

An aerial photograph of a harbor, likely Genoa, showing a large shipyard with many cranes and ships, and a marina filled with numerous small boats. The harbor is surrounded by hills and buildings.

# **International Workshop on “Benchmarking and regulation in transport”**

## **State aid issues in transport regulation**

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# Outline

1. The interplay of regulation and State aid control
2. Airports
3. Ports
4. Rail infrastructure
5. Public transport services
6. Complementarities and open issues



# **1. The interplay of regulation and State aid control**

# The role of regulation and State aid control

- Although the transport sector in Europe has been influenced by significant privatization processes, public funding is still widespread, both for the construction and operation of infrastructures (airports, ports, rail, roads) and for the provision of public transport services. At the same time, notwithstanding liberalization processes which gradually opened several markets to competition, there remain several situations of significant market power
- In such environment, both economic regulation (ER) and the control of State aid (SA) play an important role => what are the main features of their interaction? Is there room for streamlining the use of these different policy tools?



# **Objectives: economic regulation versus State aid control**

- The main objective of ER is efficiency. It is typically used to correct market failures, including the inefficiencies which may result from the lack of competition. Some efficiency-enhancing mechanisms can also be useful in the design of long-term contracts between public authorities and undertakings, both in case of direct award and in the case of tenders (e.g. for the management of infrastructures or the provision of public transport services)
- For SA, the objective is to minimize distortions of competition. The use of public resources to provide a selective advantage which can distort competition and have an impact on trade is incompatible with the common market [Art. 107(1) TFEU]; however it can be considered compatible when necessary and proportionate to pursue well defined public interest objectives [Art. 107(3); Art. 106(2) for SGEI; Art. 93 and Reg. 1370/2007 for public transport services by rail and road]

# **The economic approach to State aid control**

- the European Commission has the exclusive competence to assess whether SA is compatible with the Treaty. In recent years, it has made significant efforts to clarify its approach, so as to distinguish good aid from bad aid and to ensure that such criteria are applied consistently in the different areas
- the main idea is that public resources, when used to provide an ‘artificial’ selective advantage to an undertaking or group of undertakings, should pursue clearly defined public interest objectives (including in particular, efficiency-enhancing corrections of market failures) and be designed in a way which takes into account the need to maintain incentives to invest and to adopt efficiency-enhancing conduct on the market, both with reference to beneficiaries of the aid and to other undertakings
- the assessment of whether SA entails distortions of competition is made at all levels of the value chain, not only with respect to the direct beneficiaries of the aid measure

# **Scope of State aid control versus scope of economic regulation**

- the Commission may intervene on SA only when all the conditions of Art. 107 TFEU are met: only for measures entailing the use of public resources, imputable to public authorities and providing a selective advantage to some undertakings, which they would not have received by a 'market economy operator' (MEO principle)
- SA control intervenes only when such advantage may distort competition. When an infrastructure is used to carry out a commercial activity, its operation and also its construction may be considered economic activities and any public funding may fall into the scope of SA control (*Leipzig Halle*, C-288/11 P)
- on the other hand, where there is no actual or potential competition, either in the market or for the market (situation which is the typical target of regulatory measures) SA control is not applicable
- SA control provides common rules on efficient use of public resources also for economic activities which fall outside EU directives

# A two-way interplay

- the profitability of a regulated economic activity, including related investments, affects whether private resources are sufficient or, instead, public support is needed at conditions different from those which would have been followed by a MEO => taking the public policy objectives pursued by the Government as given (e.g. the availability of an infrastructure or a public service at the envisaged quality conditions), regulation has an impact on whether SA is needed
- in order to be considered compatible, SA should not overcompensate beneficiaries. If regulation (or the conditions of a tender) ensure that the beneficiary is efficient, the task of controlling the compatibility of SA is simplified
- regulatory accounting/separation may facilitate the control of SA
- Member States are encouraged to follow the model set by the GBER and the Commission sectoral guidelines for compatibility of SA (a ‘regulatory’ approach to SA?)



An aerial photograph of an airport. A long, straight runway runs vertically through the center of the frame. To the left of the runway is a taxiway and a grassy field. To the right is a smaller runway or taxiway. In the background, a densely populated city is visible, nestled at the foot of a range of steep, mountainous hills. The sky is blue with scattered white clouds. In the bottom right corner, there is a semi-transparent circular graphic containing the text '2. Airports'.

## **2. Airports**

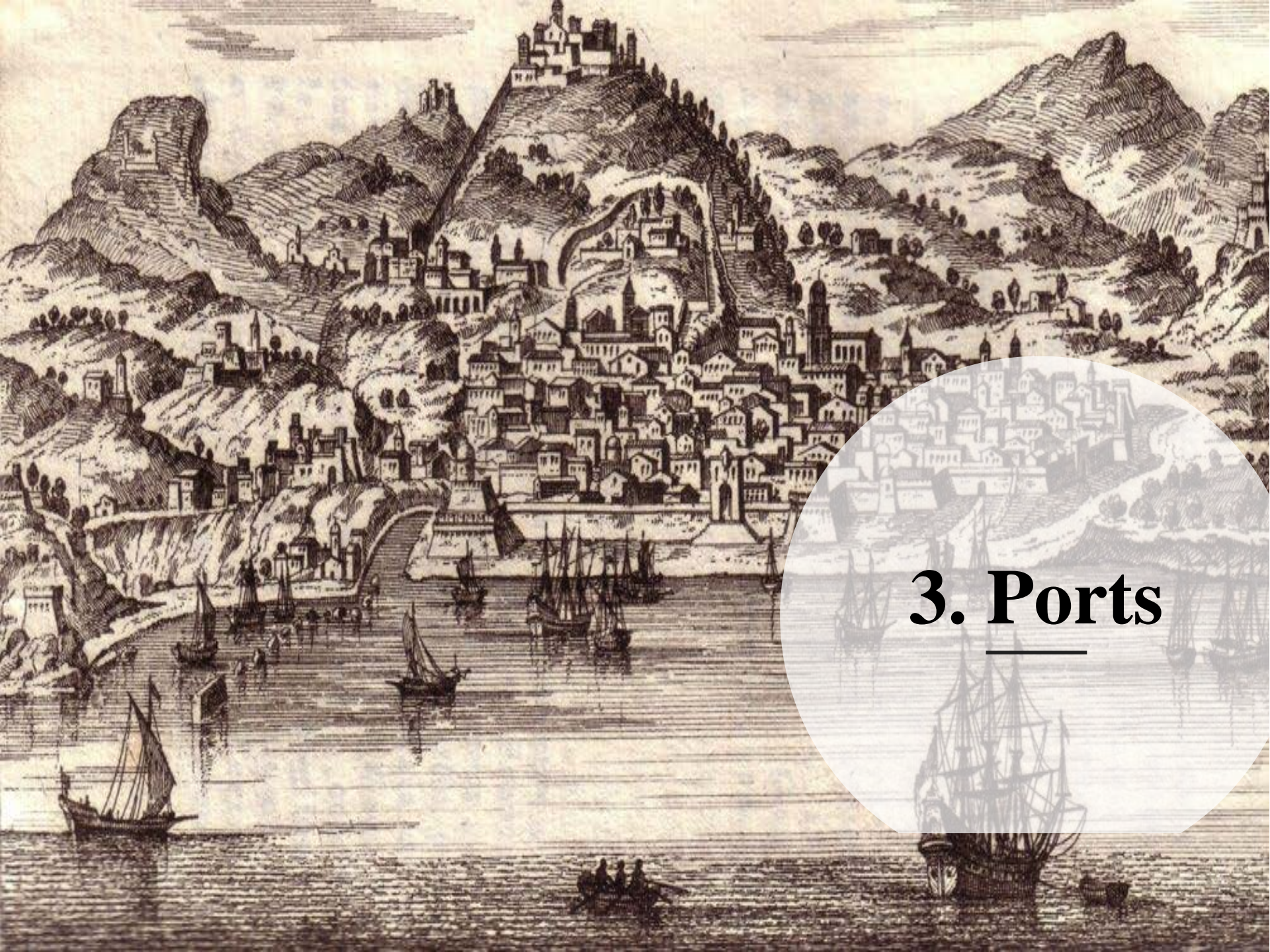
# Regulation versus SA control

- For airports, the main task of economic regulators is defining models for the adoption of airport charges which are cost oriented, promote efficiency and are capable of incentivising investments so as to foster innovation, security and the quality of services (see Directive 2009/12 for airports with traffic above 5 mln passengers). Public authorities may also be entrusted with the task of monitoring that charges for the use of infrastructures and services provided on an exclusivity basis comply with the principles of cost-orientation, transparency and fairness. In Italy, national legislation requires that the managing body of the airport, when setting charges for the use of infrastructures and services provided on an exclusivity basis, takes into account the EU average level of airport charges in comparable airports
- The importance of State aid control for airports increased since the 1990s. The 2014 Aviation Guidelines address how the Commission assesses for airports the compatibility of investment aid and operating aid

# SA and airports: some remarks

- the current approach of the European Commission is clearly pursuing two main objectives:
  - i. it aims at avoiding that public resources are used to affect competition between airports when there is no clear positive impact on a common interest objective
  - ii. it aims to ensure that airport business plans, even when supported by public resources, are sustainable and, in the foreseeable future, will not require operating aid, with the only exception of the compensation of properly defined public service obligations (therefore, in principle marginal cost pricing should not be permitted if it fails to recover total costs)
- moreover, national planning of airport infrastructures is encouraged
- for airports the Guidelines suggest that benchmarking may lead to biased results if it does not take properly into account the existence of widespread public support in comparable markets





### 3. Ports



# The EU approach to regulation

The port sector is undergoing major transformations and most ports, like airports, have to meet a lively competition. On the other hand, along the value chain there are activities which, because of economic features or of exclusive/special rights, entail some market power which may justify the introduction of efficiency enhancing mechanisms

=> common rules at EU level in Regulation (EU) 2017/352. Qualitative requirements and any limitation on the number of providers of port services should be strictly justified and procedures for granting the right to provide services must be transparent and non-discriminatory. If activity directly exposed to competition, no further constraint. As to access to port facilities, the charging system should be transparent and non-discriminatory and contribute to the maintenance and development of infrastructure and the efficient provision of services. Specific rules on accounting separation are provided. SA rules are expressly mentioned both for investment aid and for the compensation of public service obligations

# SA control: some remarks

- Also for ports, concern that public resources may be unduly used to distort competition at the different levels of the supply chain (the owner or manager of the port, operators using the port infrastructure to provide services, end-users of the port facilities)
- When a support measure is State aid, it is deemed compatible only when necessary and proportionate to achieve objectives of common interest (e.g. facilitating trade and connectivity, improved intermodal links etc.) and distortions of competition are kept at a minimum (e.g. access is provided on non- discriminatory terms)
- As to the economic conditions applied to users of the port infrastructure or users of port services, compliance with the MEOP is usually assessed by taking as a benchmark the conditions applied in comparable ports. Is the asymmetry with the approach followed for airports, whereby benchmarking is considered unreliable because of widespread public intervention, justified?





## **4. Rail infrastructure**

# The current approach

Public resources are the main source of funding of rail infrastructures, however, differently from the approach adopted for airports and seaports, so far the Commission has been reluctant to include them in the assessment of State aid. The main reason is that national rail infrastructures are seen as natural monopolies and therefore, provided that specific conditions are met, public funding is not capable of distorting competition. See the NOA notice:

“an effect on trade between Member States or a distortion of competition is normally excluded as regards the construction of the infrastructure in cases where, at the same time (i) an infrastructure typically faces no direct competition; (ii) private financing is insignificant in the sector and Member State concerned and (iii) the infrastructure is not designed to selectively favour a specific undertaking or sector but provides benefits for society at large”, e.g. is made available to all potential users on equal and non-discriminatory terms

# Operation of infrastructure and regulation

- In order to ensure that funding provided in the above mentioned situations cannot be used to cross-subsidize other economic activities, either the infrastructure owner should not engage in any other economic activity or, if this is not the case, should keep separate accounts, allocating costs and revenues in an appropriate way and ensuring that any public funding does not benefit other activities. The absence of indirect aid can also be ensured by means of a tender
- For the operation of railway infrastructure, it is still possible to exclude the existence of State aid if there is legal monopoly and competition for the market is excluded (point 219)
- The case of public funding of rail infrastructure clearly indicates that, the more remote are competitive pressures, the less State aid control intervenes and the more important becomes the role of regulatory tools aimed at disciplining incumbent undertakings and promoting efficiency





## 5. Public transport services

# **Compensation of public service obligations and SA control**

One of the main areas of State aid control concerns the compensation of public service obligations for services of general economic interest, including public transport services (ranging from air and maritime links to regional rail and local bus transport services).

The two main issues are the following:

- a. under what conditions the compensation of public service obligations (PSO) is not State aid; and
- b. if State aid cannot be excluded, under what conditions the compensation of public service obligations can be considered compatible with the Treaty.

The legal benchmarks for the assessment of compatibility are Art. 93 TFEU and its implementing regulation 1370/2007 for public transport of passengers by rail and road, and Art. 106(2) TFEU for other transport modes

# Some remarks

- SA rules for the compensation of public service obligations are very detailed. At least indirectly, they push Member States into adopting efficiency-enhancing solutions aimed at avoiding overcompensation of public service obligations
- it remains to be seen for which SGEI it is possible to find the efficient benchmark required by the fourth Altmark condition in the absence of an appropriate tendering procedure. However, the Commission acknowledges that “where a generally accepted remuneration exists for a given service, that market remuneration provides the best benchmark for the compensation in the absence of a tender”
- is the requirement of a regular ex post monitoring and recovery of overcompensation consistent with a regulation based on price or subsidy caps incentivising operators to increase their efficiency and reduce costs, or does it risk frustrating efficiency enhancing incentives?





## **6. Complementarities and open issues**

# Looking at SA control

- Whenever there is competition, also between infrastructures, State aid control aims at limiting distortions resulting from the use of State resources when not strictly justified by the need to pursue a common interest objective. The need to comply with State aid rules may increase the effectiveness of national policies and can thus be viewed as an opportunity instead of merely as a constraint. E.g.:
- basing infrastructure development on broad national strategies fosters the coherence of public measures and leads to priority setting;
- requirement of reliable business plans encourages national authorities to carry out an ex ante assessment of the economic sustainability of projects supported by public resources;
- an accurate ex ante identification of public service obligations and the criteria for their compensation is important to provide citizens with quality and efficiency;
- ex post assessment of SA measures may provide valuable indications to national authorities on how to improve their policies

# Looking at national regulatory authorities

- regulation affects the profitability of private investment and therefore affects whether market forces are sufficient to pursue a specific public policy objective. If the regulatory framework is unclear or unstable, it becomes very difficult to ascertain whether public aid is necessary and proportionate
- in sectors where effective procompetitive access regulation and accounting separation rules already exist, it may be easier to prove that there will not be distortions of competition in the use of an infrastructure financed by public resources
- regulatory authorities can provide technical support in the design of procompetitive tenders, in benchmarking exercises aiming to assess whether the MEO test is satisfied, in the elaboration of major State aid schemes in regulated sectors, as well as in the ex post evaluation of the impact of aid measures

=>regulatory authorities play an important complementary role in the design of national policies and in ensuring compliance with State aid rules