019' (2019) Institutional Paper (115).

31 Jan Maarten de Vet, Daniel Nigohosyan, Jorge Núñez Ferrer, Ann-Kristin Gross, Silvia Kuehl, and Michael Flickenschild, European Parliament Think Tank 'Impacts of the COVID19 pandemic on EU industries' (March 2021).

32 Commission 'Temporary Framework' (n 18).

33 ibid.

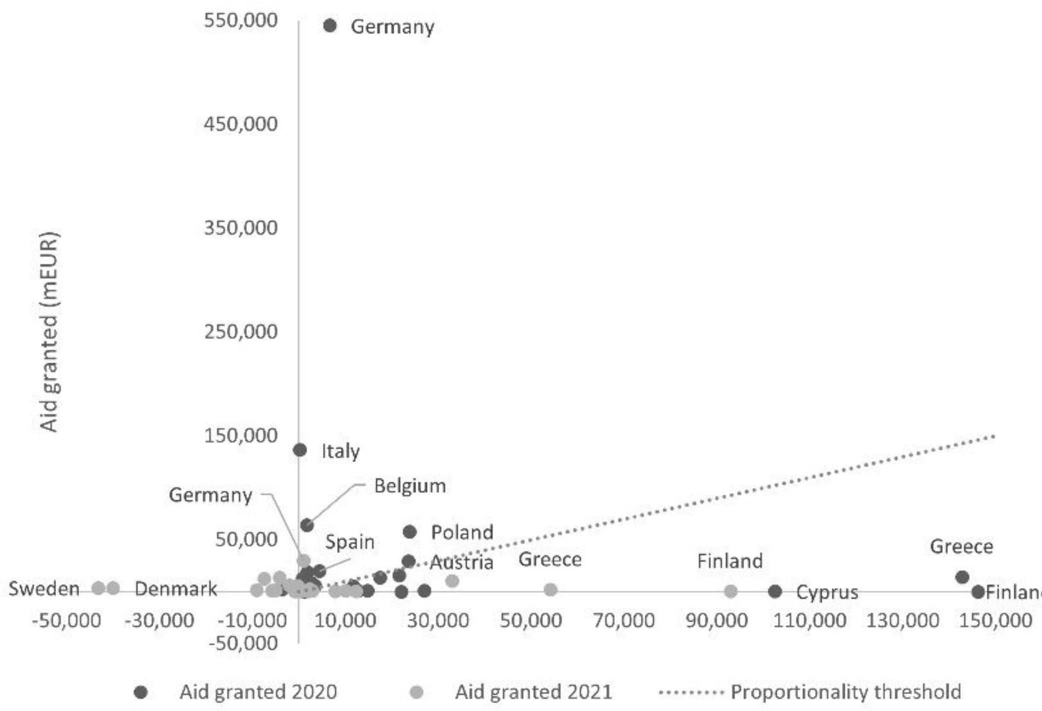

Figure 1: Overview of non-sector specific aids granted and general shocks to GDP per year per Member State

more than EUR 500 billion. Greece, for comparison, experienced a shock of EUR 142 billion, but granted no more than EUR 14.2 billion in general aid in 2020.

Any observation to the left of the vertical axis indicates that the shock in the given year was positive, meaning that the GDP in fact grew compared to the counterfactual. Also, in this case, the aid would be considered disproportionate, as there was no shock to remedy. In these cases, no aid would be considered proportionate, neither under the Temporary Framework nor Article 107(2)(b), as in theory there is no damage to remedy or counteract. Note however that this may not be the case on sectoral levels, as will be shown in the following sections.

These general results presented in the previous sections may hide developments in certain sectors. Note that these do not include sector-specific aid.

3. Sector-based Analysis

Aids amounting to about EUR 420 billion were granted to specific sectors. These are presented in the following sections, before an overall discussion on the main findings is presented in Section V.

a. Preliminary Clarifications

The term *aid* or *aid measure* refers to separate grant packages authorised by the Commission. While one aid measure may contain several separate schemes, this analysis is performed on the *aid* level. In other words, each aid package is considered as a whole, as opposed to the separate schemes it may contain. *Granted aid* refers to the total budget per aid that has been authorised by the European Commission, unless explicitly stated otherwise. The aid *actually* granted may differ from this number, but granted aids is deemed an appropriate simplification for the purpose of the analysis, as it nevertheless reflects the fiscal room for manoeuvre granted by the Commission. Note also that the analysis does not differentiate between the *form* of aid granted by the Member States, and neither is the *actual* aid amount taken into account. This simplification constitutes an important caveat, as it implicitly assumes that the aid component of a loan is equal to that of, for example, a grant.

The results presented in the following only include information from the Member States who granted aid to the sector discussed in each subsection. Sectoral data from 2021 is not fully available for Sweden and Croatia, and these are therefore not included.

The following sections will focus on the sectors hardest hit and deemed essential for the Union, including transporation (NACE code 'H'), accommodation and food services (I), and the arts, entertainment and recreation, and agriculture (A) sectors.[34]

Thereafter, the findings of the remaining sectors are summarised: Mining and quarrying (NACE code 'B'); Manufacturing (C); Electricity, gas, steam and air conditioning supply (D); Water supply, sewerage, waste management and remediation activities (E); Construction (F); Wholesale and retail (G); Information and communication (J); Financial and insurance activities (K); Real estate activities (L); Professional, scientific and technical activities (M); Administrative and support service activities (N); Public administration and defence; compulsory social security (O); Education (P); Human health and social work activities (Q); and Other service activities (S).

b. Transportation and Storage

The transportation and storage sector includes, besides air transport, land, water and rail transport related both to passenger and freight, also services related thereto, such as airports.[35] The sector contributes with 7% of the value added and accounts for 8% of employment in the EU.[36]

Transportation and storage was a targeted sector in 109 decisions, of which 26 were targeted at airlines and airport operators and their staff. Aids given in the sector have received great attention, amongst them being Lufthansa itself claiming that the EUR 9 billion bailout it received from Germany was not strictly necessary,[37] thus being challenged in front of the General Court as unlawful aid.[38] Another example is the Irish low-cost airline Ryanair's decision to challenge a wide range of aids granted to other airlines.[39]

The estimated shock in the transportation and storage sector in 2020 amounted to EUR 167.6 billion. In 2021, the picture was different and the sector had an output that was EUR 17 billion higher than what was projected before the Covid-19 outbreak.

As seen in Figure 2, there was only one incident of aid being granted that was larger than the respective shock. This was in the Netherlands, which in 2021 granted a loan to its national flag carrier KLM.[40] While the budget of the decision was EUR 3.4 billion, the shock in the transport sector as a total amounted to only EUR 526 million. While this indicates a disproportional grant, the Dutch transport sector contracted by EUR 9.6 billion without being granted any State aid in 2020. The aid grant may have been a follow-on from the contractions in 2020, and may then also be considered proportional in this context after all. Note also that the Dutch measure was a loan: The full EUR 9.6 billion did therefore not constitute aid as such to the firm.

Meanwhile, it is also clear that there were several incidents where aid was granted despite there not being an economic shock to the sector in the given year. Before strictly concluding that these were not grounded for, it is to be noted that as with the Netherlands, these Member States also had negative shocks in their respective national sectors in 2020. This may therefore also be attributed to methodological weaknesses as the lag between the aid approval by the Commission and the aid grant may have been shorter than three months. The shock may also have been present in certain periods in which the annual classification of shocks does not provide for.

Nevertheless, the results indicate that a total of 11 Member States granted aid under the Temporary Framework in cases in which there was no shock to

34 de Vet and others (n 31).

35 Eurostat, 'NACE Rev. 2: Statistical classification of economic activities in the European Community' (2008) Methodologies and Working papers: 363 <https://ec.europa.eu/eurostat/documents/3859598/5902521/KS-RA-07-015-EN.PDF> accessed 28 November 2023.

36 Eurostat, 'Covid-19 had a strong impact on businesses in the transportation and storage sector in 2020' (2023) 7, <https://ec.europa.eu/eurostat/statistics-explained/index.php?title=Businesses_in_the_transportation_and_storage_sector> accessed 28 November 2023.

37 Joe Miller and Peggy Hollinger, 'Lufthansa chief says €9bn bailout larger than needed for survival (Financial Times, 2020) <https://www.ft.com/content/5c32cd83-e639-4421-9ae2-8165ecdd5097> accessed 28 November 2023.

38 See SA.57153 – Germany – COVID-19 – Aid to Lufthansa C(2021) 9606.

39 PwC, 'Ryanair - State Aid' (2023) <https://blogs.pwc.de/en/german-tax-and-legal-news/article/235549/ryanair-state-aid/> accessed 28 November 2023.

40 See SA.57116 – Netherlands – COVID-19: State loan guarantee and State loan for KLM 2022/C 357/01.

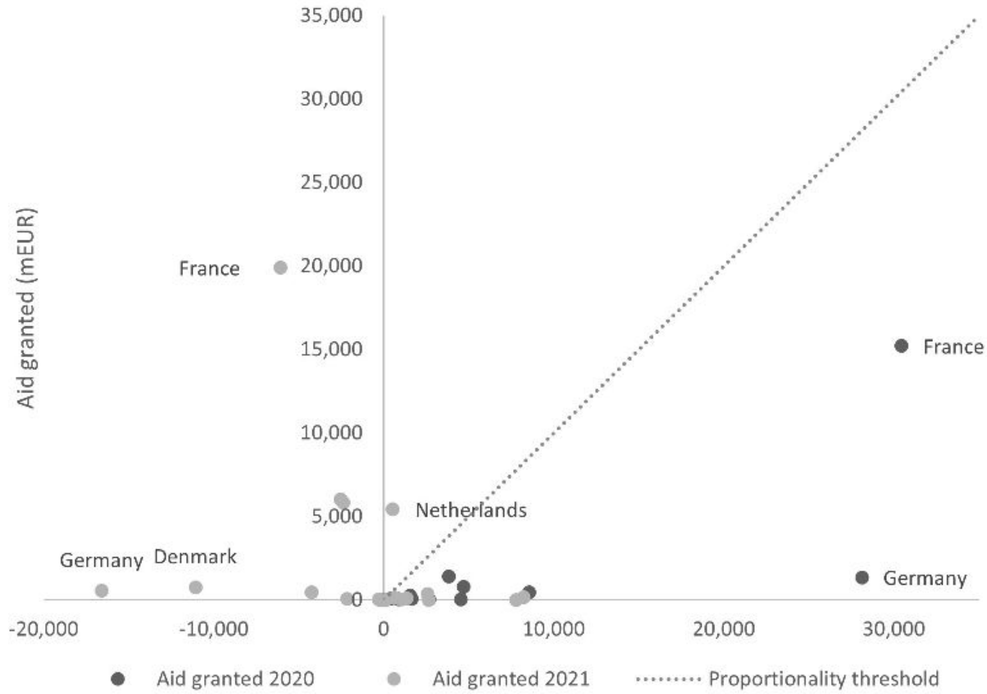

Figure 2: Transportation and storage: Overview of sectoral aids and shocks per year per Member State in mEUR

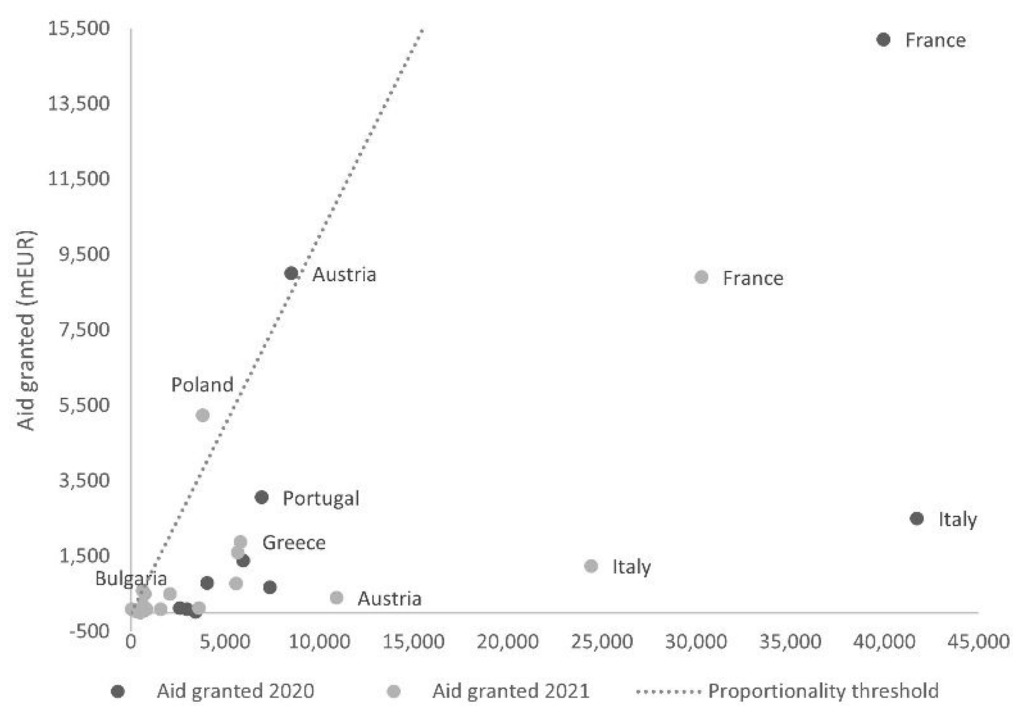

Figure 3: Accommodation and Food Service Activities: Overview of sectoral aids and shocks per year per Member State in mEUR.

remedy for. The aid given in 2021 includes French support to its national airline Air France[41] as well as KLM,[42] German aid to Berlin Brandenburg Airport,[43] and Danish and Swedish loans to Scandinavian Airlines.[44]

c. Accommodation and Food Service Activities

The accommodation and food service sector was among the worst hit in 2020 and 2021, with contractions of EUR 252.6 and 191.6 billion, respectively. Activities in the sector include the provision of hotel rooms and other accommodation, restaurants, bars, night clubs, catering, and so on, and are key to the tourism industry.[45] The sector is of special importance in certain Member States, where it for example in Greece contributes to over 20% of the employment in the non-financial Greek economy, and in Cyprus just above 16% of total employment.

Of the 95 measures available to the accommodation sector, only seven were targeting it as the only one. Most measures targeted it as part of the wider tourism-related industry, aiming to support also for example the transport, arts, recreation and culture sectors. One should therefore be cautious to quantify and pinpoint the overcompensation in this sector, although there are indications of it as seen in Figure 3. This was the case for Austria's EUR 9 billion aid in 2020, which was open to a handful of sectors, all of them in tourism-related industries.[46] The same was the case for Poland[47] and Bulgaria[48] in 2021, all three of them making available more aid to their national sectors than the corresponding shock.

d. Arts, Entertainment and Recreation

The arts, entertainment and recreation sector includes, besides concerts and other live performances also libraries, museums, sports activities and fitness facilities.[49] As a sector highly dependent on physical presence and contact, it was hit hard by the Covid-19 outbreak and the containment measures that followed.[50]

Overall, the sector experienced a shock of EUR 65.1 billion in 2020 and EUR 53.7 billion in 2021. As seen in Figure 4, a great amount of aid was directed towards the culture sector. A total of 116 measures targeted it, amounting to a total of EUR 67.2 billion, granted by 25 Member States. Many of these were however targeting a handful sectors at once.

All the aids granted by Member States in 2020 and 2021 above the dotted line, indicating overcompensation, were targeted at several sectors, with the exception of a handful of minor Czech and Greek schemes directed at the culture sector alone. These amounted to EUR 112 and 20 million, respectively.

e. Agriculture, Forestry and Fishing

The agriculture sector experienced a negative shock of EUR 15.3 billion in 2020 and a *positive* shock of EUR 15.4 billion in 2021. The sector includes broadly crop and animal production and hunting, and service activities related thereto, in addition to forestry and logging and fishing and aquaculture.[51]

Figure 5 indicates that aid granted to the sector was overcompensating and thus not proportionate in Czechia and Italy. However, while the Czech aids granted in both 2020 and 2021 are large in size, these are both also measures that target several sectors.[52] The same is the case for the Italian aid in 2020, which includes a measure of EUR 2.5 billion targeting several other sectors.[53]

41 SA.57082 - France - COVID-19 – Cadre temporaire 107(3)(b) – Garantie et prêt d'actionnaire au bénéfice d'Air France C(2020) 2983.

42 SA.59913 - France - COVID-19 – Recapitalisation of Air France and the Air France – KLM Holding C(2021) 9833.

43 SA.63946 - Germany - COVID 19 – aid to Flughafen Berlin Brandenburg C(2022) 659.

44 SA.63898 - Sweden - COVID-19 - State loan to SAS Consortium C(2020) 2983.

45 Eurostat, 'Covid-19 had a strong impact on businesses in the accommodation and food services sector in 2020' (2023), <https://ec.europa.eu/eurostat/statistics-explained/index.php?title=Businesses_in_the_accommodation_and_food_services_sector> accessed 28 November 2023.

46 SA.56981 – Austria – COVID-19: Austrian scheme for guarantees on bridge loans C(2020) 2537.

47 SA.61825 – Poland – New support to industries affected by the COVID-19 pandemic C(2021) 5266.

48 SA.60454 – Bulgaria – COVID-19: Grants for SMEs affected by temporary anti-epidemic measures under Operational Programme Innovation and Competitiveness 2014-2020 C(2021) 9960.

49 Eurostat (n 36).

50 de Vet and others (n 31).

51 Eurostat (n 36).

52 State Aid SA.57195 – Czechia COVID-19: Aid in the form of guarantees on loans for enterprises of up to 500 employees C(2020) 3340; and SA.61470 – Czechia – COVID-19: Aid in the form of guarantees on investment loans C(2021) 2330.

53 SA.57947 – Italy – COVID-19: Support measures for undertakings carrying out activities in the agricultural, forestry, fishery and aquaculture sectors and the activities related thereto, in relation with the COVID-19 outbreak crisis C(2020) 4977.

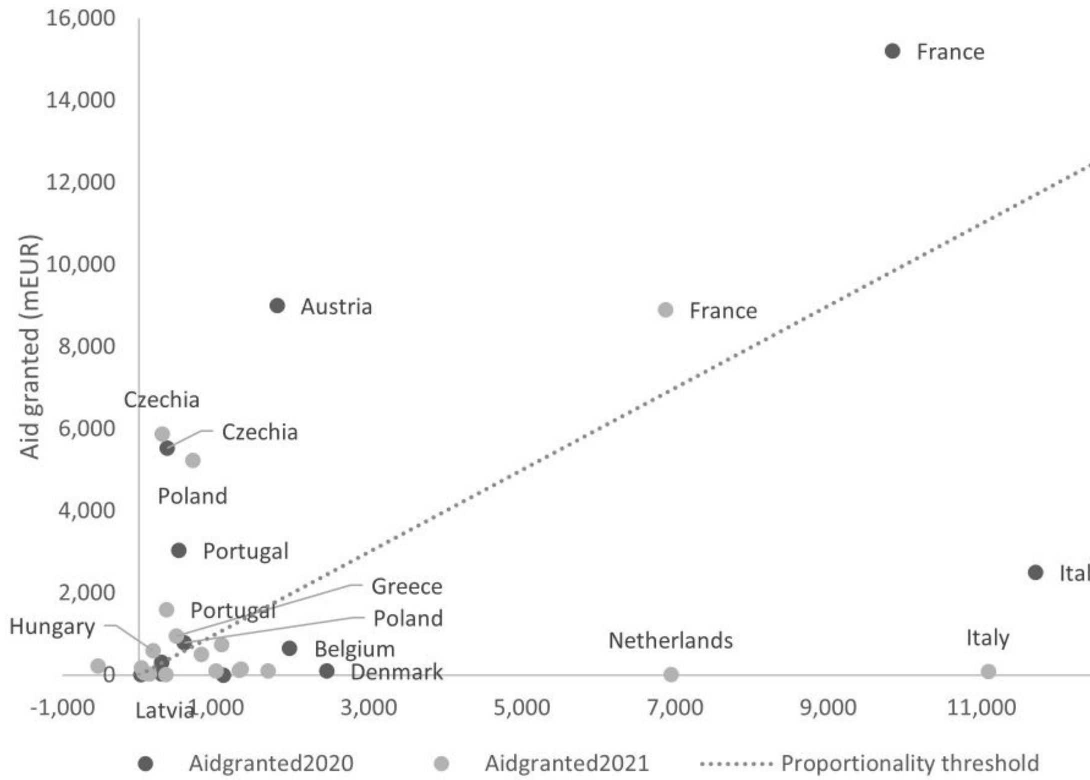

Figure 4: Arts, entertainment and recreation: Overview of sectoral aids and shocks per year per Member State in mEUR.

Further on, in Belgium, Croatia, Cyprus, Greece, Lithuania and Portugal in 2020, and Belgium, Bulgaria, Cyprus, Czechia, France, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, the Netherlands, Portugal and Romania in 2021 (that is, 14 out of 20 granting aid to the sector), the aid was not lawful in the first instance as there was no negative shock to the economic state of the sector.

f. Summary of Remaining Sectors

The picture remains the same across most of the remaining sectors. All, except for the education sector (NACE code 'P') have at least one instance of overcompensation. The electricity, water supply and public administration sectors follows closely with only one aid granted to the sectors, although each is found to be disproportionate to the sectoral shock.

The large majority of the sectors have between one and four instances of overcompensation. The most overcompensated is the Information and communication sector, with 15 Member States granting aid above the pandemic shock, and Wholesale and retail with eight Member States granting disproportionate aid, and Czechia doing this in both 2020 and 2021.

Belgium, Bulgaria, Czechia, Estonia, Greece, and Portugal all granting disproportionate aid to more than five of the 15 sectors. Finland, Hungary, Lithuania, Romania, and Spain were the only Member States not to grant any disproportionate aid in these sectors.

4. Summary

The results will be presented in brevity in this section before their implications will be further discussed in Section V. See the Appendix for an overview of results across all sectors and Member States.

The results show that the Member States to a large extent did not adhere to the principle of proportionality in their use of the flexibility provided under the Temporary Framework. Instead, there are indica-

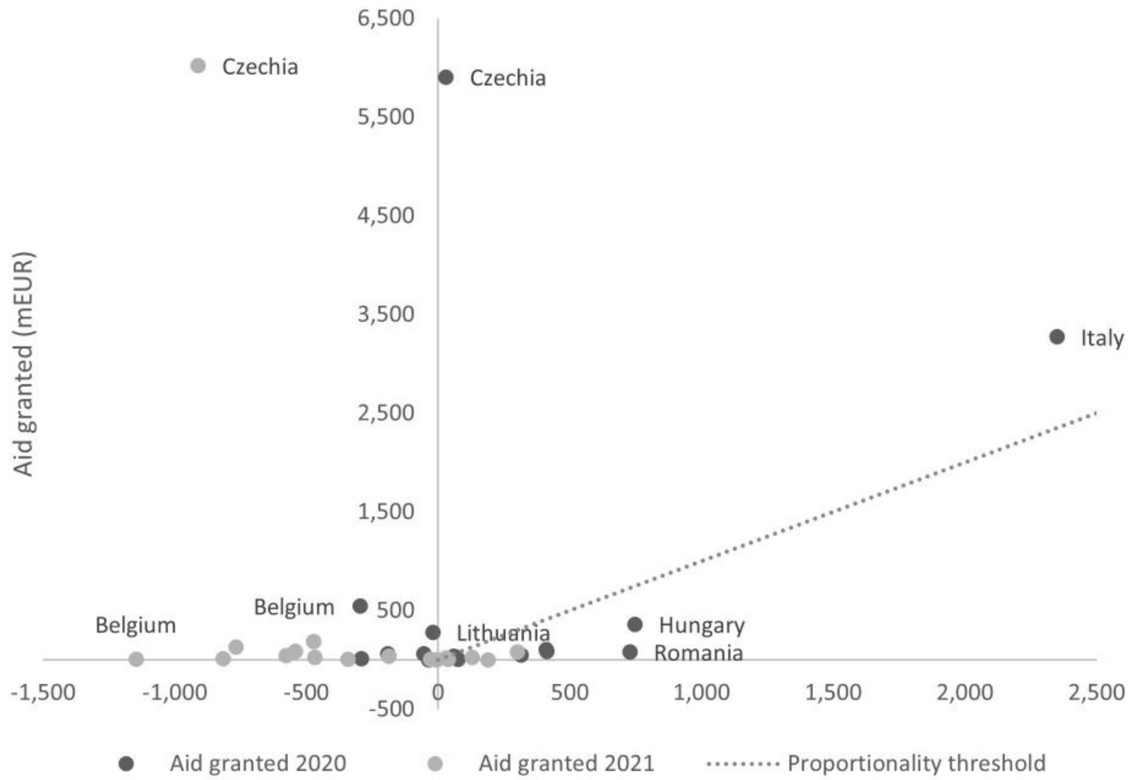

Figure 5: Agriculture, forestry and fishing: Overview of sectoral aids and shocks per year per Member State in mEUR.

tions of repeated disproportionate granting across the board.

Over half of the Member States had budgeted for aid which were disproportionate on an overall level, also without including the sector-specific aids in the calculation. For the non-sector specific aid, the difference between the general GDP contraction and the State aids granted were in many instances very large. Nine Member States granted aids which were multiple times larger than the GDP shock, which suggests there may have been breaches of the principle of proportionality. This finding is also in line with the results presented in the 2022 State Aid Scoreboard, which concludes that not only the budgeted and granted aid, but even the implemented aid reported by the Member States, exceeds the associated GDP shocks in eleven Member States.[54] Unlike this work, however, the 2022 Scoreboard does not engage with the sectoral distribution of the aid granted under the Temporal Framework.

The picture on the sectoral level is nevertheless the same, although more nuanced. Of the aids granted to the 19 sectors assessed in the analysis, the education sector was the only one in which there were no instances of disproportionate aid granted.

The distribution in Annex I shows that grants were generally targeted at the most affected sectors, and that these are generally also the ones with the highest proportion of disproportionate aids. The exceptions are the sectors of agriculture, forestry and fishing and information and communication. Somewhat surprisingly these also have the highest number of disproportionate grants: 15 Member States granted disproportionate aid to the agriculture sector, and 15 in the information and communications sector.

The average across the Member States are four instances of overcompensation on a sectoral level, where countries such as Belgium, Bulgaria, Czechia, France, Greece and Portugal stand out as those ex-

54 Commission 'State aid Scoreboard 2022' (n 6) 45-46.

ceeding the proportionality principle the most amount of times on the sectoral level. On the opposite side of the scale are Finland, Slovakia, and Spain, all granting aid limited to the size of the respective shocks. Note however that this is on the sectoral level: on the non-sector specific level, Germany, Italy, Poland, and Belgium granted the most disproportionate aids.

The same pattern emerges when accounting for the average number of disproportionate aids granted as a fraction of the total number of aids granted per Member State. Here it is the larger Member States who dominate the high end of the scale with over half of their yearly accumulated numbers showing disproportionate grants, whereas the great bulk of the smaller Member States maintain a share of disproportionate to total amount of aids below 50%. This finding is line with the overall assessment provided by the Commission.[55]

V. The Likely Impact of State Aid on the Internal Market

The findings demonstrate that there were issues with proportionality in the implementation of the Temporary Framework. The fact that disproportionate aid was granted in all but *one* of the 19 sectors analysed raises questions, and even more so after the Commission itself repeatedly has claimed the opposite: namely that even the *implemented* aid under the Temporary Framework by the Member States has been proportionate.[56] The Commission has, nevertheless, authorised the granting of state resources to a degree which is not to be considered compatible with the internal market.

1. Disproportionate Aid: The Issue

In its 2022 State Aid Scoreboard, the Commission states that aid granted by more than half of the Member States were in fact *larger* than the negative shock experienced in these Member States in 2020 and 2021, indicating, indeed, that they were not proportional. The distribution remains largely the same also when the *aid component* of the aid measures is used, as opposed to the total budgeted amounts.[57] This means that more than half of the Member States granted disproportionate aid under the Framework. The results presented in Section IV signal that these trends are also observed on sectoral levels.

The most concerning issue is however not necessarily the fact that the aid granted was disproportionate with regards to the relevant shock or contraction of the associated sector. The problem is rather that the distribution seems to be heterogeneous across the internal market, where the larger Member States have granted relatively more disproportionate aid than the smaller states in the Bloc.

The uneven distribution of aid grants under the Framework affects competition in the internal market: First, the undertakings receiving aid become increasingly more competitive relative to the undertakings who did not receive such support. Second, it has a domino effect as it invites other Member States to engage in a subsidy race, whereas support is granted to national undertakings in order to increase their competitiveness. The effect at risk is essentially a re-fragmentation of the internal market.

While it may be surprising that the Commission reached the conclusion ex-post that the aid measures granted under the Framework were proportionate, it was not necessarily so ex-ante: The measures were evaluated in unprecedented times, where the impact and duration of the economic shock caused by the Covid-19 pandemic were highly uncertain. Further on, a requirement to quantify the damages to be remedied by the State aid is not present in the Temporary Framework, although it does specify that Member States must show how aids granted under the Framework are 'necessary, appropriate and proportionate to remedy a serious disturbance in the economy of the Member State'.[58]

The hardest hit sectors of transport, hospitality, retail, culture and tourism[59] also had the most disproportionate instances of aid grants to them. This could be expected based on the sheer amount of aid measures directed at these sectors, connected to the uncertainty surrounding the duration and the intensity of the shock caused by the pandemic. Furthermore, many of the aid measures targeted at the sectors were

55 Commission 'State aid Scoreboard 2022' (n 6).

56 Commission 'State aid Scoreboard 2022' (n 6); Commission, 'Report on Competition Policy 2021' (n 26).

57 Commission 'State aid Scoreboard 2022' (n 6).

58 Commission 'Temporary Framework' (n 18) para 9.

59 de Vet and others (n 31).

for the most part open to all of them, and the conclusion of disproportional aid needs not be the reality for the actual implemented aid.

The agriculture sector, on the other hand, is historically a very important sector politically, and also a popular sector to grant aid to. The sector did however not experience an economic shock in the periods studied, so there are indications of overcompensation, although it is to be noted that most of the measures targeting agriculture was also open for multiple other sectors.

Besides the sectors most affected by the Covid-19 pandemic, the information and communication sector also stood out in the results. The aid granted to the sector must be seen in connection with the confinement measures introduced with the Covid-19 pandemic, which moved many sectors and industries to digital platforms and spaces. It is not unthinkable that the grants to the sector were also seen as ways to mitigate the shocks across the Member States in terms of development of new software and systems to cope with the new reality. While they were not necessarily proportionate to the economic contraction in the relevant sectors, the State aids given may have had far-reaching impacts which in effect did contribute proportionally to remedying the shocks experienced as a consequence of the Covid-19 outbreak.

2. Proposals To Remedy Disproportionate Granting of State Aid

First and foremost, the Temporary Framework and similar instruments aimed at tackling the effects of crises should rely on the granting of guarantees and not direct grants as the strictly preferred kind of aid granted. From a public policy point of view, also in light of the learnings from the financial crisis in 2008, it is difficult to rationalise the spending of public money on private undertakings before strictly necessary, and before the undertaking has done what it is able to do before requesting public aid.

Granting of State aid should be the very last resort: the economic actor, being the undertakings and beneficiaries of aid, already bear the upside and downside risk of their economic activity. State should only be called upon for public contribution when society is in grave danger as a cause of the economic danger, as is the case under TFEU Article 107(3)(b). In this instance this means that the undertaking in question should refrain from paying out dividends, bonuses, and so on, in addition to downgrading the shareholder value as needed.

Next, Member States should be asked to quantify the damage to be relieved, as is the case under Article 107(2)(b) TFEU, where the quantification include the kind and the size of the damage and the methodology used to reach these conclusions.[60]

There was however a fine line to balance the flexibility foreseen under the Framework on the one side, including the swift evaluation and approval of aid measures, and documentation requirements and red tape on the other. There was a strong sense of urgency, and the fast-tracked notification and evaluation was seen as a key aspect for the Framework to function as intended. However, the results of the findings suggest that there was a significant issue with disproportionate aids granted, not only on an overarching, but also on the sectoral level. Asking the Member States to outline the key parameters of concern and how they affect the beneficiaries is not unreasonable, and an attempt to quantify the shock not necessarily either.

Finally, another mitigating measure would be to require Member States not only to quantify the shocks in general but also to quantify them per sector. As shown in Section IV, many sectors did not experience a shock, but might have received disproportionate aids because they were one of the many targeted sectors listed in the decision. By increasing the level of detail regarding the intended sectoral scope of the aid, some of these issues may be alleviated. While this would have reduced some of the flexibility in terms of number of and scope of notified aids, it is not unreasonable to expect the evaluation of the measures to be simpler, potentially also allowing for the short evaluation time needed.

VI. Conclusion

This article explored whether the principle of proportionality was adhered to by the Member States in their sectoral application of the Temporary Frame-

60 Antonis Bouchagiar, 'State aid in the context of the COVID-19 outbreak, including the Temporary Framework 2020' (2021) Florence School of Regulation, European University Institute working paper <https://hdl.handle.net/1814/69678> accessed 28 November 2023.

work as a response to the Covid-19 pandemic shock. The results suggest that the aids granted have to some degree been disproportionate.

Furthermore and more concerningly, the distribution of Member States granting disproportionate aid is also heterogeneous, raising concerns about distortion of the conditions for competition on the internal market.

The findings suggest that new frameworks like the Temporary Framework, such as the Temporary Crisis and Transition Framework, should be designed and implemented with care so as not to distort competition in the internal market. Possible amendments include requiring the notifying Member State to quantify the damage to be remedied for, as is already a requirement under 107(2)(b). The exact requirement needs to be crafted with attention to detail to avoid putting up new red tape that gets in the way of the flexibility and responsiveness foreseen under circumstances such as the Temporary Framework.

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