

Special Report

**Control of State aid to financial institutions in the EU:
in need of a fitness check**



EUROPEAN
COURT
OF AUDITORS

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Timeline

Executive summary

I State aid can distort competition by giving beneficiaries an advantage over competitors. The Treaty on the Functioning of the European Union prohibits State aid unless justified in well-defined exceptional situations. The European Commission is responsible for ensuring that this principle is observed.

II When the global financial crisis of 2007 to 2008 erupted, government interventions were deemed necessary to limit the threat that banks posed to financial stability. Since then, the EU has introduced major reforms to its framework for the financial sector, with the aim of making future bank bailouts unnecessary. However, there are still cases where banks receive taxpayers' money. The Commission is responsible for assessing the compatibility of such measures with the EU's internal market, under rules that were established during the crisis and modified most recently in 2013.

III The objective of the audit was to assess whether, during the audited period, the Commission performed its control of State aid to financial institutions appropriately with a view to ensuring that aid was exceptional and limited to the minimum necessary. We found that the Commission had appropriate resources and tools to carry out its control of State aid but was not always in a position to use them to full effect.

IV Our audit covered the period from August 2013, the date the current Commission rules for State aid to the financial sector came into effect, until the end of 2018. We examined parts of the internal control framework (in particular how the Directorate-General for Competition measured performance), the organisational setup, including resources, and the (legal) framework for State aid control, including the relevant State aid rules. In addition, we examined the Commission's implementation of its State aid control, including whether it adhered to its internal processes and procedures.

V We found that the Directorate-General for Competition had set objectives for the exercise of State aid control with sufficient clarity and identified risks to their achievement. It had established indicators to measure its performance, as required, but these did not fully capture the Commission's performance in the control of State aid to financial institutions. Moreover, it had not formally evaluated the effectiveness of its application of the crisis rules during the period covered by our audit.

VI The Commission had an appropriate organisational set-up for the control of State aid to financial institutions, which allowed for appropriate information flow and management oversight. The Commission had established a robust ethical framework, and the Directorate-General for Competition promoted a strong ethical culture, including a commitment to adhere to the highest professional standards. The Commission had allocated sufficient staff resources to the control of State aid to financial institutions. The Commission had the necessary powers for effective and efficient State aid control. Thus, it had the means to ensure that its decisions would be based on correct information.

VII The Commission's rules for the control of State aid to the financial sector were generally well drafted and clear. The Commission had reviewed and adapted these Communications as economic conditions improved in 2010, 2011, 2013, but had not done so since. We observed that market realities improved during the audited period and up to the outbreak of COVID-19, and the regulatory framework changed, but that the State aid rules themselves have not been changed since 2013.

VIII The Commission's case-handling activities complied largely with internal processes. The Commission had assessed restructuring plans very rigorously, requiring detailed information and scrutinising it thoroughly. However, it did not contest Members States' submissions that the conditions for an exceptional approval of State aid existed in each individual case. Likewise, the Commission had agreed measures intended to limit distortions of competition without analysing the impacts in the published decisions.

IX It may therefore be needed to consider streamlining of the Commission's control of State aid to the financial sector. Based on the observations in this report, we recommend that the Commission:

- Carries out an evaluation of whether the State aid rules continue to be appropriate and take corrective action where required.
- Further enhances compliance with internal processes and best practices.
- Improves performance measurement.

X This performance audit is part of ECA's work on financial and economic governance. It complements ECA reports already published on financial supervision and competition policy and can contribute to discussions on the rehabilitation of the EU banking sector. The decision to carry out this audit was triggered by the

observation that 10 years after the financial crisis erupted, the EU banking sector remained an important beneficiary of State aid, despite the EU's significant efforts to make bailouts of banks unnecessary. Our audit work was finalised prior to the COVID-19 outbreak and this report does not take into account new developments and policy changes that occurred in response to the pandemic. Nevertheless, it provides lessons that continue to be relevant: (a) it is important to ensure that aid to mitigate a crisis is limited to damage caused by the crisis and (b) the use of crisis rules should be re-evaluated once the crisis abates. The State aid rules concerning banks, that were subject of this audit, remain applicable alongside the initiatives the Commission has taken since the end of the audit, such as setting up the Temporary Framework.

Introduction

State aid control under the TFEU

01 State aid control, an exclusive competence of the European Commission, is aimed at ensuring the integrity of the internal market by protecting competition from market distortion by Member States. A company that receives support from its government gains an advantage over its competitors. The Treaty on the Functioning of the European Union (TFEU) generally prohibits State aid unless justified for general economic development reasons or in well-defined exceptional situations, for example to remedy a serious disturbance in a Member State's economy pursuant to Article 107(3)(b) TFEU (see [Box 1](#)).

Box 1

Article 107 TFEU (ex Article 87 of the Treaty establishing the European Community)

1. Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.

3. The following may be considered to be compatible with the internal market:

(b) aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State;

02 The European Commission is in charge of ensuring that this prohibition is observed and that exemptions are applied effectively and uniformly across the EU. The Commission has a broad discretion in the enforcement of Article 107(3) TFEU¹, which it can exercise by adopting guidelines that define how the Commission assesses the compatibility of a measure. This compatibility assessment has to be based on the

¹ See C-290/07 P *Commission v Scott* EU:C:2010:480, paragraphs 64-66.

application of sound economic principles. In this regard, the Commission Communication of 8 May 2012 on EU State aid modernisation stated that the complexity of the existing rules created challenges for State aid control and called for the identification and definition of common principles to ensure consistency of guidelines and equal treatment across measures and economic sectors². The Commission does not have discretion in assessing whether a Member State measure constitutes State aid, except for any complex economic assessments that the Commission may have performed, e.g. in order to establish whether it gives the beneficiary an advantage.

Judicial Review by the EU Courts

03 The Commission's State aid decisions and its procedures for arriving at them are subject to judicial review by the EU Courts, on terms described in the TFEU and the case law of the EU Courts. If an EU act is believed to violate the EU Treaties, secondary law adopted in its application or fundamental rights, the Court of Justice can be asked to annul it. Under the second paragraph of Article 263 TFEU, an annulment action can be brought by 'privileged applicants', such as Member States and the EU institutions, which are not required to demonstrate an interest in bringing proceedings. Under Article 263(4) TFEU, individuals or companies can also ask the Courts of Justice to annul an EU act that directly and individually concerns them.

04 Thus, Member States and beneficiaries can challenge a State aid decision. Competitors can claim their procedural rights have been violated in cases where they consider the Commission should have opened a formal investigation. In order to challenge the merits of a state aid decision, competitors do not have legal standing unless they can show their position on the market has been substantially affected in a way that renders their case singular. Actions by other individuals or companies (including bailed-in shareholders and bondholders) are generally not admissible unless they can demonstrate that a State aid decision concerns them directly and individually.

² See recital 6 of the Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on EU State aid modernisation (SAM), COM(2012) 209 final: <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2012:0209:FIN:EN:PDF>

05 The degree of judicial review by the EU Courts varies as regards the substance of State aid decisions. To assess whether a measure constitutes “aid” within the meaning of Article 107(1) TFEU, the General Court must conduct a comprehensive review as to whether a measure falls within the scope of that article. However, such a review is more limited where the appraisals by the Commission are technical or complex in nature.

06 In relation to the compatibility review pursuant to Article 107(3) TFEU, in which the Commission enjoys broad discretion, judicial review is confined to establishing that the rules of procedure and the rules relating to the duty to give reasons have been complied with, and to verifying the accuracy of the facts relied on and that there has been no error of law, manifest error in the assessment of the facts or misuse of powers. Moreover, the Commission should act consistently. The Court of Justice confirmed, in particular, that the judicial review by the EU Courts of the Commission’s assessment of whether an event results in a serious disturbance in the economy is subject only to a manifest error test, as described above³.

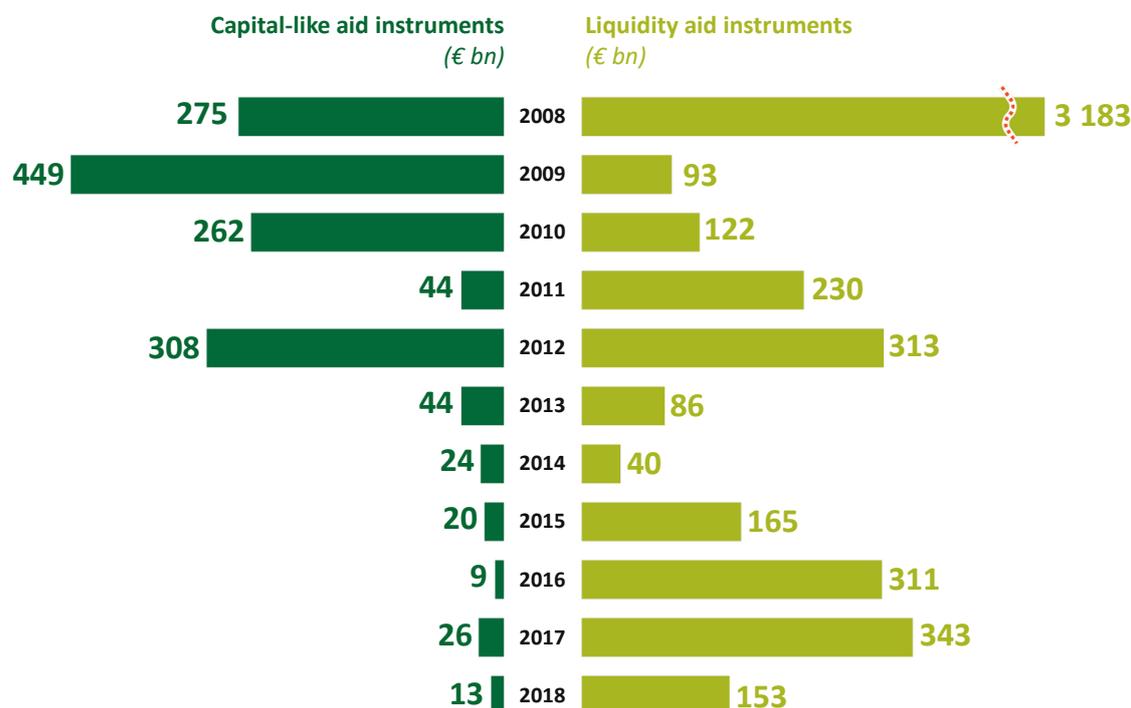
State aid to financial institutions – during and after the global financial crisis

07 The global financial crisis of 2007 to 2008 triggered an unprecedented increase in State aid to financial institutions in the following years. Public intervention was considered necessary to limit the threat that banks posed to financial stability. They were also considered crucial for addressing the systemic bank and sovereign debt crises in a number of countries in the EU. The use of taxpayers’ money for bank bailouts far exceeded State aid to other sectors during the financial crisis. The EU banking sector, which according to the European Federation of Banks contributed 4 % to the EU Member States’ collective GDP in 2017⁴, remains a major beneficiary of State aid. *Figure 1* illustrates the State aid amounts approved between 2008 and 2018. In general, the amount of State aid approved for the financial sector has stabilised.

³ See Joined Cases C-57/00 P and C-61/00 P, paragraphs 99-100.

⁴ *Banking in Europe*: EBF Facts & Figures 2018, p. 12: <https://www.ebf.eu/wp-content/uploads/2018/09/Banking-in-Europe-2018-EBF-Facts-and-Figures.pdf>

Figure 1 – State aid approved between 2008 and 2017



Source: ECA based on European Commission Scoreboard.

08 A reduced need for government intervention in the EU banking sector in recent years has had an impact on the Commission’s State aid control activities. The decrease in aid amounts is reflected in the number of cases the Commission has had to handle. The Commission took on average 57.5 decisions annually from 2009 to 2012. This decreased to eight decisions in 2016, 21 in 2017 and six in 2018. At the time of the audit, the Commission expected aid to decrease further in the future.

09 As a consequence of the financial crisis, the EU adopted a number of measures to ensure the stability of the financial sector. In March 2009, the European Council agreed on the need to improve the regulation and supervision of financial institutions within the EU and based on the “de Larosière Report”⁵, in particular the creation of a European Systemic Risk Board (ESRB) responsible for macro-prudential oversight (for more detail see [Box 2](#)).

⁵ Report, The High-Level Group on Financial Supervision, Brussels, 25 February 2009, https://ec.europa.eu/economy_finance/publications/pages/publication14527_en.pdf

Box 2**Monitoring systemic risk in EU financial sector after the global financial crisis**

Established in 2010, the ESRB is in charge of monitoring and assessing systemic risks for the purpose of limiting the risk of failure of systemic components and enhancing the financial system's resilience to shocks, thereby mitigating negative impacts on the internal market and the real economy.

If the ESRB detects a risk which could seriously jeopardise the orderly functioning and integrity of the financial markets or the stability of the whole or part of the Union's financial system, it should promptly inform the Council of the situation.

If the ESRB determines that an emergency situation may arise, it should contact the Council and provide an assessment of the situation. The Council should then assess the need to adopt a decision addressed to the European Supervisory Authorities determining the existence of an emergency situation.

10 The post-crisis repair also prompted an overhaul of the EU's micro-prudential framework, establishing an EU-wide crisis-management framework and fostering common supervisory approaches. The Bank Recovery and Resolution Directive (BRRD) was adopted in spring 2014 to provide authorities with comprehensive and effective arrangements to deal with failing banks at national level, as well as cooperation arrangements to tackle cross-border banking failures. So far, the new framework has been applied only in a limited number of cases. In its review of the implementation of the BRRD and the SRM Regulation, the Commission identified some weaknesses, in particular in the coordination between the relevant actors, but considered it premature to design and adopt legislative proposals⁶.

⁶ REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL on the application and review of Directive 2014/59/EU (Bank Recovery and Resolution Directive) and Regulation 806/2014 (Single Resolution Mechanism Regulation), p. 5: <http://ec.europa.eu/transparency/regdoc/rep/1/2019/EN/COM-2019-213-F1-EN-MAIN-PART-1.PDF>

11 The BRRD was introduced with the intention to avoid future bank bail-outs and to protect taxpayers in the EU⁷ and does not prejudice the compatibility of a measure with the EU Treaties under EU State aid rules. Under the BRRD, if a bank requires extraordinary public support, it is deemed failing or likely to fail – a decision to be taken by supervisory or resolution authorities except in the particular circumstances laid down in the Directive - and must be wound down under normal insolvency proceedings or, in exceptional circumstances, resolved. In addition, the BRRD stipulates narrow conditions for the use of government support in resolution. For more details, see [Box 3](#).

Box 3

Conditions for extraordinary support under the BRRD:

Member States support to solvent institutions - precautionary measures (Article 32(4)(d) BRRD):

- required in order to remedy a serious disturbance in the economy of a Member State and preserve financial stability,
- confined to solvent institutions,
- precautionary and temporary,
- proportionate to remedy the consequences of the serious disturbance, and
- not be used to offset losses that the institution has incurred or is likely to incur in the near future.

Support to failed institutions - resolution fund and alternative financing arrangements (Article 44(5) and 101 BRRD):

- losses cannot be passed to other creditors,
- losses totalling not less than 8 % of total liabilities including own funds have already been absorbed, and

⁷ European Commission, New crisis management measures to avoid future bank bail-outs, June 2012: https://ec.europa.eu/commission/presscorner/detail/en/IP_12_570
See also European Council - Brussels – 12-13 December 2012 – Conclusions, point 11.

- o funding provided by the resolution fund is limited to the lower of 5 % of total liabilities including own funds or the means available to the resolution fund and the amount that can be raised through ex-post contributions within 3 years.

Support to failed institutions - Government financial stabilisation tools (Article 56 BRRD):

- o as a last resort after having assessed and exploited the other resolution tools to the maximum extent practicable whilst maintaining financial stability.

12 Another response to the financial crisis was the creation of the Banking Union. Although still incomplete at the current juncture, institutional integration has gone even further among euro area Member States⁸. The first two pillars of the Banking Union – the Single Supervisory Mechanism (SSM) and the Single Resolution Mechanism (SRM) – have been established. The third pillar, a common system for deposit protection, is not yet in place. Moreover, according to the Commission, further measures are needed to tackle the remaining risks of the banking sector (in particular, those related to non-performing loans, or the initiatives to help banks diversify their investment in sovereign bonds)⁹.

13 The EU's economic climate had improved considerably since the global financial crisis and it remained generally favourable up to the outbreak of COVID-19. There is broad consensus that banks in Europe have become more resilient, thanks to the measures taken after the financial crisis. However, their profitability remains low. Europe has too many banks, and the post-crisis European banking sector is more

⁸ For a comprehensive overview see REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL on the application and review of Directive 2014/59/EU (Bank Recovery and Resolution Directive) and Regulation 806/2014 (Single Resolution Mechanism Regulation) – Introduction: https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/190430-report-bank-recovery-resolution_en.pdf

⁹ EU Commission, Completing the banking union: https://ec.europa.eu/info/business-economy-euro/banking-and-finance/banking-union/what-banking-union_en#completing-the-banking-union

fragmented across national borders than before the crisis¹⁰. Legacy problems still exist in some countries. There has been progress on the resolution of non-performing loans (NPLs), but the current NPL level in the EU is still higher than in other major developed countries¹¹. Moreover, NPLs may increase again if the impacts of the COVID-19 outbreak on the economy cannot be mitigated.

14 It has to be noted that the role of the Commission as the controller of State aid cannot be viewed in isolation regarding the financial sector. The Commission is only one important link in a chain. A chain that also consists of Member States deciding to support a bank, bank management, external auditors, bank supervisors and resolution authorities who all have a role to play. It might so happen that State aid control comes into play if the newly established system did not perform as intended. In earlier Special Reports issued by the ECA in 2017¹² and January 2018¹³ we identified deficiencies in the preparations for resolution (SRB) and some design flaws in and signs of inefficient implementation of the crisis management framework (ECB). In addition, there continue to be concerns that the banking sector may still not be ready for the new, stricter rules. Thus, the Commission's role continues to be crucial and challenging at the same time.

¹⁰ See, for example Mario Draghi, Foreword to the ECB Annual Report on supervisory activities 2018: <https://www.bankingsupervision.europa.eu/press/publications/annual-report/html/ssm.ar2018~927cb99de4.en.html#toc1>

The report on the EUROFI FINANCIAL FORUM 2019 provides a detailed account of the views expressed by public and private sector representatives on the latest regulatory developments in the financial sector and how to improve the functioning of the EU financial market: <http://helsinki2019.eurofi.net>

¹¹ The amount (€658 billion) and the ratio of non-performing loans (NPLs) of 3.2 % had reached the lowest level in Q4 2018 while dispersion across EU/EEA countries had remained high (0.45 % to 41.2 %). See EBA Risk Dashboard Q4 2018: <https://eba.europa.eu/sites/default/documents/files/documents/10180/2666948/5836f313-b390-4f24-99bf-815fc036a7ce/EBA%20Dashboard%20-%20Q4%202018.pdf>

¹² Special report 23/2017: Single Resolution Board: Work on a challenging Banking Union task started, but still a long way to go: https://www.eca.europa.eu/Lists/ECADocuments/SR17_23/SR_SRB-BU_EN.pdf

¹³ Special report 02/2018: The operational efficiency of the ECB's crisis management for banks: https://www.eca.europa.eu/Lists/ECADocuments/SR18_02/SR_SSM2_EN.pdf

State aid to financial institutions – the State aid rules

15 The mandate of the Commission in the implementation of Articles 107 and 108 TFEU is to preserve competition in the internal market and a level playing field in the EU. During the financial crisis, the State aid framework was adapted to focus on financial stability as an overarching objective, for the banking sector, while seeking to ensure that aid and distortions of competition between banks and across Member States were kept to the minimum necessary. The latter is crucial to ensure State aid does not obliterate the level playing field between aid recipients and their competitors and healthier companies, while also limiting the amount of taxpayers' money going into failed financial institutions¹⁴. The Commission set out specific State aid rules for the application of Article 107(3) for aid to financial institutions during the crisis, hereinafter the crisis rules, which were amended in 2010, 2011 and 2013 (see **Box 4**). The 2013 Banking Communication repealed the 2008 Banking Communication and made certain revisions to the Impaired Asset Communication and the Restructuring Communication¹⁵.

¹⁴ Commission website "Competition policy and economic recovery, Tackling the financial crisis, State aid": https://ec.europa.eu/competition/recovery/financial_sector.html (last update: 16.4.2012).

¹⁵ See Section 7 of the 2013 Banking Communication.

Box 4**Commission Communications for financial institutions**

Communication from the Commission — The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis, 13 October 2008 (see [IP/08/1495](#))

Communication from the Commission — The recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition, 5 December 2008 (see [IP/08/1901](#))

Communication from the Commission on the Treatment of Impaired Assets in the Community Banking Sector, 25 February 2009 (see [IP/09/322](#))

Communication from the Commission — Temporary framework for State aid measures to support access to finance in the current financial and economic crisis, adopted on 17 December 2008 (see [IP/08/1993](#)), as amended on 25 February 2009.

Communication from the Commission — The return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules, 23 July 2009 (see [IP/09/1180](#))

Communication from the Commission — on the application, from 1 January 2011, of State aid rules to support measures in favour of banks in the context of the financial crisis (see [IP/10/1636](#))

Communication from the Commission — on the application, from 1 January 2012, of State aid rules to support measures in favour of banks in the context of the financial crisis (see [IP/11/1488](#))

Communication from the Commission — on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis (see [IP/13/672](#))

16 On 19 March 2020, the Commission adopted a Temporary Framework to enable Member States to further support the economy in the COVID-19 outbreak¹⁶. Concerning banks, the Communication states that aid to non-banks will not be considered as (in-direct) aid to banks and that measures to support banks in case of direct damage suffered as a result of the Covid-19 outbreak would be considered as measures under Article 107(2)(b) TFEU and would not be assessed under the existing rules. Any measures, which fall outside the Communication or are not covered by Article 107(2)(b) TFEU must be notified to the Commission and shall be assessed under the State aid rules applicable to the banking sector. Hence, the State aid rules that were subject of this audit remain applicable.

¹⁶ COMMUNICATION FROM THE COMMISSION Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak (2020/C 91 I/01): [https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52020XC0320\(03\)](https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:52020XC0320(03))

Audit scope and approach

17 We have conducted previous audits on competition policy, including State aid control, but we have never carried out a dedicated performance audit on the enforcement of EU competition policy in the area of State aid to financial institutions. We decided to carry out this audit in light of the new regulatory framework for the EU banking sector and market developments.

18 Our audit focused on the period from August 2013 until the end of 2018. We assessed whether the Commission managed the control of State aid to financial institutions appropriately with a view to ensuring that aid was exceptional and limited to the minimum necessary. Focussing on DG COMP, we asked:

- Did the Commission have appropriate tools and resources to carry out its control of State aid?
- Did the Commission enforce the control of State aid to ensure that aid is exceptional and limited to the minimum necessary?

19 In terms of achievement of objectives, we looked at DG COMP's objectives setting, its risk assessment, the suitability of the performance measurement framework and whether DG COMP had performed ex-post evaluations and impact assessments. We analysed the organisational structure within DG COMP (including internal controls and the appropriateness of the resources deployed) as well as DG COMP's ethical framework. Moreover, we analysed whether the Commission had the necessary legal powers and whether the procedural framework and internal processes facilitated efficient and transparent practices. We examined whether the State aid rules for banks were based on ex-ante assessments, whether the current rules were fit for purpose and whether they reflected market and regulatory realities.

In order to assess whether the Commission had been effective in exercising State aid control we examined the entire State aid procedure and also reviewed whether the Commission's processes and procedures ensured that its decisions were sound¹⁷.

20 Ex-ante State aid control by a public authority is unique to the EU. Therefore, we used EU documents to derive standards for our audit. We collected audit evidence by reviewing documents supplied by DG COMP, as well as through interview with staff. We used an expert panel to discuss the main results of our work.

¹⁷ A performance audit is an independent, objective and reliable examination of whether undertakings, systems, operations, programmes, activities or organisations are operating in accordance with the principles of economy, efficiency and effectiveness, and whether there is room for improvement (ISSAI 300). The Court of Justice of the European Union (CJEU) interprets EU law to make sure it is applied in the same way in all EU countries, and settles legal disputes between national governments and EU institutions. It can also, in certain circumstances, be used by individuals, companies or organisations to take action against an EU institution, if they feel it has somehow infringed their rights.

Observations

Achievement of objectives, risk assessment and evaluations

21 The Commission's Internal Control Framework requires setting of objectives, assessment of risks relating to them, and performance measurement. Impact assessments and evaluation of legislation and non-spending activities, unless exempted, are required to be performed in accordance with the guiding principles of the Commission's Better Regulation guidelines, to assess the performance of EU interventions and analyse options and related impacts on new initiatives.

Objective setting and performance measurement

22 DG COMP set objectives with sufficient clarity to identify and assess related risks in accordance with the Commission's Internal Control Framework¹⁸. Up-to-date objectives and mission statements have to be set at every level and for the most significant activities, down to the tasks and objectives assigned to individual staff members. Mission statements must be aligned with the Commission's responsibilities under the Treaties and its policy objectives. As required, DG COMP set objectives clearly enough to identify risks to their achievement in its 2016-2020 Strategic Plan, and further specified and updated these objectives in its (annual) Management Plans (AMP).

23 DG COMP established result and output indicators as required. However, the indicators used do not measure the effect of DG COMP's activities, partly due to factors that are outside of the control of DG COMP. The purpose of performance indicators for objectives is to make it possible to monitor progress towards their achievement¹⁹. DG COMP reported on the achievement of its objectives in its Annual Activity Reports (AARs). **Box 5** includes the indicators discussed in this paragraph for each relevant objective.

¹⁸ Principle 6 of the COMMUNICATION TO THE COMMISSION FROM COMMISSIONER OETTINGER Revision of the Internal Control Framework (Internal Control Framework): https://ec.europa.eu/budget/library/biblio/documents/control/C_2017_2373_Revision_ICF_en.pdf

¹⁹ Principle 6 of the Internal Control Framework - Monitoring.

Box 5

Relevant objectives and indicators (from DG COMP's Annual Management Plans²⁰)

Specific objective 7: Better targeted growth enhancing aid (used from 2013 to 2015)

- **Result indicator 2:** Overall level of crisis aid to the financial sector actually used by Member States, expressed as percentage of 2013 EU 28-GDP.

Specific objective 9: Stability and promotion of competition in the banking sector (introduced in 2016).

- **Result indicator 1 (2016):** For each stress test carried out by the SSM or the EBA, calculate the ratio of a) State aid and Fund aid to banks in the test sample to cover shortfalls identified in the stress test to b) the total capital shortfall identified by the stress test at the respective observation date.
- **Result indicator 2 (2016):** Ratio of (a) State aid to all banks in the EU in the form of capital-relevant instruments to (b) the stock of total capital and reserves for all banks in the EU.
- **Output indicator (since 2017): Adoption of Commission decisions.**

Specific objective 12: EU competition law instruments maintained aligned with market realities and contemporary economic and legal thinking.

- **Result indicator:** Stakeholder consultation on new rules (Eurobarometer 2014).

24 However, the result indicators used reflect external factors and lack a clear causal relationship to the Commission's State aid control activities. For example, for the objective "Better targeted growth-enhancing aid", the result indicator used "percentage of aid compared to GDP"²¹ reflect the fact that there had been less need

²⁰ See AMP's of DG COMP 2013-2018.

²¹ See for example AMPs DG COMP of 2013-2015.

for aid and that GDP has increased in recent years. The result indicators used to measure the Commission's achievement of the objective "Stability and promotion of competition in the banking sector" reflect the increased resilience of banks in general, due partly to the use of taxpayers' money, rather than the Commission's activities²². Moreover, the indicator for the objective of keeping EU competition law in tune with market realities showed stakeholders' satisfaction with their level of involvement in consultations²³, but not whether rules were aligned with market realities.

25 The Commission's performance indicators did not measure the success of restructurings or the impact of its State aid decisions on the EU banking markets. The Commission had not defined performance indicators that demonstrate that restructurings have been a success, which is crucial in view of the number of cases where banks later turned out not to be viable²⁴. Nor were there indicators to measure the impact of the State aid approved by the Commission on the integrity of the internal market in general and EU banks' cross-border activities in particular.

²² See AMP DG COMP, 2016, specific objective 9:

https://ec.europa.eu/info/sites/info/files/comp_mp_2016_en.pdf

²³ See Eurobarometer Standard Qualitative Study – DG Competition Stakeholder Survey (2014), Aggregate Report, p. 27: "There was a high overall level of satisfaction with DG Competition's consultation on new rules, although some participants felt that their views are not always taken into account":

http://ec.europa.eu/competition/publications/reports/surveys_en.html

²⁴ The purpose of the Commission's requirement to submit restructuring plans and their *ex-ante* assessment is ensuring that viability can be regained within a reasonable timeframe and on a solid and lasting basis (Point 8 of the 2013 Banking Communication). However, several beneficiary banks in our sample required additional government interventions in the form of additional liquidity or equity, after found viable by the Commission. One bank, after two consecutive recapitalisations, required additional aid for its liquidation (in the 3 year of the 5-year restructuring period). Remaining high NPL levels and exposures to sovereign risk are further reasons to doubt the success of restructurings.

Risk assessment

26 DG COMP had identified risks to the achievement of its objectives and determined how such risks should be managed. The Commission’s Internal Control Framework also requires risk assessment and risk management²⁵. DG COMP’s risk assessment process was based on and consistent with the Commission’s risk assessment process. DG COMP had identified and assessed risks in a bottom-up exercise involving the operational units in charge of competition policy enforcement, coordination units and other horizontal units.

27 DG COMP’s risk assessment however, did not include risks to the achievement of the objectives relevant for the control of aid to the financial sector, nor the risk of its rules no longer being aligned with market realities. DG COMP’s risk assessment did not cover potential risks to the achievement of the objectives set specifically for the control of State aid to the financial sector. Moreover, maintaining State aid rules aligned with market realities is crucial to ensure effective enforcement of EU competition law²⁶. In our view, this is particularly relevant for rules meant to deal with the exceptional circumstances triggered by the global financial crisis²⁷. However, the Commission did not categorise the risk that the crisis rules do no longer reflect market realities as a “key risk” for an effective enforcement of the prohibition of State aid.

Impact assessment and evaluation

28 The Commission’s Better Regulation guidelines require an impact assessment process to support policymaking by gathering and analysing evidence. According to the guidelines, policy preparation should be supported by both evaluations and impact assessments. Both look at how a problem is, or should be, addressed to achieve the desired objectives²⁸. The Commission uses evaluations to determine whether EU policies or laws are still justified, whether they need changes, or whether they should

²⁵ Principle 7 of the Internal Control Framework.

²⁶ DG COMP’s 2016-2020 Strategic Plan, p. 39.

²⁷ The 2008 Banking Communication stressed that invoking Article 107(3)(b) of the Treaty is possible only in those genuinely exceptional circumstances (see paragraph 44).

²⁸ Better regulation guidelines, section 3.3, p. 8.

simply be discontinued. The Better Regulation principles also stress that good implementation of policies also involves monitoring their application on the ground. This is to ensure that they achieve their intended results and that – if not, or if there have been unintended consequences – corrective action can be taken.

29 A Commission Staff Working Paper²⁹ and an external study commissioned by the European Parliament³⁰ looked at whether the crisis rules had achieved their objectives in 2011. DG COMP staff concluded that the State aid granted and the State aid control by the Commission had contributed to preserving the Internal Market throughout the crisis. The authors found that distortions of competition had occurred in various ways but concluded that:

- o the Commission had effectively operated a coordination tool that allowed for a consistent treatment of all Member States and banks; and
- o the most efficient means that had allowed the Commission to minimise the risks of distortions of competition had been far-reaching restructuring obligations.

For the period up to 2011, the EP study found that a substantial part of the measures to fight the financial crisis had been outside the scope of State aid rules and that the effect of State aid was difficult to disentangle from the effect of other factors. The authors concluded that:

- o the Commission had not been successful in maintaining a consistent approach across countries and firms; and

²⁹ Commission Staff Working Paper: *The effects of temporary State aid rules adopted in the context of the financial and economic crisis*, Brussels, 5.10.2011 SEC(2011) 1126 final: https://ec.europa.eu/competition/publications/reports/working_paper_en.pdf

³⁰ European Parliament Directorate General for Internal Policies Department A: *Economic and Scientific Policy Economic and Monetary Affairs Study*, “State Aid Crisis Rules for the Financial Sector and the Real Economy”: <https://www.europarl.europa.eu/document/activities/cont/201107/20110714ATT24010/20110714ATT24010EN.pdf> (EP study).

- o differing practices between Member States had weakened the functioning of the internal market, despite efforts by the Commission³¹.

In addition, the study expressed concern about a lack of transparency and underlined the need for the Commission's decisions to be published more swiftly³².

30 There had been no formal evaluation of the current crisis rules. Although the Commission had consulted Member States and other stakeholders prior to the 2013 revision, it had not formally evaluated the effectiveness of the crisis rules. The current version of the Banking Communication was published in August 2013 after consultation with Member States and dialogue with the Economic and Financial Committee including central banks. The Commission also made some modifications to other crisis rules, which remained in place at the time of our audit. The Commission had not formally evaluated the achievement of its objectives nor the EU added value of its crisis rules, with a view to amending or suspending them since then³³. Nor had the Commission formally evaluated the impact of its crisis rules and their application on competition in the EU's banking markets.

Management structures, ethical framework and resources

31 The Commission's internal control framework requires the establishment of comprehensive management structures. Management structures must allow effective internal supervision of all related activities and support the achievement of its objectives. It must delegate appropriate responsibilities and design and implement proper reporting lines that enable the execution of authority, the fulfilment of responsibilities and flow of information³⁴. In addition, the Commission should have a

³¹ EP Study, Chapter 2.4.2. Maintaining a consistent approach across countries and firms and 2.5 Main Findings.

³² EP Study, p. 39.

³³ The only available document dealing with the impacts of the State aid approved by the Commission is a *Competition State aid brief* "State aid to European banks: returning to viability". This document, which only presents the authors' not the Commission view, seeks to demonstrate that the restructuring plans approved by the Commission under State aid rules have helped to save many European banks and made them viable again.

³⁴ Principle 3 of the Internal Control Framework.

competent workforce and deploy its resources effectively in support of the delivery of its priorities and core business³⁵.

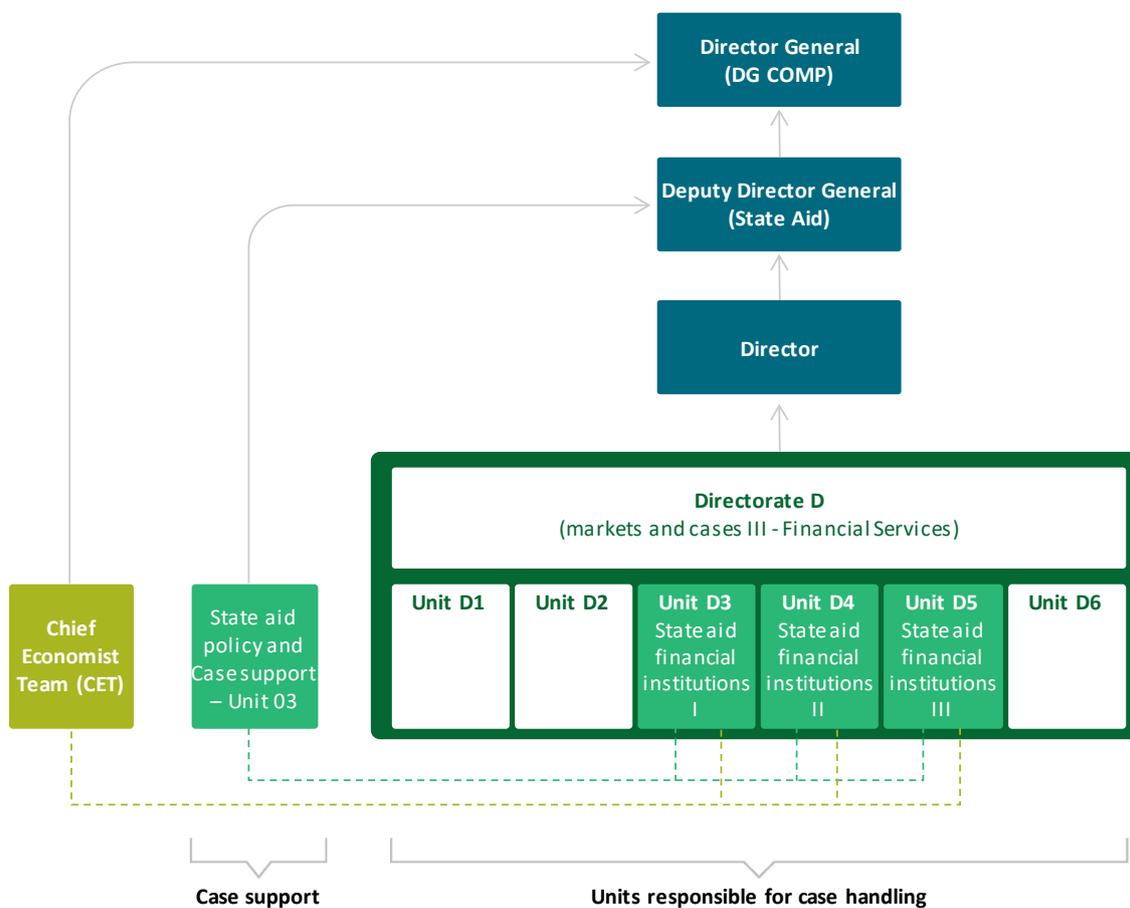
Management structures

32 A matrix structure with proper reporting lines allowed for appropriate information flow and adequate internal supervision by senior management.

DG COMP had established an instrument-sector based matrix structure designed to promote instrument and sector knowledge. Three dedicated units were in charge of handling cases of State aid to financial institutions. A coordination unit provided support on substance and procedural issues, and the Chief Economist Team was involved in the process, but there was no documentation of its input in terms of detailed economic analysis concerning the resulting distortions of competition or the existence of market failures in individual cases. *Figure 2* illustrates the organisational structures responsible for the control of State aid to financial institutions.

³⁵ AMP DG COMP 2018, Objective 2.

Figure 2 – Organisational structure for state aid control to financial sector



Source: ECA based on DG COMP's organigram.

Ethical framework

33 DG COMP promoted a strong ethical culture, focusing on prevention. In line with the Commission's policy of fostering a corporate ethical culture, DG COMP focused on prevention by education and training. Staff have to submit an annual declaration that they will comply with the ethical rules. Case-handlers have to sign a conflict of interest form for every case in which they were involved. Potential conflicts are assessed on a case-by-case basis.

34 DG COMP's ethical framework refers to the general obligations for EU staff and highlights that dissemination of insider information and insider trading are criminal offenses. Unlike staff in other Commission departments, DG COMP staff, as well as any other Commission staff involved in State aid cases, can have privileged access to market sensitive information on individual market participants. In addition, its decisions in State aid cases have a significant impact on financial markets, particularly

on the prices of beneficiaries' shares and bonds. Nevertheless, DG COMP did not have monitoring or other arrangements in place to check that staff complied with the rules when making financial transactions.

Human and IT resources

35 The Commission had allocated sufficient staff resources, but attracting and keeping the necessary talent had become more challenging. Staff generally had strong educational backgrounds and specialist knowledge, as well as relevant work experience. Well-designed on-the-job training and a mentoring programme, as well as an intranet knowledge-sharing tool, allowed new staff to become familiar with their tasks and more experienced case-handlers to keep their knowledge up to date. Directorate D had faced a wave of departures in 2015 and 2016, and a number of highly experienced staff had recently left³⁶. DG COMP had struggled to find suitable candidates, but had taken mitigating measures. Overall, the Commission was well equipped for dealing with a largely reduced number of cases during the audited period.

36 The Commission plans to introduce new IT systems to help management and staff to perform, document and monitor their work more efficiently. The Commission's IT systems are meant to contribute to the secure, efficient and integrated management of competition cases and provide essential support for its daily operations. DG COMP did not have a single system for automatically collecting and storing all documents related to a case, but rather used various applications. However, DG COMP had decided to lead the development of a new common case management system to replace the ageing case and document management systems. In this way, it intends to modernise its IT systems and to address the risk of no longer being able to maintain its enforcement capacity due to insufficient performance of its current IT system³⁷.

Framework for State aid control and State aid rules

37 Appropriate powers and procedural tools are a precondition for efficient and effective State aid control. State aid rules should be well drafted in order to ensure they adequately reflect the objectives of the Treaty and promote a restrictive

³⁶ Case Management Plan April and November 2018, p. 23.

³⁷ Risk registry table: actionable risk number 22.

interpretation of the exception from the rule that prohibits State aid. To this end, it is also crucial that they reflect market realities (including relevant changes in the regulatory framework) in any given period of time.

Procedural framework for State aid control

38 The Commission has the necessary powers for effective and efficient State aid control. Under Article 108(3) TFEU, Member States must notify the Commission of planned measures and must not put them into effect without prior Commission approval. The principle of sincere cooperation requires the EU and the Member States to assist each other. In addition, Member States must take any appropriate measure to ensure fulfilment of their obligations arising out of the Treaties and facilitate the achievement of the EU's tasks and objectives³⁸.

39 The Procedural Regulation provides an appropriate framework for the exercise of the Commission's powers. The Procedural Regulation and its predecessors stipulate rules for State aid procedures. Member States must notify the Commission in sufficient time of any plans to grant aid and, in the notification, provide all information necessary to enable the Commission to take a decision³⁹. The Commission must examine a notification as soon as it receives it. After a preliminary examination, within 2 months of receiving a complete notification⁴⁰, the Commission will:

- o where it finds that the notified measure does not constitute aid, take a decision to this effect;

³⁸ Article 4(3) of the Treaty on European Union (TEU).

³⁹ Article 2 of the Procedural Regulation.

⁴⁰ As per article 4(5) Procedural regulation, "the notification shall be considered as complete if, within 2 months from its receipt, or from the receipt of any additional information requested, the Commission does not request any further information. The period can be extended with the consent of both the Commission and the Member State concerned. Where appropriate, the Commission may fix shorter time limits".

- where it has no doubts as to the measure's compatibility with the internal market, decide that the measure is compatible ('decision not to raise objections')⁴¹;
- where it has doubts as to the measure's compatibility with the internal market, decide to initiate proceedings pursuant to Article 108(2) TFEU ('decision to initiate the formal investigation procedure')⁴².

Where the Commission has not taken such a decision, the aid will be deemed to have been authorised⁴³.

40 In particular, the Commission has the legal powers to ensure that its decisions are based on complete and correct information. The requests for information under the Procedural Regulation serve to provide the Commission with the information needed in order to make an assessment. Under Article 5 of the Procedural Regulation, the Commission can request information from notifying Member States at any stage of the procedure. When the Commission opens a formal investigation procedure under Article 4(4) of the Procedural Regulation interested parties can submit comments and the Commission may request market information from other sources under certain conditions⁴⁴. Moreover, in cases where incorrect information from the notifying Member State was a determining factor for a decision, Article 11 of the Procedural Regulation grants the Commission the power to revoke that decision.

41 In addition to the formal procedures and powers set out in the Procedural Regulation, the Commission had developed voluntary cooperation procedures, notably 'pre-notification contacts', which are described in a Best Practice Code. The Code of Best Practice for the conduct of State aid control procedures (the "Best

⁴¹ Article 4 of the Procedural Regulation.

⁴² Article 4(4) of the Procedural Regulation.

⁴³ Article 4(6) of the Procedural Regulation (also known as Lorenz procedure).

⁴⁴ See Article 7 of the Procedural Regulation.

Practice Code”)⁴⁵ had been updated in 2018⁴⁶ after consultation with Member States and other stakeholders. According to the Commission, the pre-notification phase offers the chance to discuss the scope of the information to be submitted and to provide guidance to a Member State to ensure a notification is complete. The 2018 revision of the Best Practice Code recognised that pre-notification contacts can include discussing legal and economic aspects of measure in an informal and confidential manner before it is formally notified as a best practice, particularly to address those aspects that might not be fully in line with the State aid rules, including in cases where significant changes to the measure are necessary⁴⁷. *Figure 3* gives an overview on the differences between the formal and informal procedures.

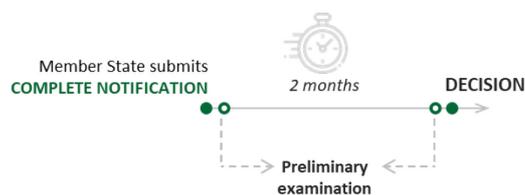
⁴⁵ Code of Best Practice for the conduct of State aid control procedures (2009/C 136/04): <https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:C:2009:136:0013:0020:EN:PDF>

⁴⁶ Code of Best Practices for the conduct of State aid control procedures (2018/C 253/05): [https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018XC0719\(01\)&from=IT](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018XC0719(01)&from=IT)

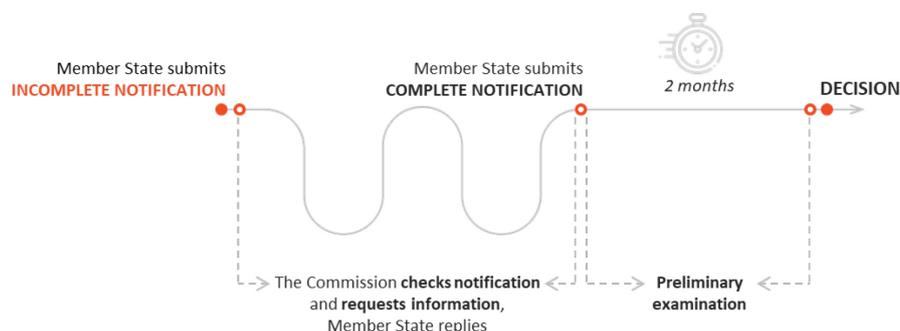
⁴⁷ See Point 11 of the 2018 Best Practice Code.

Figure 3 – Procedure regarding a notified aid

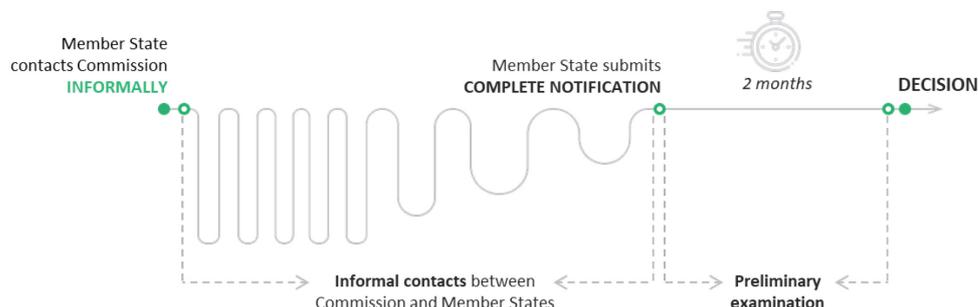
Complete notification



Incomplete notification



Informal procedure



Source: ECA.

42 The Commission had opted to recognise an extended scope and duration of the pre-notification contacts as best practice. The 2018 revision thus extended the recommended indicative timeline for pre-notification contacts from two to six months. The summary of replies to the public consultation⁴⁸ showed that Member States generally appreciated the existence of this informal consultation. Still, some found that the duration was too long. Two out of the 21 respondents called for more transparency. In our view, the length of the pre-notification phase, which may be one indicator of doubts after notification, may also increase the risk of legal challenges.

⁴⁸ Summary of submissions in response to the Public Consultation on the Code of Best Practice on the conduct of State aid control proceedings:
https://ec.europa.eu/competition/consultations/2016_cbp/submissions_summary_en.pdf

State aid rules

43 The Commission's rules for the control of State aid to the financial sector are generally well drafted and clear. The 2013 Banking Communication is drafted in a clear and straightforward way and is largely consistent with previous Crisis Communications. It follows the same structure as the 2008 Banking Communication, which makes it easier to comprehend the general logic and functioning of the rules. However, the lack of explicit criteria for the determination of serious disturbance means that the Commission has a great margin of appreciation.

44 The Commission is committed to State aid rules that are fit for purpose and to ensuring that they are aligned with market realities and contemporary economic and legal thinking. The principle that State aid rules have to be kept up-to-date was also explicitly emphasised in the 2013 Banking Communication⁴⁹. The initial crisis rules, including the 2008 Banking Communication, followed an ECOFIN Council conclusion and reflected market realities at that time. Back in 2008, prompted by the impact of the global financial crisis, the ECOFIN Council had decided to take all necessary measures to enhance the soundness and stability of the banking system to restore confidence in the proper functioning of the financial sector, when even fundamentally sound banks had no access to funding due to the general market turmoil. At the time, in the 2008 Banking Communication the Commission considered the genuinely exceptional circumstances to allow for the application of the former Article 87(3)(b) TEC, which is now Article 107(3)(b) TFEU (see [Box 6](#)). The current 2013 Banking Communication also emphasises that derogation from Article 107(3)(b) TFEU remains possible only as long as such a crisis situation persists, but is not as specific in this regard⁵⁰.

⁴⁹ Point 93 of the 2013 Banking Communication: "The Commission will review this Communication as deemed appropriate, in particular so as to cater for changes in market conditions or in the regulatory environment which may affect the rules it sets out."

⁵⁰ Point 6 of the 2013 Banking Communication.

Box 6**Serious disturbance according to 2008 Banking Communication**

“It needs to be emphasised, however, that the above considerations imply that the use of Article 87(3)(b) cannot be envisaged as a matter of principle in crisis situations in other individual sectors in the absence of a comparable risk that they have an immediate impact on the economy of a Member State as a whole. As regards the financial sector, invoking this provision is possible only in genuinely exceptional circumstances where the entire functioning of financial markets is jeopardised.

Where there is a serious disturbance of a Member State's economy along the lines set out above, recourse to Article 87(3)(b) is possible not on an open-ended basis but only as long as the crisis situation justifies its application.”

45 The Commission had reviewed and adapted its Communications as economic conditions gradually improved in 2010 and 2011. The Commission had reviewed the 2008 Banking Communication in 2010 and again in 2011, determining both times that Article 107(3)(b) of the Treaty remained applicable. According to the revised communications, the Commission justified the article’s use in light of a faster-than-expected economic recovery, and adapted them with a view to preparing the transition to the post-crisis regime and to designing permanent State aid rules for bank rescue and restructuring in normal market conditions. In 2011, the Commission explained that the exacerbation of tensions in sovereign debt markets that took place in 2011, had put the banking sector in the Union under increasing pressure.

46 The Commission had amended the crisis rules in 2013 after consultations with Member States and other stakeholders. The current version of the Banking Communication was published in August 2013 after consultation with Member States and dialogue with the Economic and Financial Committee. Unlike the original crisis rules, for the latest iteration there was no ECOFIN Council Resolution.

47 However, there had not been a review of the latest version from 2013; nor was one planned at the time of our audit. The 2013 Banking Communication explicitly stipulated that “the Commission will review this Communication as deemed appropriate, in particular so as to cater for changes in market conditions or in the regulatory environment which may affect the rules it sets out”. The European Parliament called on the Commission repeatedly to re-evaluate on an annual basis whether the requirements for the application of Article 107(3)(b) TFEU in the financial

sector continue to be fulfilled⁵¹. The Commission did not formally evaluate the 2013 Banking Communication nor whether the application of Article 107(3)(b) was still justified after 2013 and until the end of the audited period. Neither was a formal evaluation planned for the near future at the time of our audit. According to the Commission, there was no obligation to review at a pre-determined date, nor any automatic trigger for one.

48 The crisis rules continued to be applicable without changes although the economic conditions in the EU and its financial markets had changed since the last revision of the State aid rules in 2013 and they have been generally favourable until the outbreak of COVID-19. The EU banking sector still faced challenges, but these have become less widespread. Other EU institutions in charge of financial stability did not determine during the audited period whether systemic risks continued to seriously jeopardise the orderly functioning and integrity of financial markets or the stability of the whole or part of the EU's financial system. Moreover, in the 2013 Banking Communication, the Commission had emphasised the need to ensure a smooth passage to the future BRRD regime and a smooth interplay between the different roles and responsibilities of all the authorities involved⁵². The crisis rules were not reviewed following the transposition of the BRRD as of January 2015 and January 2016.

49 In addition, the crisis rules did not include specific provisions for the State aid assessment of government interventions that are compatible with the BRRD. The precautionary and temporary measures permissible under Article 32 BRRD are limited to solvent institutions (see **Box 3**). In the 2013 Banking Communication, the Commission recognised that, due to the specificities of credit institutions and in the absence of mechanisms allowing for the resolution of credit institutions without threatening financial stability, it might not be feasible to liquidate a credit institution under ordinary insolvency proceedings. For that reason, State measures to support the liquidation of failing credit institutions may be considered as compatible aid, subject to compliance with the requirement specified in point 44. Such mechanisms, in the form of resolutions tools, had to be in place by 1 January 2016. The Commission considered that its approach continued to be appropriate.

⁵¹ For example, point 33 of the European Parliament resolution of 19 April 2018 on the Annual Report on Competition Policy (2017/2191(INI)).

⁵² Points 13 and 14 of the 2013 Banking Communication.

50 As regards burden sharing, the BRRD is stricter than the 2013 Banking Communication. Since the transposition of the BRRD, government support had to comply with the BRRD bail-in requirements, in addition to being compatible with EU State aid rules. Moreover, when the Commission undertakes State aid assessments of the government stabilisation tools referred to in the BRRD, it should separately assess whether the BRRD requirements, in particular those relating to the minimum loss absorption requirement of 8 % are complied with, as well as whether there is a very extraordinary situation of a systemic crisis justifying resorting to those tools⁵³. The BRRD stipulates stricter bail-in requirements than 2013 Banking Communication in order to achieve one of the legislators' objectives: to protect public funds by minimising reliance on extraordinary public financial support to failing institutions⁵⁴, which were not reflected in the State aid rules. For more detail, see [Figure 4](#).

Figure 4 – Bail-in requirements for public support in resolution

Under BRRD

(Art. 44 and 101 BRRD)

- Bail-in of shareholders, junior debt holders, senior debt holder including (non-protected) depositors
- Minimum requirement for bail-in: not less than 8 % of total liabilities
- Cap on public support of funding: the lower of 5 % of total liabilities or the means available to the resolution fund



Under State aid rules

(point 44 BC)

- No bail-in of senior debt holders and depositors
- No minimum requirement for bail-in
- No cap on public support

Source: ECA.

⁵³ Recital 57 of the BRRD.

⁵⁴ Recital 45 of the BRRD.

Exercise of State aid control

51 Compliance with internal processes and procedures ensures the achievement of objectives and fosters accountability. Adherence to the highest standards of professionalism and intellectual rigour (including of legal and economic analysis) as well as ensuring due process and transparency are paramount for the quality of the exercise of State aid control activities. According to its internal control framework, the Commission should define corporate policies that establish what is expected and procedures to put policies into action⁵⁵. Control activities need to verify adherence and thus ensure that objectives are achieved.

Adherence to internal processes and procedures

52 The Commission's State aid control adhered to the structures, reporting lines, and authorities and responsibilities established for this purpose, ensuring appropriate management and political oversight. The internal decision preparation process – which takes place before any decision is proposed to the Commissioner for Competition – is subject to multiple checks, balances and controls. Together with other relevant actors, the management decides on the line to take and preferred options. Multiple management and operational meetings provide an opportunity to discuss, review and decide on key issues. The case-shaping meetings allow the responsible Deputy Director-General to be involved at an early stage, depending on the complexity and the phase of the case. The College of Commissioners decides collectively on a given case, thus giving them overall political responsibility.

53 The decision-making process gave other DGs the opportunity to raise their concerns. The final consultation between different Commission departments before taking a decision is the inter-service consultation (ISC). Its purpose is to align their positions and work out a common approach before bringing a proposal before the College. If this consultation gave rise to a negative opinion on the proposal, it would need to be changed before being brought before the College. If the opinion is positive with comments, the proposal is accepted and it is up to the lead department, i.e. DG COMP, to consider the comments.

⁵⁵ Principle 12 of the Internal Control Framework – Control activities: Deploys through policies and procedures.

54 In all of the sampled cases, other Commission departments had agreed to DG COMP's proposals as required. Other Commission departments, particularly the Directorate-General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA) and the Legal Service, had been consulted and provided their opinions in all instances. Our sample did not include cases where other DGs had given a negative opinion. In a few cases, positive opinions included comments and questions on for example, the justification provided, the reasoning and the economic assessment.

55 The Commission's case-handling activities largely adhered to its non-binding and continuously updated internal guidelines. Internal working tools such as the Manual of Procedures⁵⁶ operationalise how to conduct an investigation and internal arrangements such as reporting lines and the detailed administrative steps in case-handling, in order to ensure that the procedural requirements are met. The Manual of Procedures covers every potential step in the lifetime of a case to ensure a flawless case-handling process.

56 The Commission endeavours to ensure consistent document management to facilitate public access to documents. Access to documents is an essential component of the policy of transparency being implemented by the European institutions. Under the Treaty, all EU citizens and residents enjoy this right of access⁵⁷. The Commission has put in place standard rules to ensure that it is able, at any time, to provide information on matters for which it is accountable. On 16 January 2015, prompted by the fact that retrieving important documents often took too long because they were not properly registered, filed and preserved, the Secretariat-General issued a note on document management and access to documents. It emphasised that good document management within the Commission was essential for the institution's efficiency and effectiveness, for facilitating the exchange and retrieval of information, and for ensuring compliance with the applicable regulations on, among other things, access to documents. For more detail on document management at the Commission, see **Box 7**.

⁵⁶ A public version is available on the Commission's website – *EU Competition law State Aid Manual of Procedures* – Internal DG Competition working documents on procedures for the application of Articles 107 and 108 TFEU Revision 10/7/2013:
https://ec.europa.eu/competition/state_aid/studies_reports/sa_manproc_en.pdf

⁵⁷ Regulation (EC) No 1049/2001 of the European Parliament and of the Council of 30 May 2001 regarding public access to European Parliament, Council and Commission documents Official Journal L 145, 31.5.2001, pp. 0043 – 0048.

Box 7

Document management at the Commission⁵⁸

The Commission's Guidelines on document management and access to documents and the Commission Decision on document management require that a document drawn up or received by the Commission must be registered if it contains important information, which is not short-lived and/or may involve action or follow-up by the Commission or one of its departments. Since keeping documents in a working space such as shared drives or electronic mailbox folders does not ensure their integrity, preservation and retrieval. It is therefore essential that all documents that meet the registration criteria defined in the eDomec rules are actually registered in Ares or in another Commission document management system.

The guidelines include a non-exhaustive list of documents which require action or follow-up or involves the responsibility of the institution and, therefore, are important and have to be registered:

- formal notes/communications, both received and sent;
- financial documents; (as per BUDG guidelines);
- minutes of meetings, especially with other institutions or external stakeholders, and, for important meetings, briefings/speaking/defensive etc;
- information received/sent from/to other institutions or external stakeholders;
- contributions to inter-service consultations or pre-consultations;
- documents, even informal (e-mails or notes to the file) that attest situations or events, justify decisions made or otherwise explain the development of official actions;
- instructions notes, guidelines.

Documents that do not have to be registered include:

- drafts (i.e. documents not yet validated by the person who will sign them or take responsibility for them);
- e-mails and other texts circulated within an informal exchange of views between colleagues;
- exchanges on short lived matters (such as invitations);

- o information on one's personal situation.

57 DG COMP's document management largely complied with the standards.

DG COMP's State aid Manual of Procedures stipulates requirements for DG COMP's document management that complement and further specify the Commission's uniform rules⁵⁹. The Manual of Procedures states that all "relevant" case-related information must be stored in ISIS⁶⁰. It adds that the registration requirement applies in particular to all documents that might be relevant in the case of litigation.

Documents are not registered automatically but rather on request by case-handlers unless submitted via SANI, the official notification tool. The Commission, in general, systematically registered documents in ISIS as required. However, (case-related) briefings and minutes of coordination meetings and meetings with the Commissioner were not registered in the case files but in separate files⁶¹. Minutes of most meetings with Member States had been taken and registered. However, there were also few instances where this was not the case⁶². In addition, we found evidence of contacts before the pre-notification phase that were not documented in ISIS.

⁵⁸ Secretariat General, NOTE TO DIRECTORS GENERAL, HEADS OF CABINET AND DIRECTORS OF EXECUTIVE AGENCIES Subject: Document management and access to documents: https://www.asktheeu.org/de/request/2786/response/9713/attach/6/Ares%202015%20182108%20persdataremoved%20Redacted.pdf?cookie_passthrough=1

These guidelines were updated in 2018 in order to provide updated guidance on what should be registered including updated practical registration criteria to ensure that all relevant documents have been registered and can be retrieved. The updated list contains all documents included in the 2015 list.

⁵⁹ ManProc, section 2.2 Document management – ISIS.

⁶⁰ ISIS is the document management system used for case-handling activities. DG COMP deploys various applications to collect and store documents. ISIS is just one such system. Other applications include DECIDE, for monitoring and recording the Commission-wide decision-making process, and SANI, for Member States to send State aid notification forms. Case-related working documents and files produced by the case team that are not directly relevant are stored in the unit's electronic case library (shared drive).

⁶¹ These files were not included in our review which was limited to the case files.

⁶² This is not compliant with the Commission Guidelines, which emphasise that minutes of meetings, especially with other institutions or external stakeholders, and, for important

58 The internal State aid Manual of Procedures and the State Aid Best Practices Code stipulate non-binding comprehensive guidance for pre-notification contacts, which were not always fully adhered to. According to the Manual of Procedures⁶³, pre-notification contacts should, in principle, only take place on the basis of a written draft notification. This draft notification should be sent via secured email and be registered in ISIS. There were separate pre-notification files for every State aid procedure from our sample. In most cases, they comprised parts of the compatibility review such as the analysis of restructuring plans and the negotiation of commitments but did not contain written draft notifications.

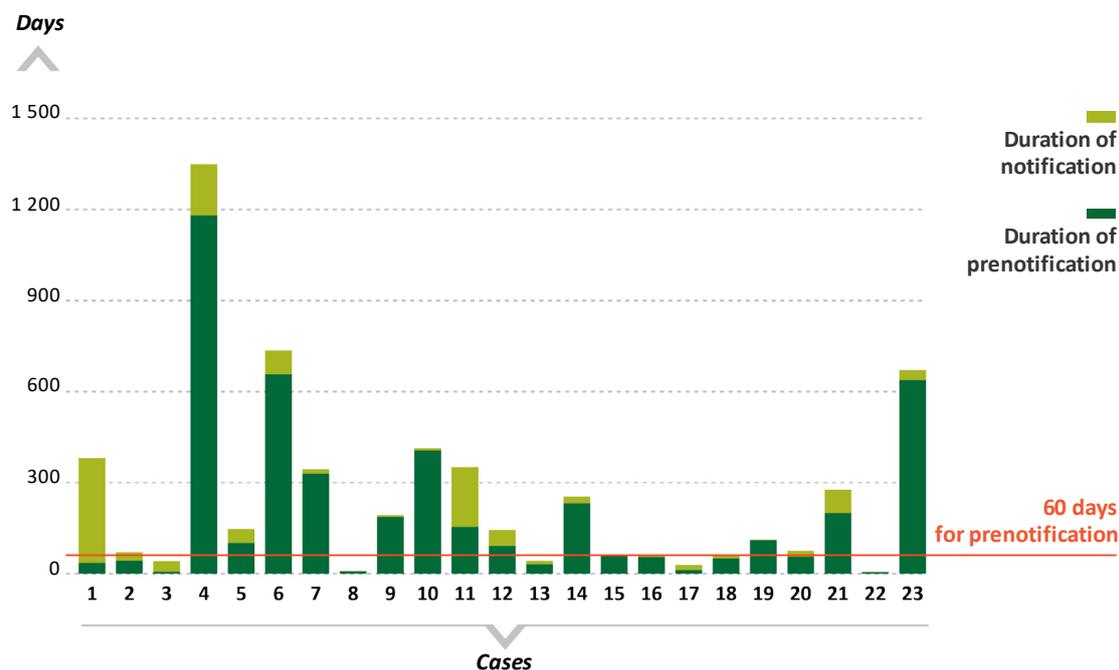
59 The pre-notification phase did not always result in shorter overall procedures as intended. Pursuant to the Manual of Procedures, the pre-notification phase should ideally not last more than 2 months in standard cases, ideally followed by the complete notification. In more complex cases, an extended pre-notification phase may be appropriate⁶⁴. In 11 out of 23 cases, the pre-notification phase did not exceed 2 months. However, in the instances where it took longer, there were long delays: 9 out of 12 of such pre-notification contacts lasted over 150 days (up to 1 181 days). In most cases where there had been pre-notification contacts (18 out of 23), the Commission was able to take a decision within 2 months of the official notification. However, the average duration of the procedures, including pre-notification contacts, was 253 days and the longest procedure took 1 350 days, which may be explained by the technical complexity of the banking cases. The Commission had, after consultation with Member States, revised the Best Practice Code in 2018, with an indicative length of the pre-notification period of 6 months. A complete list showing the duration of the procedures in our sampled cases can be found in [Figure 5](#).

meetings, briefings/speaking/defensive etc. are important and have to be registered. The Commission argued that these concerned information that was not relevant and short-lived and provided explanations for each of these cases.

⁶³ ManProc, section 5.3 Pre-notification – Steps.

⁶⁴ ManProc, section 5.4. Pre-notification – Timing.

Figure 5 – Duration of state aid procedures



Source: ECA based on data submitted by DG COMP.

60 Publishing decisions took a long time, and some relevant information was not published. The Commission is obliged to publish its decisions or a summary notice in the Official Journal. However, Member States can request the non-disclosure of certain information covered by the obligation of professional secrecy. Usually, Member States have 15 working days to make such a request. If no such request is made, the decision will normally be disclosed in full⁶⁵. In such cases, publication should take place within 2 months, according to the Manual of Procedures⁶⁶. We found that in 19 out of 29 cases in our sample, it had taken the Commission more than 100 days to publish the non-confidential version of the decision in the Official Journal⁶⁷. For more details, see

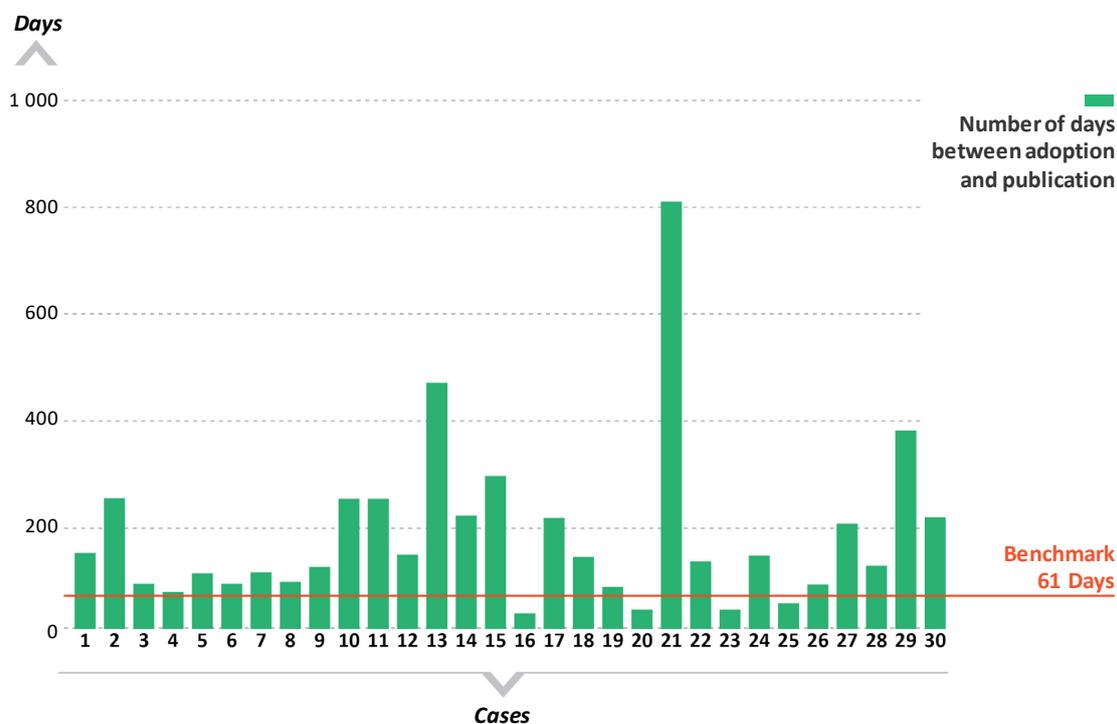
⁶⁵ Article 4.2 of the Communication from the Commission of 1.12.2003 on professional secrecy in State Aid decisions: [https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52003XC1209\(02\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52003XC1209(02)&from=EN)

⁶⁶ ManProc, section 1.1.1 – 1.2. The non-confidential version.

⁶⁷ There were also cases where publication took more than 1 year, including one case where it took the Commission more than 2 years to publish a decision it had taken only 2 months to adopt.

Figure 6. We found that in some cases where delays had been caused by Member States, the Commission had tried to expedite the process – sometimes publishing decisions without the Member States’ consent⁶⁸.

Figure 6 – Time taken for publication of decisions



Source: ECA based on data submitted by DG COMP.

61 The Commission rejected unjustified requests to keep information confidential, but rarely published the full text of its decisions. The State aid Manual of Procedures describes the general principles for the publication of decisions set out in the Commission Communication of 1 December 2003 on professional secrecy in State aid decisions, and emphasises the overriding interest in making public the full substance of its decisions, while duly respecting the confidentiality of business secrets. As a result, the Commission rarely agreed to keep all requested information confidential. Nevertheless, most State aid decisions were redacted, and information important for

⁶⁸ Point 26 Communication on professional secrecy: “Where the Member State concerned does not indicate which information it considers to be covered by the obligation of professional secrecy within the period prescribed by the Commission, the decision will normally be disclosed in full.”

understanding their implications was not disclosed in full⁶⁹. Often, Member States had not indicated in time what information they considered confidential or had not provided appropriate reasons. In fact, we found that in a number of instances, case-handlers had considered that such requests did not meet the criteria set out in the Communication (see **Box 8** for examples of what the Commission considers to be business secrets). In addition, the Commission was also not always consistent in its approach. For example, the Commission disclosed figures either partially, published ranges, or there was no information at all.

Box 8

Business secrets according to the Manual of Procedures

Typical examples of business secrets are:

- methods of assessing manufacturing and distribution costs;
- production secrets and processes;
- supply sources;
- quantities produced and sold;
- market shares;
- customer and distributor lists;
- marketing plans;
- cost price structure;
- sales policy;
- information on the internal organisation of the firm.

Turnover is normally not considered a business secret, to the extent that it is published in the annual accounts or otherwise known on the market; requests for confidentiality concerning turnover which are not in the public domain would have to be motivated and evaluated on a case by case basis.

⁶⁹ For example, information on restructuring targets, e.g. on the future Return on Equity to be achieved, is rarely disclosed in a way that would allow interested parties to assess whether restructuring targets have been met.

This type of data can only be considered a business secret if it is "secret", i.e. not publicly available (see paragraph 14(a) of the Communication).

62 The Commission monitored the implementation of its decisions through monitoring trustees. The Commission appoints trustees, paid by the banks, to monitor the implementation of commitments in every case. Commitments may be undertaken either to limit distortions of competition or to ensure the bailed-out bank becomes viable again. Hence, the monitoring encompassed the beneficiaries' financial performance and adherence to other commitments. In addition, this monitoring process provides the Commission with many valuable insights, including on any lack of success in implementing previous measures, as well as information on any new aid measures planned by Member States without informing the Commission as required.

63 The results of monitoring were not published and commitments were sometimes modified. The Commission did not publish information or keep statistics on the number of cases in which commitments had or had not been complied with. The Commission sometimes approved changes to commitments and extended the deadlines for their implementation, even though such changes, according to the Commission requirements, should be exceptional and limited to cases of significant new factual developments. The Commission emphasised that, in such cases, it always ensures that the newly proposed commitments preserved the balance of the original decision. However, we found that the explanations of how this would be achieved were not sufficiently detailed and, for some of the Commission's published decisions did not provide sufficiently detailed explanations.

State aid decisions for financial institutions on substance

64 State aid decisions need to be based on legally and economically sound assessments. As a general rule, the Treaty and the Commission's Rules of Procedure⁷⁰ require the Commission to state reasons, i.e. to justify its decisions. This includes the requirement that decisions be based on legally and economically sound assessments and substantiated by the underlying facts. DG COMP's core principles emphasise that aiming at the highest rigour and quality in legal assessment and economic analysis is key for the quality of its assessments. For the Commission, its case practice and the EU Courts' case law serve as the most important source of guidance in this regard. The

⁷⁰ The Code of Good Administrative Behaviour is an annex to the Commission's Rules of Procedure.

coordinated decision-making process, the checks and balances and quality controls that the Commission has put in place are to ensure that the Commission assessment complies with these requirements in each individual case.

65 The Commission assessed restructuring plans very rigorously, requiring detailed information and scrutinising it thoroughly. The Restructuring Communication stipulates very detailed requirements on the information to be included in a restructuring plan. The Commission requires restructuring plans to be comprehensive, detailed and based on a coherent concept. They should demonstrate how the bank would restore its long-term viability without State aid. The extensiveness and depth of the information that Member States have to submit illustrate the high level of scrutiny to which the Commission subjects restructuring plans (see **Box 9**). In the cases we examined, the Commission had asked for additional or more pertinent information where needed.

Box 9

Information to be included in a restructuring plan pursuant to the Restructuring Communication⁷¹

- Where, on the basis of previous Commission guidance or decisions, a Member State is under an obligation to submit a restructuring plan, that plan should be comprehensive, detailed and based on a coherent concept.
- It should demonstrate how the bank would restore long-term viability without State aid as soon as possible.
- The notification of any restructuring plan should include a comparison with alternative options, including a break-up, or absorption by another bank, in order to allow the Commission to assess whether more market oriented, less costly or less distortive solutions are available consistent with maintaining financial stability.
- In the event that the bank cannot be restored to viability, the restructuring plan should indicate how it could be wound up in an orderly fashion.
- The restructuring plan should identify the causes of the bank's difficulties and the bank's own weaknesses and outline how the proposed restructuring measures remedy the bank's underlying problems.

⁷¹ [https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52009XC0819\(03\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52009XC0819(03)&from=EN)

- The restructuring plan should provide information on the business model of the beneficiary, including in particular:
 - its organisational structure;
 - funding (demonstrating viability of the short and long term funding structure);
 - corporate governance (demonstrating prevention of conflicts of interest as well as necessary management changes);
 - risk management (including disclosure of impaired assets and prudent provisioning for expected non-performing assets);
 - and asset-liability management;
 - cash-flow generation (which should reach sufficient levels without State support);
 - off-balance sheet commitments (demonstrating their sustainability and consolidation when the bank bears a significant exposure);
 - leveraging;
 - current and prospective capital adequacy in line with applicable supervisory regulation (based on prudent valuation and adequate provisioning), and;
 - the remuneration incentive structure, (demonstrating how it promotes the beneficiary's long-term profitability).
- The viability of each business activity and centre of profit should be analysed, with the necessary breakdown [...]

[...] The expected results of the planned restructuring need to be demonstrated under a base case scenario as well as under 'stress' scenarios. For this, restructuring plans need to take account, inter alia, of the current state and future prospects of the financial markets, reflecting base-case and worst-case assumptions. Stress testing should consider a range of scenarios [...].

- Assumptions should be compared with appropriate sector-wide benchmarks, adequately amended to take account of the new elements of the current crisis in financial markets [...].

66 The Commission has exclusive competence for the State aid compatibility assessment and, in this capacity, the Commission considers that the conditions for the existence of a serious disturbance in the Member State have been met in all cases. In its assessment of the serious disturbance in each individual case, the Commission took into account the Member State's submission. By adopting the Banking Communication, the Commission has bound itself to assessing State aid to support the liquidity, viability or orderly exit of banks under Article 107(3)(b) TFEU, due to the crisis situation and the risk for financial stability at large which amount to a serious disturbance in the economy. The Commission then considered that Member States were best placed to make an initial assessment whether an uncontrolled market exit of a particular bank would threaten financial stability (or cause other serious disturbance in the Member State). Correspondingly, the Commission did not contest whether a serious disturbance existed in each individual case. Nor do the crisis rules specify what information a Member State should submit. Except in cases in countries subject to an economic adjustment programme, we rarely found in the case files economic or - in our view - other relevant data to support the assertion that such a disturbance existed.

67 Not all published decisions included details of such assessments of whether there was a serious disturbance⁷². Often, the Commission referred generally to the 2013 Banking Communication without contesting the Member State's arguments on the individual circumstances of the specific case in question (see [Box 10](#)). However, such a general reference does not explain why the Commission considered that a serious disturbance existed in the cases in question with the exception of countries subject to an economic adjustment programme. In our view, neither were such conclusions supported by corresponding assessments by the Council nor the ESRB (for more detail on the mission of the ESRB see [Box 2](#))⁷³.

⁷² Including cases where a country had not experienced negative growth and its banks had avoided serious problems during the financial crisis.

⁷³ Within the remit of its exclusive competence for State aid control, the Commission is neither bound by such assessment nor are they a precondition for the application of Article 107 (3)(b) TFEU.

Box 10

Examples of how the Commission justified the application of Article 107(3)(b) in individual restructuring decisions

“The Commission has acknowledged that the global financial crisis may create a serious disturbance in the economy of a Member State, which can be addressed through State measures supporting financial institutions. This has been successively detailed and developed in the six Crisis Communications, as well as in the 2013 Banking Communication.”

“The Commission recalls that, since the beginning of the financial crisis, it has systematically used Article 107(3)(b) TFEU as legal basis to assess any restructuring or liquidation aid to banks in difficulty. Assessing the present measures under Article 107(3)(b) TFEU is therefore fully consistent with previous cases.”

68 For cases of liquidation aid, the Commission did not contest Member States’ assertions that a potential bank failure constituted a threat to financial stability. The 2013 Banking Communication does not define situations where it might not be feasible to liquidate a credit institution under ordinary insolvency proceedings without threatening financial stability; nor does it define what information Member States must submit as evidence of such a threat. The decisions on liquidation aid in our sample were based on statements on potential threats to financial stability provided by Member States⁷⁴ (see [Box 11](#)). All decisions concerned banks with market shares ranging from 0.02 % to 2 %. There are a number of potential reasons why the failure of even a non-systematically relevant bank could pose a potential threat to financial stability. For the cases we examined, we consider that the Commission did not explain these reasons in the published decisions⁷⁵.

⁷⁴ According to the Commission, Member State authorities are best placed to assess whether an uncontrolled market exit of a particular bank would threaten financial stability, because it is the Member States that have data on exposure to other banks, on interconnectedness or spill-overs.

⁷⁵ This included cases where the SRB had previously rejected assertions that the banks could not be wound down under normal insolvency proceedings without posing a threat to financial stability and refused to apply resolution tools.

Box 11**Examples of how the Commission justified the application of Article 107(3)(b) in individual decisions on liquidation aid**

“In the 2013 Banking Communication, the Commission acknowledged that Member States should encourage the exit of non-viable players, while allowing for the exit process to take place in an orderly manner so as to preserve financial stability. Since the [...] measures are aimed at allowing the positive outcome of a sale that ensures the orderly market exit of the [...] banks as stand-alone entities through their absorption by an eventual purchaser, the Commission considers that it will assess the compatibility of the [...] measures by reference to the 2013 Banking Communication.”

“In the 2013 Banking Communication, the Commission acknowledged that Member States should encourage the exit of non-viable players, while allowing for the exit process to take place in an orderly manner so as to preserve financial stability. As mentioned in recital [...], the resolution authority states the ordinary insolvency procedure would not be apt to achieve the resolution objectives, and especially the overarching objective of preserving financial stability, to the same extent as the Measures.”

“By letter dated [...], the [...] stated that the situation of the bank threatened financial stability and that an urgent intervention was therefore necessary to avoid a serious disturbance in the economy of [...]. The [...] pointed out that liquidation under ordinary insolvency would not be in the public interest as it would put financial stability at risk, interrupt the provision of critical functions, affect the protection of depositors and destroy value. Moreover, the [...] stated that in case of regular liquidation of the bank, the [...] Deposit Guarantee Scheme ("DGS") would be called on to immediately reimburse covered deposits. This would put significant additional stress on the banking system given the need to collect those amounts from the contributors to the DGS, the [...] banks.

“According to the [...] authorities it would not be possible to avoid a serious disturbance in the economy in the areas where [...] and [...] operate with a particular impact on interruption of SME's business activities and lending to households.”

69 The crisis rules require effective measures to limit distortions of competition.

The 2013 Banking Communication sets requirements intended to ensure that aid amounts are limited to the minimum necessary. These requirements include burden sharing from shareholders and holders of subordinated bonds, preventing outflows, and imposing restrictions on payments to shareholders and bondholders, as well as caps on remuneration. They also include bans on acquisition and price dumping, in order to limit distortions of competition. Our analysis of the decisions found that the

Member States made commitments to implement such measures. However, it was not always clear how these commitments were calibrated to the distortive effect of the specific measure⁷⁶. In the published decisions that we examined we did not find that the Commission had analysed the impact of measures on market structures and entry barriers as required by the 2013 Banking Communication⁷⁷. According to the Commission, such assessments are not required nor performed for other sectors.

70 The Restructuring Communication explicitly requires “that the notification of any restructuring plan should include a comparison with alternative options, including a break-up, or absorption by another bank, in order to allow the Commission to assess whether more market oriented, less costly or less distortive solutions are available consistent with maintaining financial stability”⁷⁸. In the sample, we found that the Commission did not verify that there were no less costly or less distortive alternatives to a measure. The Commission pointed out that, in line with case law, it cannot impose alternative measures on Member States, but it could only assess the compatibility of the proposed measure.

⁷⁶ Point 20 of the 2013 Banking Communication: “In any event, measures to limit distortions of competition should be calibrated in such a way so as to approximate as much as possible the market situation which would have materialised if the beneficiary of the aid had exited the market without aid.”

⁷⁷ Point 11 of the 2013 Banking Communication: “Furthermore, in its assessment of burden-sharing and measures to limit distortions of competition the Commission assesses the feasibility of the proposed measures, including divestments, and their impact on the market structure and entry barriers. At the same time, the Commission has to ensure that solutions devised in a particular case or Member State are coherent with the goal of preventing major asymmetries across Member States which could further fragment the single market and cause financial instability, impeding recovery within the Union.”

⁷⁸ Point 9 of the Restructuring Communication.

Conclusions and recommendations

71 The Commission had appropriate resources and tools to ensure effective State aid control. It has well-defined internal processes and procedures which promote the achievement of objectives and foster accountability. It has suitable organisational structures, with proper reporting lines which allow for appropriate information flow and adequate internal supervision by senior management (see paragraphs 31-32). It has a robust ethical framework, albeit with some weaknesses in relation to handling of market sensitive information and a comprehensive set of core principles that promote integrity and adherence to the highest professional standards (see paragraphs 33-34). The necessary human and IT resources were in place for efficient law enforcement (see paragraphs 35-36). The Commission has the necessary powers for effective State aid control and an appropriate procedural framework (see paragraphs 37-42). Thus, the Commission had all the necessary means to ensure its decisions were based on correct information.

72 We consider that the State aid rules were not fully fit for the purpose of controlling state aid to financial institutions in line with the objectives of the Treaty during the period of our audit (see paragraph 48). The State aid rules for the financial sector seek to ensure financial stability while keeping distortions of competition to a minimum. The crisis rules are generally well drafted and clear, although they do not define criteria for a serious disturbance (see paragraph 43). However, the crisis rules were not revised following improvements in the market circumstances during the audited period and the overhaul of the regulatory framework after the financial crisis, including the fact that the BRRD has restricted the possibilities to grant aid to banks without this resulting into resolution (see paragraphs 48-50).

Recommendation 1 – Carry out an evaluation whether the State aid rules continue to be appropriate and take corrective action where required

To ensure the EU State aid rules for the financial sector continue to be appropriate for market realities and the applicable regulatory framework, the Commission should:

- (1) carry out an evaluation of the current crisis rules (including the overall effect of the control of state aid on the competition in the EU banking markets) to decide on appropriate measures.

- (2) If the evaluation identified a need to revise the crisis rules, the Commission should among other things reflect on whether:
- (a) to set out assessment criteria for a “serious disturbance” regarding the application of Article 107(3)(b) TFEU;
 - (b) to incorporate the common assessment principles ;
 - (c) to adjust the conditions for the compatibility of precautionary measures and aid in resolution; and
 - (d) to further specify the level of detail for information to be submitted.

Timeframe: 2023 (for the evaluation)

73 The Commission managed State aid procedures largely in line with its (non-binding) internal processes. The Commission’s exercise of State aid control adhered to the structures, reporting lines, and authorities and responsibilities established for this purpose (see paragraph 52). The College took its decisions after other DGs had had an opportunity to raise concerns (see paragraphs 53-54). The Commission’s case-handling activities mostly adhered to internal processes (see paragraph 55). Document management largely complied with the Commission’s standards (see paragraphs 56-57). However, State aid procedures were lengthy and were not always fully transparent, partly due to an extensive use of informal pre-notification contacts by Member States before they notify (see paragraphs 58-59). The publication of decisions was often delayed due to the discussions with Member States concerning the right to conceal confidential information in the public version of the decisions (see paragraphs 60-61).

Recommendation 2 – Further enhance compliance with internal processes and best practices

In order to increase efficiency, accountability and transparency, the Commission should:

- (1) improve its document management and ensure all relevant documents are registered;
- (2) encourage Member States that pre-notifications contacts should not exceed the Best Practices Code’s indicative time limit of 6 months and should be based on written draft notifications; and

- (3) enhance the cooperation with Member States in order to speed up the publication of the non-confidential versions of decisions and ensure consistent approach regarding what information is not disclosed.

Timeframe: 2022

74 State aid decisions need to be based on legally and economically sound assessments (see paragraph 64). The Commission analysed restructuring plans rigorously (see paragraph 65), but did not contest Member States' assessments of whether a serious disturbance including threats to financial stability existed in each individual case (see paragraphs 66-67). The Commission imposed measures intended to limit distortions of competition but did not analyse the actual impacts of each measure on competition (see paragraph 69). Performance indicators were not entirely fit for purpose as they reflected external factors beyond the control of the Commission and did not always reflect the Commission's activities (see paragraphs 23-24). Nor had the Commission formally evaluated how well its sectoral State aid rules had worked, or whether it should change or simply discontinue its approach (see paragraphs 28-30).

Recommendation 3 – Improve performance measurement

In order to demonstrate the effect of the State aid control and to enhance its transparency and accountability towards the European Parliament and EU citizens, the Commission should:

- (1) define suitable and relevant indicators for the control of State aid to financial institutions, which reflect the results of DG COMP's activities, in order to effectively monitor progress towards objectives in the context of its annual reporting; and monitor the suitability of the indicator(s).

Timeframe: 2022

This Report was adopted by Chamber IV, headed by Mr Alex Brenninkmeijer, Member of the Court of Auditors, in Luxembourg at its meeting of 28 July 2020.

For the Court of Auditors

Klaus-Heiner Lehne
President

Glossary

Bail-in: Means of averting bank failure whereby a bank recapitalises through existing shareholders (rather than being rescued with public money).

Banking union: One of the building blocks for completing Economic and Monetary Union, which consists of an integrated financial framework with a single supervisory mechanism, a single bank resolution mechanism and a single rulebook.

Banking Recovery and Resolution Directive (BRRD): Directive laying down rules and procedures for the recovery and resolution of various types of financial institutions.

Better Regulation: A concept that guides EU policy and law-making, based on the principles that regulation should achieve its objectives at minimum cost and be designed in a transparent, evidence-based manner with citizen and stakeholder involvement.

Chief Economist Team: Team within the Commission's Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs that develops, coordinates and produces economic analysis to ensure that the directorate-general's initiatives are based on sound economic evidence.

de Larosière Report: A February 2009 report that called for an overhaul of Europe's system of financial regulation.

Insider trading: Buying or selling shares with a view to making a profit or minimising a loss with the benefit of information that, if generally known, would affect their value.

Non-performing loan (NPL): A loan on which payments have been overdue for a specified time span (usually 90 days), or where there is evidence that full repayment is unlikely.

Resolution: The orderly winding-up of a failing financial institution to ensure the continuity of its essential functions, preserve financial stability, and protect public funds by minimising the need for public financial support.

Resolution fund: A fund set up to help finance the orderly resolution of failing financial institutions.

Single Resolution Board: Central resolution authority within the banking union, tasked with ensuring the orderly resolution of failing financial institutions at minimal cost to taxpayers and the rest of the economy.

Single resolution mechanism: Mechanism under which the Single Resolution Board and national resolution authorities have centralised power of resolution, being directly responsible for the resolution of all financial institutions in Member States participating in the banking union.

Single rulebook: Set of legislative texts that all financial institutions in the EU must comply with.

Single supervisory mechanism: The EU's system for supervising financial institutions, comprising the ECB and the national supervisory authorities of participating countries.

Sovereign bond: Debt security issued by a government to support government spending.

State aid: Direct or indirect government support to a business or an organisation, putting it at an advantage over its competitors.

List of abbreviations

AAR: Annual Activity Report

BRRD: Banking Recovery and Resolution Directive

CET: Chief Economist Team

DG COMP: Directorate-General for Competition

DG FISMA: Directorate-General for Financial Stability, Financial Services and Capital Markets Union

EBA: European Banking Authority

ECB: European Central Bank

ECOFIN: Economic and Financial Affairs Council

EP: European Parliament

ESAs: European Supervisory Authorities

ESRB: European Systemic Risk Board

ISC: Inter service consultation

NPL: Non-performing loan

SRB: Single Resolution Board

SRM: Single resolution mechanism

SSM: Single supervisory mechanism

TFEU: Treaty on the Functioning of the European Union

FINAL REPLIES OF THE EUROPEAN COMMISSION TO THE EUROPEAN COURT OF AUDITORS SPECIAL REPORT

“CONTROL OF STATE AID TO FINANCIAL INSTITUTIONS IN THE EU: IN NEED OF A FITNESS CHECK”

EXECUTIVE SUMMARY

Common Commission reply to paragraphs I-X.

Since 2008, the European Commission has applied State aid rules under the Treaty to the financial sector on the basis of specific guidelines. The Commission adopted over 500 decisions during the last decade based on these guidelines.

During the audited period (2013-2018), and together with the implementation of the EU resolution framework since 2015, the uniform application of the State aid control exercised by the Commission in the financial sector has contributed to safeguarding the Union’s financial stability by preventing the disorderly failure of otherwise viable banks and by facilitating the orderly market exit of unviable entities. It has contributed to making the EU banking sector more robust through the cleaning-up of banks’ balance sheets, the instigation of deep restructuring, and the market exit of the least efficient players. It has also preserved fair competition by requiring aided banks to implement measures to mitigate competition distortions. Finally, it has required private loss-sharing by the aided banks’ shareholders and subordinated creditors. The Commission considers that it has used its resources and tools efficiently and to the effect in line with its rules and procedures.

As the European Court of Auditors (“the ECA”) recognises, the Treaty confers a wide margin of discretion on the Commission to interpret the criteria based on which it can find State aid measures compatible. To this end, the Commission has to carefully consider various economic and legal elements before concluding that a specific situation justifies State aid to a specific beneficiary. Finding the balance whether the aid is justified to achieve an objective of common European interest, including remedying a serious disturbance in the economy, is an assessment that the Treaty has entrusted to the Commission.

In exercising that assessment, the Commission in 2013 revised its guidelines setting out the criteria for compatible aid to financial institutions impacted by the effects of the crisis. It has done so after consultations with stakeholders, including with Member States as the grantors of aid. These criteria remain valid until today, as effects of the crisis continue to persist in the banking sector across the EU. Economic recovery had been weak in a number of Member States and the situation of the banking sector had not returned to the situation before 2008. Furthermore, certain Member States were until recently part of economic adjustment programmes.

In 2014, a new EU banking regulatory framework was introduced, notably the Bank Recovery and Resolution Directive (BRRD)¹, the Single Resolution Mechanism Regulation (SRMR)², and the Deposit Guarantee Scheme Directive (DGSD)³.

In this new regulatory setting, newly created actors have taken up their responsibilities in the Banking Union, namely the European Central Bank (ECB) as the central supervisor of banks within the Single Supervisory Mechanism (SSM) and the Single Resolution Board (SRB) in its role in the Single

¹ OJ L 173, 12.6.2014, p. 190–348

² OJ L 225, 30.7.2014, p. 1–90

³ OJ L 173, 12.6.2014, p. 149–178

Resolution Mechanism (SRM)⁴. It should be noted that whilst a lot of progress has been made since 2015, the implementation of the BRRD is still ongoing⁵, e.g. with respect to the build-up of bail-inable instruments. In addition, still today, there are pockets of vulnerabilities in parts of the European banking sector, e.g. due to high levels of non-performing loans and low profitability in the sector.

Any plans to grant State aid have to be submitted to the Commission by Member States. Likewise, where the SRB intends to use the Single Resolution Fund, the SRMR⁶ requires that the SRB submits its proposal to grant Fund aid to the Commission for approval. The Commission's role as competition enforcer in essence consists of assessing whether the positive effects of the aid outweigh the negative effects on competition. The Commission makes this assessment *ex ante*, i.e. when the aid proposal is notified prior to its implementation by the Member State concerned. This implies that the performance of financial institutions *ex post*, i.e. after having received State aid, cannot be solely attributed to the Commission as other actors and other factors play an important role as well, which makes it difficult to define performance indicators that reflect the contribution of State aid control in an unequivocal manner. Member States may decide to grant State aid to help prevent or mitigate possible adverse consequences of distressed or failing banks in full compliance with the EU resolution framework.

By minimising competition distortions when public support is provided, the financial sector State aid guidelines safeguard the level playing field, irrespective of whether Member States participate in the Banking Union or not. In the new regulatory setting, the co-legislators have entrusted important responsibilities to other actors, for example the day-to-day supervision of banks, the setting of capital requirements, the running of stress tests and asset quality reviews, the decision whether a bank is 'failing or likely to fail', whether a bank is put into resolution or not. And not least, the decision to grant aid and to design an aid measure is the responsibility of the Member State. The Commission's role was and is limited to assessing the compatibility of the notified State aid measure with the internal market.

The Commission considers that the State aid rules specifically designed to address the effects of the financial crisis on banks were still in line with market realities during the period covered by the audit. It is important for the Commission to apply the same rules to all Member States. For these reasons, the Commission has found it premature to launch a formal evaluation of the State aid guidelines for the financial sector. This continues to be the case for the near term as the economic effects of the ongoing COVID-19 crisis, including on banks, clearly constitute a serious disturbance in the economies of Member States.

State aid rules should reflect market realities and at the same time provide a stable guide for market participants as to the exercise of State aid control. When necessary, the Commission will adjust its State aid rules rapidly in order to reflect dramatic changes in the economic environment, as it has just done in response to the COVID-19 outbreak. The Temporary Framework for the real economy was adopted quickly and entered into force already on 19 March 2020. Among other measures, this Framework enables Member States to channel aid to the real economy through banks. In the first three months after the entry into force of this Temporary Framework, the Commission already adopted more than 160 decisions⁷ approving over 200 national measures notified by all 27 Member States and the UK. On this basis, Member States are able to grant an estimated EUR 2.2 trillion in aid to help companies deal with the impact of COVID-19 on their business. In this way, State aid control

⁴ In addition, the Commission endorses and gives legal effect to the SRB's resolution schemes for banks, in cases where the SRB determines that the resolution of a failing bank is in the public interest.

⁵ See report from the Commission to the European Parliament and the Council on the application and review of Directive 2014/59/EU (Bank Recovery and Resolution Directive) and Regulation 806/2014 (Single Resolution Mechanism Regulation), COM(2019) 213 final, 30.4.2019. On line available on: https://ec.europa.eu/info/sites/info/files/business_economy_euro/banking_and_finance/documents/190430-report-bank-recovery-resolution_en.pdf

⁶ In particular, its Article 19.

⁷ A list of all State aid decisions adopted regarding COVID-19 measures can be found here: https://ec.europa.eu/competition/state_aid/what_is_new/covid_19.html

contributes significantly to the EU's overall efforts to mitigate the economic effects of the COVID-19 outbreak and to enable a strong recovery, while safeguarding the level playing field.

With regard to the State aid rules for the financial sector, the Commission has applied its common rules consistently to the specific circumstances of about 200 cases throughout the audited period. The Commission's interventions, at times taken under immense time pressure to preserve depositor confidence and financial stability, have greatly contributed to maintaining a level playing field in the EU financial sector and limiting competition distortions. In the individual decisions it has taken, the Commission, based on the balanced criteria as expressed in the guidelines, has verified each time whether the conditions for the approval of State aid proposed by the Member State were fulfilled, and whether the State aid measures it assessed were necessary and the amount of aid was limited to the minimum necessary to achieve the common interest objectives at issue. It is evident from every State aid decision that the Commission has taken into account the new regulatory environment in its State aid assessments, whenever it was legally required to do so.

The Commission's State aid decisions are subject to a series of checks and balances, internal and external. Most notably, the substantial review of the compatibility of the Commission's application of the State aid rules with the Treaty is the exclusive competence of the Court of Justice of the European Union as provided in Article 263 and Article 267 TFEU. In exercising that power, it is for the Court of Justice of the European Union to judge the legal reasoning, the procedures and the facts that underpin action by the Commission.

Against the above background, in response to the ECA's recommendations, the Commission:

- accepts the recommendation to evaluate the State aid rules for banks in line with its Better Regulation guidelines. The economic impact of the crisis created by the COVID-19 outbreak constitutes a serious disturbance in the economy of Member States and there is high uncertainty on the economic outlook. Therefore, the Commission will conduct an evaluation when the economy has recovered and at the latest in 2023;
- accepts the recommendation to further increase the efficiency of internal processes and where applicable the Commission will remind Member States to respect best practices;
- accepts the recommendation to define suitable and relevant performance indicators, which can be included in its annual Management Plan to reflect the results of DG Competition's activities and to monitor their suitability.

INTRODUCTION

Common Commission reply to paragraphs 01-16.

State aid is an objective notion defined by the Treaty, which is for the Court of Justice of the European Union to interpret and by which the Commission is bound.⁸ On the other hand, the Treaty confers the assessment of the compatibility with the internal market of a State aid measure proposed by a Member State on the Commission as its exclusive competence. For this assessment, the Commission performs a "balancing test", weighing the positive effects of a measure against its negative effects on trade and competition in the common market.

The general principles of this balancing test are detailed, with considerations of the sectoral context, in a number of guidelines for particular aid categories. By assessing an aid measure under the (in view of the objective of the aid) relevant guidelines, the Commission therefore applies the balancing test in

⁸ The Commission has laid out its understanding of the case law by the EU Courts in the Notice on the Notion of Aid. OJ C 262, 19.7.2016, p. 1–50

each case. The Commission recalls in this context that if a given aid measure, by nature of its objective, falls within the scope of existing guidelines and therefore has to be assessed under these guidelines, only the assessment criteria as formulated in those guidelines apply.

For State aid to banks, the Commission most recently reflected the principles of the balancing test in the 2013 Banking Communication. These guidelines, as they are intended to address very divergent situations, set out principles, which the Commission consistently applies across all Member States, while taking into consideration the relevant specificities of the case. The compatibility assessment criteria can be grouped in three “key pillars”:

- 1) The minimisation of distortions of competition following the granting of aid to preserve fair competition to a maximum extent (e.g. by limiting the growth of the balance sheet of aided banks, requiring the sale of certain activities or assets, or prohibiting aggressive commercial practices);
- 2) Burden-sharing to limit the amount of State aid needed, thereby reducing moral hazard (e.g. through loss participation by bank shareholders and subordinated creditors, but also divestments and remuneration or pricing requirements) and incidentally also reducing the burden to taxpayers;
- 3) The demonstration of the banks’ long-term viability, taking into account the measures required under the other two pillars. If viability cannot be demonstrated, the bank should exit the market in an orderly manner.

The Commission’s compatibility assessments are always *ex ante* assessments, based on the facts available to the Commission at the time of the assessment of the notified measure.

State aid rules applicable to the banking sector make a distinction between three types of aid:

- 1) ‘Liquidity aid’ to address temporary liquidity concerns of otherwise solvent entities;
- 2) ‘Restructuring aid’ to help entities in distress restore their long-term viability and thus support them in preserving their economic activity;
- 3) ‘Liquidation aid’ to support the orderly market exit of entities in distress for which long-term viability cannot be restored.

After their respective entry into force, the new EU regulatory framework for bank resolution and the specific State aid rules for the banking sector have been consistently applied without discrimination by the Commission. In line with jurisprudence of the General Court and the Court of Justice of the European Union, where provisions of the EU bank resolution rules are so intrinsically-linked to the object of the aid that they cannot be assessed separately, the Commission has made an assessment of those provisions in the respective State aid decision. Furthermore, as the EU bank resolution rules as well as capital regulations are implemented by other authorities, the Commission works in close cooperation with the ECB, the SRB and national supervisory and resolution authorities.⁹ While each of these actors operate within their own mandate, they all share the objective to secure a sound and stable financial sector. The Commission regularly interacts and coordinates with supervisory and resolution authorities at EU and national level, to address complex and urgent situations and avoid the disorderly failure of banks entailing risks to financial stability. However, there is a division of roles and responsibilities in the new regulatory environment that should be taken into account when discussing State aid control in the banking sector.

In particular, it is either for the ECB or the national supervisor to declare a bank failing or likely to fail. Following this declaration, the responsible resolution authority (in the Banking Union this is the

⁹ The ESRB has a different objective and mandate, which the Commission considers not to be relevant for the specific purpose of assessing the compatibility of State aid under Article 107(3) TFEU.

SRB for significant institutions¹⁰) has to decide whether it is in the public interest to put the bank into resolution, or whether a bank could be wound down under national insolvency law. If the SRB or the national resolution authority considers that resolution action would not be in the public interest, EU law stipulates that the bank is wound down in line with national insolvency law. The Commission becomes involved in its role as competition enforcer when the resolution of a bank entails the use of e.g. the Single Resolution Fund¹¹ or alternatively, when in a national insolvency proceeding the Member State considers it necessary to grant State aid¹². In both types of situations, the aid measures have to be notified to the Commission for assessment under EU State aid rules.

The Commission has been applying Article 107(3)(b) TFEU as the legal basis for its State aid decisions concerning banks since 2008.¹³ This legal basis remains a valid justification, as there is still evidence showing that the financial sector has not completed its adjustment cycle from the crisis, that pockets of vulnerability are still present, and that new risks for the sector have emerged.

OBSERVATIONS

Common Commission reply to paragraphs 21-25 (Objective setting and performance measurement)

Each Commission service produces an annual Management Plan for the year ahead, which reflects the activities of the service and how they contribute to meeting the objectives of the Commission set out in the service's strategic plan. The performance indicators serve to monitor progress towards objectives in the context of its annual reporting. The Commission points out that it always seeks to have the best possible performance indicators within the existing constraints, such as the availability of the most recent reliable and consistent data, commonly recognised methodologies and well-established unique causal relationships to base the indicators on. The Commission is open to improve its performance measurement, but result indicators should be suitable for the purpose of an annual Management Plan. Therefore, it sees many challenges to measuring in a simple, operational manner with an unambiguous causal direction, annual performance results on broad phenomena, like the "*integrity of the internal market in general*" highlighted by the ECA.

In this light, the Commission does not consider that the success of bank restructurings could be summarised in a simple, suitable indicator for annual Management Reports of the Commission services. The Commission, in its role as State aid enforcer, necessarily assesses viability and the related commitments by the Member State from an *ex-ante* perspective. The Commission is also kept informed about the implementation of specific commitments that the Member State may have provided through dedicated monitoring reports by the independent trustees that it appoints. However, legally monitorable commitments that relate to specific actions are different from the many factors that can influence the success of a five-year restructuring period, in particular macro-economic or business developments that are not covered by the commitments. The Commission does not take control of aided undertakings, and the implementation of commitments remains the responsibility of the Member State. Neither does the Commission act as a supervisor and hence cannot monitor the banks' day-to-day performance or the broader market developments.

In the audited period, the Commission has approved individual restructuring aid in over 25 cases and only very few received repeated capital support. According to the ECA, several banks in their sample

¹⁰ Outside the Banking Union and for less significant institutions inside the Banking Union, this decision is taken by national resolution authorities.

¹¹ Before the Single Resolution Fund (or national resolution funds) can be used, the EU resolution framework requires that the bank's losses will have to be covered by the bail-in of shareholders and creditors and where necessary also of senior debt.

¹² Where aid is granted by Member States in national insolvency proceedings the burden sharing requirements apply, i.e. shareholders and holders of subordinated instruments have to contribute in full to the cost of the measures but depositors and senior creditors are not required to contribute.

¹³ In March 2020, in view of the current COVID-19 outbreak, the Commission has adopted a Temporary Framework under the same legal basis (OJ C 91I, 20.3.2020, p. 1–9).

that had received such aid later required additional government interventions after having been found viable by the Commission. Without going into the details of individual cases, it is worth pointing out that each case presents a complex assessment in very different circumstances.¹⁴ In addition, for a sample of 175 banks the Commission services have assessed the return to viability of aided banks by comparing them to non-aided banks. The findings which were published in 2015 show that, on average, the performance¹⁵ of restructured banks converges towards the values of banks that did not receive aid albeit only at the end of the restructuring period.¹⁶ For these reasons, additional government interventions at a later stage should not be interpreted as contradicting the viability assessment that the Commission performed *ex ante*.

Common Commission reply to paragraph 26-27 (Risk assessment)

The Commission points out that the risk identification and selection process in place in DG Competition is sector-neutral, and highlights both significant actionable risks, where mitigating action is necessary, and accepted risks, where mitigating actions are already in place in line with the Commission internal guidelines that apply to all its services.

To ensure effective competition enforcement in the EU, the Commission regularly maintains its legal instruments aligned with market realities and contemporary economic and legal thinking, by evaluating and reviewing them. It does this, either as foreseen in the legal instrument or framework itself, or alternatively, by assessing on the basis of its market knowledge and stakeholder interaction, and today in the context of the Better Regulation framework, when to launch an evaluation and possibly a review of the rules, unless an exemption applies. Therefore, maintaining legal instruments aligned with market realities and contemporary economic and legal thinking applies as a general principle, sector-specific policy guidance like in the area of State aid to financial institutions, has not been specifically identified as a significant risk. Nevertheless, market developments are constantly observed. It must also be borne in mind that competition rules, in particular guidelines, provide stability and legal certainty for market participants and Member States, and therefore changes to the rules must be carefully considered.

As already outlined, the Commission has a comprehensive policy framework for State aid in the financial sector in place, which it has applied consistently. Therefore, DG Competition has had no reason to deviate from its sector-neutral approach and qualify this sector/instrument, differently from other sectors/instruments, as a significant risk with a potential to risk the attainment of the DG's objectives.

Common Commission reply to paragraphs 28-30 (Impact assessment and evaluation)

The Better Regulation framework is an important tool in the Commission's policy development. It came into force in 2015, after the adoption of the Banking Communication in 2013. Nonetheless, in 2013 the Commission had already gained significant experience in the application of State aid rules specific to the financial sector, and against that it carefully assessed the relevant factors, which were consulted with all Member States and other stakeholders. The Commission furthermore notes that the

¹⁴ Where the Member State argued that further government intervention was necessary, many factors can play a role. In some cases, the initial aid was provided during a macroeconomic adjustment programme, in a situation of high volatility. In others, repeated aid was provided prior to 2013 or repaid before a subsequent intervention. In a number of cases, repeated capital support resulted in market exit of the banks in question, which is an important outcome from a competition perspective. From a competition perspective, it makes indeed a difference whether banks receive capital support for restructuring or as liquidation aid. It also makes a difference whether banks receive capital support or liquidity support (in form of guarantees on senior funding). Whether NPL levels or sovereign exposure affect the success of restructurings, is not possible to determine without looking at the individual case.

¹⁵ Measured using operational and risk indicators, profitability, and funding and solvency positions.

¹⁶ European Commission: Competition State aid Brief (2015/1): State aid to European banks: returning to viability, available at: https://ec.europa.eu/competition/publications/csb/csb2015_001_en.pdf

Better Regulation Guidelines do not prescribe the specific point in time when policies should be evaluated, but describe how to carry out an evaluation when there has been a political decision to launch the evaluation on certain policies or if the policy legislation stipulates provisions to carry out evaluations.

In any event, the Commission considers that its rules applicable to the compatibility assessment of State aid in the financial sector are – and have been throughout the audited period – adequate and fit for purpose. As already clarified, there was no requirement to formally evaluate the 2013 Banking Communication during the audited period and the Commission considers that the rules were aligned to market realities while also providing a stable and proven guide to all Member States and market participants.

Commission reply to paragraph 32 (Management structures)

The Commission positively notes the ECA's assessment that DG Competition's management structures were adequate. The Chief Economist and its team in DG Competition make important contributions to the State aid control of the Commission, and these contributions are taken into account by DG Competition in the preparation of its decisions in this field.

Common Commission reply to paragraphs 33-34 (Ethical framework)

The Commission welcomes the general recognition of a strong ethical framework and considers that its rules are well suited also to staff dealing with market-sensitive information. The Commission points out that Articles 11 to 26(a) of its Staff Regulations constitute the ethical framework set by the co-legislators for the staff of the European institutions. On that basis, the institutions adopt more detailed rules for their staff. Based on the risk assessment carried out in DG Competition, obliging the staff to seek prior clearance for certain private financial transactions would be a disproportionate control, also in view of the processing of (sensitive) personal data according to Article 4 (1)(c) of Regulation 2018/1725, which states that the processing of personal data must be adequate, relevant and limited to what is necessary in relation to the purposes for which they are processed ("data minimisation").

Furthermore, the Commission notes that in a recent prior audit concerning the EU institutions' ethical framework the ECA made positive remarks about DG Competition's guidance and procedures concerning ethics.¹⁷

The Commission finally points out that in the banking cases (or more generally) no instances of wrongdoing have been reported by the competent authorities that are designated in the EU for this purpose.

Common Commission reply to paragraphs 35-36 (Human and IT resources)

The Commission welcomes the ECA's conclusion about the quality of the Commission's staff working in the area that has been the subject-matter of the audit. The Commission recalls that – thanks to the mitigating measures it took – DG Competition at all times had (and has) highly qualified and capable staff to perform its tasks.

Common Commission reply to paragraphs 38-42 (Procedural framework for State aid control)

The Commission and its services exercise State aid control according to the mandate from the Treaty and with the help of formal and informal processes. The formal procedures are laid down in Council

¹⁷ See points 37 and 71 of ECA Special Report 13/2019 - The ethical frameworks of the audited EU institutions: scope for improvement. On line available on:
https://www.eca.europa.eu/Lists/ECADocuments/SR19_13/SR_ethical_frameworks_EN.pdf

Regulations,¹⁸ while the Commission and Member States as the grantors of aid have also recognised best practices on informal cooperation, which are laid down in the Best Practices Code¹⁹ in a transparent manner. Such informal cooperation, called the pre-notification phase, offers the possibility for Member States to consult the Commission on planned measures on an informal and non-binding basis. The length and depth of such informal exchanges depend on how advanced a Member State's plan is. Naturally, a more vague idea for a potential measure usually entails more exchanges until the Commission is able to get the adequate level of detail needed to provide meaningful feedback to the Member State. Indeed, the results of the public consultation carried out in the context of the 2018 revision of the Best Practices Code – which is not specific to any sector – show that an extended pre-notification phase was perceived positively by most respondents and indeed constitutes best practice. Furthermore, the Commission cannot refuse to enter into such informal discussions with Member States even if the latter choose not to follow the best practices indicated in the Best Practices Code. Finally, since even in case of such informal pre-notification contacts, any Commission decision regarding an aid measure may only be made after a formal notification, the procedural rights of third parties stipulated in the Procedural Regulation²⁰ are safeguarded in the same way as in a State aid procedure without this informal pre-notification phase. In this context, the Commission points out that the General Court of the European Union has found that merely the length of the pre-notification contacts cannot be regarded as an indicator of doubts about compatibility.

Common Commission reply to paragraphs 43-50 (State aid rules)

The Commission affirms that the development of guidelines for the compatibility assessment of State aid in a particular sector falls within its exclusive State aid control competence as laid down in the Treaty. The choice of legal basis is part of exercising this competence, and the Commission considers that Article 107(3)(b) TFEU has remained the appropriate legal basis to assess the compatibility of aid measures for financial institutions during the audited period. Indeed, today this is particularly valid, as the COVID-19 outbreak is a major shock to the EU economies.

In particular, the Commission considers that its decisions (i) to maintain Article 107(3)(b) TFEU as legal basis for State aid to banks over the audited period, and (ii) to not yet review the 2013 Banking Communication, were appropriate in light of the following considerations:

- Non-negligible weaknesses in the economies persisted during the audited period and remain, even if these may not affect all Member States equally²¹. For example, the negative fall-out of the crisis (e.g. in the form of large stocks of non-performing loans) is still present in several Member States. It must be noted that these legacy issues having been posing a threat to the viability of banks. The Commission considers that where Member States decide that aid measures are necessary to deal with such issues they are still a consequence of the crisis. Therefore the Commission considers that the assessment it made in 2013 on the general application of Article 107(3)(b) TFEU when adopting its guidelines and which is summarised in point 6 of the 2013 Banking Communication has remained valid. Moreover, applying the same principles of the 2013 Banking Communication has ensured equal treatment among all Member States. Of course, the regulatory framework on resolution has been applicable since its entry into force.
- An evaluation, and possible review, of the 2013 Banking Communication would benefit from the experience of how failing banks are dealt with under the resolution framework. It should be noted

¹⁸ In particular, the “Procedural Regulation” (Council Regulation (EU) 2015/1589 of 13 July 2015 laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union, OJ L 248, 24.9.2015, p. 9) and the “Implementing Regulation” (Commission Regulation (EU) 2015/2282 of 27 November 2015 amending Regulation (EC) No 794/2004 as regards the notification forms and information sheets, OJ L 325, 10.12.2015, p. 1–180).

¹⁹ Commission Notice on a Best Practices Code on the conduct of State aid control proceedings, OJ C 253, 19.7.2018, p.14-27

²⁰ See footnote 18

²¹ See for instance Section 4.1 of the 2020 European Semester. On line available on: <https://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1584543632863&uri=CELEX%3A52020DC0150>

that the EU's resolution framework and in particular the SRB became fully operational in 2016 but so far, there have been only few cases.²²

State aid rules and the bank resolution framework apply in parallel. State aid control is an exclusive competence conferred upon the Commission by the Treaty, on which the adoption of secondary legislation in the domain of prudential requirements and resolution has no direct bearing. Also, the Commission cannot use its competences in State aid control to enforce other provisions in Union law, except where such provisions apply and are intrinsically-linked to the compatibility of a concrete aid measure. The text of the BRRD makes direct reference to the EU State aid framework, and it is clear from the text of the BRRD that the co-legislators recognised the applicability of the State aid framework (and the 2013 Banking Communication), while setting themselves conditions in the BRRD on the use of extraordinary public support in exceptional cases (e.g for precautionary recapitalisation and government financial stabilisation tools) within the new resolution framework. Furthermore, the BRRD does not preclude aid from resolution financing arrangements in resolution or State aid outside of resolution (e.g. under national insolvency proceedings). The type of procedure followed (i.e. resolution or national insolvency proceedings) is ultimately the responsibility of supervisory and resolution authorities, while of course the competition competences of the Commission remain important.

In general, the 2013 Banking Communication distinguishes between banks for which a return to viability can be demonstrated and those for which it cannot and which – from a competition perspective – should exit the market. In the State aid rules, it is therefore important to separate the concepts of “restructuring aid” (for banks which are viable in the long-term) and “liquidation aid” (to facilitate the orderly market exit of banks that are not viable in the long-term). As regards the possibility to grant aid to facilitate the market exit of a bank, the relevant provisions of the 2013 Banking Communication focus on mitigating competition distortions. The provisions for liquidation aid to be compatible in terms of competition rules do not depend on any particular legal regime and therefore apply both in resolution, when publicly managed funds are used, and outside resolution (i.e. in national insolvency proceedings).

In response to the observation that the stricter bail-in requirements of the BRRD were not reflected in State aid rules, it is important to note that in the State aid decisions adopted during the audit period, the Commission has assessed the intrinsically-linked provisions of the BRRD as part of the compatibility assessment. This would also include the bail-in requirement in cases where the Single Resolution Fund or national resolution funds would intervene²³.

Common Commission reply to paragraphs 52-63 (Adherence to internal processes and procedures)

The inter-service consultation is an important element of the Commission's decision-making. While DG Competition prepares the draft for the decision (which is an internal draft document and hence work in progress), the inter-service consultation ensures the involvement of other Commission services with regard to their respective fields of responsibility. According to the Commission's internal procedural rules, a positive opinion with comments by another service means agreement subject to the comments being taken into account. The lead service (i.c. DG Competition) then revises the draft decision by addressing the comments provided and the decision is presented to the Commission only after an agreement with the commenting services has been reached. Against this background, the Commission notes that the comments mentioned in paragraph 54 were few and of course very specific to the context of the respective cases. In any case, Commission services making constructive comments to one another is a normal part of the Commission's decision-making and these comments are then properly addressed in this process. In each of the audited cases, the final draft of the State aid decision was agreed with the services consulted, so that it could be submitted to the College of Commissioners for formal adoption.

²² For more details see footnote 4

²³ The Commission notes that to date there have been no cases where this requirement had to be checked.

Concerning the registration of documents, the Commission's document management policy provides that those documents that are relevant for the decision-making process have to be registered. This registration is done in one of the document management systems of DG Competition. The Commission considers that no relevant documents were missing on a systematic basis and that the ongoing upgrade of DG Competition's case registration infrastructure will facilitate the compliance with the internal guidance in this area.

DG Competition's Manual of Procedures contains non-binding guidance that sets out the principles of the working arrangements internally for its staff. As already outlined above, the Best Practices Code sets out non-binding best practices on informal cooperation with Member States. While it would indeed be best practice if Member States were to submit a draft notification in the informal pre-notification phase, the Commission cannot refuse discussions with a Member State if this is not done. This is particularly so in banking cases, where informal contacts can be useful even if measures are still at a tentative, early planning stage. It does not need further explanation that this should happen under strict confidentiality. However, if Member States choose not to apply these non-binding best practices, this does not constitute a breach of the procedural rules on DG Competition's part.

The Commission would like to qualify the statement in paragraph 60 that "*some relevant information was not published*". The Commission must reconcile two obligations, namely the requirement to state the reasons for its decisions under Article 296 TFEU and therefore ensure that its decisions contain all the essential elements on which they are based, and that of safeguarding the obligation of professional secrecy.²⁴ This implies that there can be information relevant for the Commission's assessment, which cannot be disclosed in full to the public. This notwithstanding, the process of agreeing with Member States on the confidential information can sometimes be challenging, in the Commission's experience.

The Commission points out that there is no legal obligation for it to publish results of the monitoring of the specific committed actions. The commitments form part of the notification by the Member State and are assessed and published as part of the decisions. The subsequent monitoring of the commitments, normally with the support of an independent trustee, however, serves as a source of confidential information for the Commission. If a breach of commitments requires the Commission to take further action, its decision will become public. Alternatively, if there are no such breaches, the Commission notes that the information obtained through the monitoring is protected by confidentiality.

Similarly, a Member State is always able to propose a subsequent change to the commitments it had submitted to allow the Commission to perform the balancing test for an aid measure. The Commission will then assess whether the proposed change in the commitments leaves the balance of the original decision unaltered, and adopt and publish a motivated decision to this effect. The Commission does not share the ECA's view expressed in paragraph 63. It considers that the Commission's decisions adequately explained why the change in commitments does not alter the balance of the original decision.

Common Commission reply to paragraphs 64-70 (State aid decisions for financial institutions on substance)

The Commission considers that it has always verified the existence of a serious disturbance. Through the adoption of guidelines (i.e. the 2013 Banking Communication), the Commission has bound itself to assessing State aid to support banks under Article 107(3)(b) TFEU, in light of the crisis situation and the risk for financial stability at large which amount to a serious disturbance in the economy. As regards the application of these guidelines in a given case, the Commission points out that the Member States' authorities are responsible to decide whether they wish to grant aid to prevent an uncontrolled market exit of a particular bank that would threaten financial stability. Where a Member

²⁴ Point 18 of Commission communication C(2003) 4582 of 1 December 2003 on professional secrecy in State aid decisions, OJ C 297, 9.12.2003, p. 6–9

State decides that such aid should be granted, it notifies the planned aid to the Commission, and it is then the Commission's responsibility to assess the compatibility of that aid with the internal market. The Commission notes that it is the Member State concerned that has to demonstrate that aid was necessary because of a threat to financial stability in the absence of State aid. In this context, the Commission assessed whether the arguments brought forward by the national authorities were sound or, wherever applicable and necessary, if additional evidence was needed. In addition, the Commission considers that the consequences of the crisis persist at least in parts of the banking sector in the EU and therefore continued to apply the same set of rules in all Member States. In this context, the Commission highlights the duty of loyal cooperation of the Member State concerned in accordance with Article 4(3) TEU. The Commission also notes that none of its decisions has been appealed on these grounds.

Against the above background, the Commission confirms that it took into account the Member State's submissions in the assessment of the serious disturbance in each individual case. It combined this with the Commission's knowledge of the general economic situation in the Member State concerned which does not have to be registered in the case file.²⁵ Furthermore, the Commission points out that the Council has acknowledged the existence of risks to financial stability whenever approving (or amending) an economic adjustment programme (e.g. for Greece).

Specifically with respect to liquidation aid, the Commission notes that the ECA recognises that the disorderly failure of even a small bank can pose a risk to financial stability. For the notified liquidation aid measures, the Commission had found the evidence provided by Member States sufficient. Where relevant, this evidence was combined with the Commission's knowledge of the general economic situation in the Member State concerned. The Commission acknowledges that the 2013 Banking Communication does not describe the evidence that must be submitted by the Member States when they plan to grant liquidation aid. However, the Commission considers it was not necessary to include such detailed prescriptions in its guidelines. Indeed, the Procedural Regulation is a sufficient basis for the Commission to request any further information it needs from Member States to perform its compatibility assessment. The Commission has explained above that it assesses whether the arguments put forward by the national authorities are sound and if need be asks such further evidence.

Commitments are proposed by the Member States, and they respond to the specific circumstances of the case. They are assessed in the State aid decisions as part of the balancing test in order to ensure that undue distortions to competition stemming from the proposed aid measure are mitigated. A number of commitments are binary (e.g. a dividend ban or acquisition ban either apply or not). Others commitments (like divestments or the exit from business lines) clearly free up market space for competitors and the Commission assesses whether the commitment is proportionate to the aid amount. The mitigation effect from commitments on the beneficiary to behave in line with market practice, for example on pricing, is also evident. While the Commission monitors compliance with the specific committed actions, this is related to validity of the aid but not *ex post* assessment of the market effects of the measures as implemented. It has already been explained that the compatibility assessment is an *ex ante* assessment, i.e. before the aid measure is implemented by the Member State, on the basis of the information available at that moment. Therefore, the calibration of the commitments to the distortive effect has been performed in each case and the Commission considers that it has provided sufficient assessment in its decisions.

Point 9 of the 2009 Restructuring Communication concerning the comparison with alternative options, including a break-up, or absorption by another bank, refers to the possible contents in the notification for a restructuring plan, i.e. a submission by the Member State – and is not an obligation

²⁵ The Commission notes that the ESRB has not directed any recommendation to the Commission whether a serious disturbance related to a bank in distress existed or whether it does not, and is thus not in a position to comment whether the ESRB would do so.

for the Commission. In line with the case-law of the EU Courts²⁶, the Commission is obliged to only assess the measure as notified by the Member State. It cannot analyse all potential alternative measures capable of achieving the same objective in order to declare the notified measure compatible. *A fortiori*, the Commission does not have the power to replace the notified measure with an alternative measure that it may find more appropriate, more proportionate or less distortive. Furthermore, the choice of a particular aid measure is often a function of supervisory requirements or of the decision by a resolution authority (in case of funds from the SRF or a national resolution fund), which the Commission assesses in its capacity as State aid authority with respect to its compatibility with State aid rules.

CONCLUSIONS AND RECOMMENDATIONS

Commission reply to paragraph 71

The Commission considers that its ethical framework, which according to the ECA is robust, is also appropriate to minimise the risk of inappropriate handling of market sensitive information for the reasons set out above in the reaction provided to paragraphs 33-34.

Commission reply to paragraph 72

The Commission considers that State aid rules were fully fit for the purpose of controlling State aid to financial institutions during the audited period and therefore did not have to be revised for the reasons set out above in the first section and in the detailed reaction provided to paragraphs 30 and 43-50.

Recommendation 1 – Carry out an evaluation whether the State aid rules continue to be appropriate and take corrective action where required

The Commission accepts this recommendation.

In relation to recommendation 1, the Commission accepts to launch an evaluation, in line with its Better Regulation guidelines. The economic impact of the crisis created by the COVID-19 outbreak constitutes a serious disturbance in the economy of Member States and there is high uncertainty on the economic outlook. Therefore, the Commission will conduct an evaluation when the economy has recovered and at the latest in 2023.

Commission reply to paragraph 73

The Commission emphasises it complied with the binding Procedural Regulation and the Implementing Regulation at all times. This should be kept strictly separate from the Commission's internal (non-binding) and more detailed guidance to staff. Nonetheless, any deviation from this internal guidance was not material and did not affect the outcome of the Commission's assessments. The length of State aid procedures in some banking cases is the result of the sensitivity and complexity of such aid measures, which depend on decisions of other actors. In particular, these actors include supervisors and resolution authorities, which, like the Commission in these cases, must protect confidential discussions and market-sensitive information. It should also be recalled that the Commission cannot refuse to give advice to Member States on the State aid implications of potential plans at any stage of the process even if Member States do not always fully adhere to the Best Practices Code. Finally, the Commission recalls that the publication of decisions must avoid divulging business secrets while ensuring maximum transparency, as explained above in the reaction to paragraphs 58-61, and that the timeliness of this publication above all depends on the good cooperation by Member States.

²⁶ Cases T-135/17 SCOR v Commission, paras 94 and 123; T-57/11 Castelnou Energía v Commission, para. 171; C-159/94 Commission v France, para. 101.

Recommendation 2 – Further enhance compliance with internal processes and procedures

The Commission accepts this recommendation.

Concerning recommendation 2(1), the Commission notes that it will roll out a new case management tool (Case@EC) which will facilitate document management also for State aid cases. In this context, the Commission will also remind its staff of the applicable rules regarding document registration and will revise its internal guidance in line with the new document management tool.

Regarding recommendation 2(2), the Commission will remind Member States of the best practices for pre-notification contacts as described in the Best Practices Code. In particular, the Commission will do this in the State aid modernisation Working Group with Member States.

In relation to recommendation 2(3), the Commission recalls that it strongly depends on the cooperation from the Member States to ensure a timely publication of its decision, as the ECA acknowledges. While the Commission has used the tools available to publish State aid decisions without Member States' consent, it would be disproportionate to deploy them immediately and in all cases. The Commission is therefore not in a position to commit alone that this process can be sped up in practice. However, the Commission will remind Member States of the process for confidentiality requests in the State aid modernisation Working Group with Member States. The Commission will also consider providing further internal guidance to staff to ensure an efficient and consistent handling of confidentiality requests by Member States.

Commission reply to paragraph 74

The Commission confirms that its State aid decisions are all based on legally and economically sound assessments and welcomes the ECA's conclusion regarding the rigorous analysis of restructuring plans. The Commission considers that its approach to assess the existence of a serious disturbance was appropriate for the reasons set out above in the detailed reaction provided to paragraphs 64-70. With respect to the impact of measures intended to limit distortions of competition, the Commission points out that it has calibrated these measures (which take the form of commitments) to the distortive effect in each case in the balancing test. The Commission considers that it has provided sufficient reasoning in each decision. As regards performance indicators for the purposes of annual management, the Commission recalls that there are many challenges to build reliable and relevant indicators as set out above in the detailed reaction provided to paragraphs 21-25. Finally, the Commission has already explained that there was no ground to launch a formal evaluation of the 2013 Banking Communication during the audited period. The Commission refers in this respect to the arguments set out above in the executive summary and the replies to paragraphs 28-30 and to paragraphs 43-50.

Recommendation 3 – Improve performance measurement

The Commission accepts this recommendation.

With regard to this recommendation, the Commission agrees to revisit its performance indicators in the context of the Strategic Plan 2020-2024 and the Management Plan 2020, which are currently being prepared. These indicators necessarily concern outputs and results stemming from the activities of DG Competition, over which DG Competition can have control and which are measurable in a reliable and efficient way. The Commission will monitor whether these performance indicators remain suitable.

Audit team

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This performance audit was carried out by Audit Chamber IV Regulation of markets and competitive economy, headed by ECA Member Alex Brenninkmeijer. The audit was led by ECA Member Mihails Kozlovs, supported by Edīte Dzalbe, Head of Private Office and Laura Graudiņa, Private Office Attaché; Zacharias Koliass, Principal Manager; Jörg Genner, Head of Task; Giorgos Tsikkos, Vasileia Kalafati, Marc Hertgen and Maria Isabel Quintela, Auditors. Michael Pyper provided linguistic support.

As a consequence of the COVID-19 pandemic and the strict confinement conditions, no picture of the audit team could be provided.

Timeline

Event	Date
Adoption of Audit Planning memorandum (APM) / Start of the audit	22.1.2019
Official sending of draft report to Commission (or other auditee)	14.5.2020
Adoption of the final report after the adversarial procedure	28.7.2020
Commission's (or other auditee's) official replies received in all languages	27.8.2020

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Our audit found that, for the period from August 2013 to the end of 2018, the Commission had appropriate resources and tools including an appropriate organisational set-up to carry out its control of State aid financial institutions. However, it had not always been in a position to use them to full effect.

The Commission's performance indicators did not fully capture its performance. We observed that market realities improved during the audited period and up to the outbreak of COVID-19 and that the regulatory framework had changed, but that the applicable State aid rules themselves have not been modified since 2013.

In addition, we found that the effectiveness of the Commission's State aid control may have occasionally suffered from the fact that the Commission did not contest Member States' submissions that the conditions for an exceptional approval of State aid existed in each individual case.

ECA special report pursuant to Article 287(4), second subparagraph, TFEU.



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