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Client Alert Commentary

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EU State Aid Temporary Framework for COVID-19 — Fourth Amendment

The fourth amendment extends and modifies the framework to support companies affected by COVID-19.

On 13 October 2020, the European Commission (Commission) published a fourth amendment to the Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak (Temporary Framework).

The fourth amendment:

- Extends the availability of measures set out in the Temporary Framework
- Adds a new instrument allowing governments to provide support for uncovered fixed costs of companies that have suffered from the suspension or reduction of their business activities
- Modifies rules for Member State exit from recapitalisation measures
- Extends the temporal removal of all countries from the list of "marketable risk" countries under the Short-term export-credit insurance Communication (STEC)

The Temporary Framework

The Temporary Framework, which the Commission introduced on 19 March 2020, was designed to enable national governments to use the full flexibility of the State aid rules to support the economy during the pandemic.

In it, the Commission explained in particular that

- there is a category of measures under which support can be granted immediately by Member States without the Commission's involvement. This includes no-aid measures that fall outside the scope of EU State aid control *e.g.* support applicable to all undertakings or directly to consumers. This category also includes aid measures that are exempted from notification as *de minimis,* are covered by the General Block-Exemption Regulation (GBER), or are part of certain repurposed schemes already approved

- In addition, aid falling under three further categories can be granted if notified to and approved by the Commission:
  - Liquidity support such as loans and guarantees for cash-flow shortfalls granted to SME and large undertakings
  - Compensation for damages caused directly by COVID-19 which can be granted also for specific sectors particularly hit by the outbreak (for instance transport, entertainment & culture, tourism & hospitality, retail and banks)
  - Support to remedy the serious disturbance to the Member States' economy caused by COVID-19 – as the Commission did during the 2008 Financial Crisis, this is the aid that the specific rules of the Temporary Framework considers compatible. The first temporary measures allowed are liquidity schemes, guarantees on bank loans or subsidized public loans, flexible export credit insurances, safeguards, and leniency for aid through and for banks

The first amendment (adopted on 3 April 2020) enables Member States to grant further State aid to accelerate R&D, testing, and production of products relevant to fighting the pandemic, and allows for targeted support to help protect jobs and those sectors and regions hit particularly hard by COVID-19.

The second amendment (adopted on 8 May 2020) allows Member States to provide State aid in the form of recapitalisations and subordinated debt to companies affected by COVID-19.

The third amendment (adopted on 29 June 2020) allows Member States to support micro and small companies, including startups, by providing public support to such companies even if they were already in financial difficulty on 31 December 2019. It also provides incentives for private investors to participate alongside the State in recapitalisations.

Extension of the availability of measures

The fourth amendment prolongs all provisions of the Temporary Framework by six months until 30 June 2021, except for recapitalization measures which are prolonged by three months until 30 September 2021.

Before 30 June 2021, the Commission will assess the need to further prolong or adapt the Temporary Framework.

Support for part of companies' fixed costs

The fourth amendment introduces a new instrument to allow governments to contribute to part of companies' fixed costs on a temporary basis. To be eligible, companies must show that their turnover declined by at least 30% compared to the same period in 2019 due to the COVID-19 pandemic. The maximum amount that governments may contribute to a company's fixed costs is €3 million.

Modified rules for Member State exit from recapitalisation measures

Under the Temporary Framework, Member States may provide aid in the form of equity and/or hybrid capital instruments to companies facing difficulties due to the COVID-19 pandemic. The fourth amendment creates a new possibility for Member States to redeem their recapitalisation through an independent valuation.

Until now, a Member State may exit a COVID-19 recapitalisation measure either by the beneficiary company purchasing back the stake the Member State had acquired, or by the Member State selling its shares to other investors by means of the stock exchange or public consultation of potential purchasers. In case of a public consultation of potential purchasers, the Member State may give existing shareholders priority rights to buy at the price resulting from the public consultation.

The fourth amendment introduces the following new means for a Member State to redeem its recapitalization, which can be used two years after the granting of the COVID-19 recapitalisation.

(i) Where the Member State is the only existing shareholder

A public consultation of potential purchasers may be replaced by a valuation of the beneficiary performed by an independent expert. If the independent valuation establishes a positive market value, the State is deemed to have exited from the COVID-19 recapitalisation, even if the beneficiary remains State-owned. For COVID-19 recapitalisation measures that exceed €250 million, the Member State is obliged to submit the independent valuation to the Commission.

(ii) Where the Member State is one of several existing shareholders

For the part of the COVID-19 equity that the State would need to retain in order to restore its shareholding to that before the COVID-19 recapitalisation, an independent valuation in accordance with the rules set out in (i) above may be used.

For the rest of the COVID-19 equity, a competitive sales process must be undertaken, and the Member State will not have priority rights. If this competitive process concerns a significant part of the beneficiary's shares, that sales price can also be considered an independent valuation for the equity the State retains, as noted above.

Similar to what was already foreseen for the price resulting from a sale process, if the valuation under (i) or (ii) above results in a positive market value that is still lower than the minimum price at which the beneficiary could buy back the State's COVID-19 equity, then the governance rules (*inter alia* restrictions on acquisitions, dividend payments and share buybacks, management remuneration, and cross-subsidization of other integrated activities, as well as reporting and transparency requirements) will continue to apply until four years after the granting of the COVID-19 recapitalisation measure. Instead, if the valuation establishes a negative market value, a restructuring plan of the beneficiary may need to be notified to the Commission for approval.

Extension of temporary removal of all countries from list of "marketable risk" countries

The STEC provides that "marketable risks" shall not be covered by export-credit insurance with the support of Member States. In March 2020, the Commission found that there was a lack of sufficient private insurance capacity for short-term export-credits as a result of the COVID-19 pandemic. As a result, it deemed all commercial and political risks associated with exports to the countries listed in the Annex to the Short-term export-credit insurance Communication (STEC) as temporarily "non-marketable" until 31 December 2020.

The fourth amendment extends this temporary removal of all countries from the list of "marketable risk" countries under the STEC until 30 June 2021.

Remarks

This extension and enhancement of the Temporary Framework underscores the Commission's unprecedented willingness to approve aid to support business impacted by the increasingly long-term consequences of the COVID-19 pandemic. Over the past 8 months, the Commission has approved under the Temporary Framework more than 250 separate measures. Among these, measures as sizeable as the German €6 billion contribution to the recapitalisation of Deutsche Lufthansa AG as part of a scheme supporting specific sectors of national economies harmed by the pandemic.

While this action is certainly welcomed, some wonder whether this very lenient approach will imply a permanent relaxation in State aid control.

At the same time, a number of companies remain unable to access aid schemes approved under the Temporary Framework as the Commission has not been able to synchronize the application of different instruments. For instance, certain PE-backed companies that have retained losses due to their specific leverage structures, arbitrarily fall foul of the Temporary Framework's requirement that an undertaking must not have been "in difficulty" on 31 December 2019, according to the definition retained by the GBER.

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