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INTERNATIONAL AND REGIONAL ORGANISATIONS

REVIEW AND ANALYSIS

EUROPEAN UNION

Specialist Editors: Dr Vincent J G Power; Jason Chuah

STATE AID FOR MARITIME TRANSPORT

Case C–400/99 *Italy v Commission*¹

Jason Chuah

Introduction

In 1999, the Commission commenced investigatory procedures into complaints that the Italian Government was granting unauthorised state aid to its domestic ferry services operated by various undertakings or companies within the Tirrenia di Navigazione group.² Those investigations culminated in a Decision declaring the measures taken by the Italian Government to be unlawful.³ Pursuant to the Decision, the Commission asked Italy to suspend payment of any aid in excess of the net additional cost of providing services of general economic interest. Italy refused. Its government and six companies in the Tirrenia group brought actions in the ECJ and the CFI respectively seeking the annulment of the Decision.

The procedural history of this case is especially long drawn out for various reasons, but the net result was that the CFI suspended proceedings pending a ruling from the ECJ on the legality of the Decision. In the meantime, through protracted negotiations and examination, the Commission decided to suspend the application of the Decision as regards some of the state aid measures in question – that is to say, some of the measures were pronounced no longer to be incompatible with the proscription against unlawful state aid. The aid, in relation to certain companies in the group, was found to be justified on the grounds of compensating the provision of public services. The Decision remained applicable, however, to two aid measures provided by the Italian Government.

It might additionally be noted that the Commission considered the aid not to be part of an existing aid scheme but a new aid; as such, it relied on Article 88(3) instead of Article 88(1) EC in issuing the

¹ Judgment of 10 May 2005, ECJ.

² In general, state aid may only be granted to ships entered in the Member State's register. According to the recent Guidelines on State aid for maritime transport (OJ 2004 C 13, p 3 (17 January 2004)), aid may exceptionally be granted in respect of other ships provided: (a) they comply with the international standards and Community law (including those relating to security, safety, environmental performance and on-board working conditions); (b) they are operated from the Community, and (c) their shipowner is established in the Community and the Member State is able to show that the register (elsewhere) contributes directly to the objectives of the Guidelines (supra n 14). Flagging thus is particularly important in the context of state aid for maritime transport.

³ OJ 1999 C306 p 2.

Decision.⁴ One primary issue of the present case was thus whether the Commission had correctly classified the aid measures as new aid.

Context

There were two types of state aid which the Commission alleged to be in breach of the treaty provisions:

- (a) a tax treatment from which the Tirrenia group benefited in respect of the fuel and lubricating oils for its vessels
- (b) subsidies paid to compensate the Tirrenia group for maritime services the group was obliged to provide to the public.

The Commission recognises that some state aid to maritime transport is necessary, but has always been concerned that there should be consistency of practice and policy between Member States. In its Communication of 17 January 2004⁵ it published a set of guidelines on how and to what extent the granting of state aid to the maritime sector would be tolerated. Preferential fiscal treatment of shipowning companies by Member States is not a new phenomenon; many Member States have taken special measures to improve the so-called 'fiscal climate' for shipowning companies, including, for example, accelerated depreciation on investment in ships, or the right to reserve profits made on the sale of ships for a number of years on a tax-free basis, provided that the profits are reinvested in ships. Such preferential fiscal treatment, especially where it is discriminatory, are generally incompatible with the spirit of the free movement principles. However, the Commission is not disinclined to approve the fiscal treatment, given the need for EU flag states to compete with flags of convenience. There should therefore, as a rule, be a link between the tax relief scheme and a Community flag. Additionally, any aid provided 'must be necessary to promote the repatriation of the strategic and commercial management of all ships concerned in the Community and, in addition, that the beneficiaries of the schemes must be liable to corporate tax in the Community'.⁶

As far as maritime cabotage is concerned, the Commission has stated that if an international transport service is necessary to meet imperative public transport needs, Public Services Obligations (PSOs) may be imposed or Public Service Contracts (PSCs) may be concluded, provided that any compensation is subject to the provisions of state aid. The duration of such contracts should necessarily be limited to a reasonable period so as not to result in the creation of a private monopoly.

Procedural arguments

Right to be heard

It is noteworthy that under Article 88(2), there should be an opportunity for the Member State to inform and, possibly, explain that the measures in question do not constitute state aid or constitute existing aid. That was indeed the claim of the Italian Government in the present case. The ECJ ruled that, as regards that procedural opportunity, the Member State should be entitled to respond to each

⁴ Article 88 reads:

- '(1) The Commission shall, in cooperation with Member States, keep under constant review all systems of aid existing in those states. It shall propose to the latter any appropriate measures required by the progressive development or by the functioning of the common market.
- (2) If after giving notice to the parties concerned to submit their comments, the Commission finds that aid granted by a State or through State resources is not compatible with the common market having regard to Article 87, or that such aid is being misused, it shall decide that the State concerned shall abolish or alter such aid within a period of time to be determined by the Commission.

If the State concerned does not comply with the decision within the prescribed time, the Commission or any other interested State may, in derogation from the provisions of Articles 226 and 227 refer the matter to the Court of Justice direct.

- (3) The Commission shall be informed, in sufficient time to enable it to submit its comments, of any plans to grant or alter aid. If it considers that any such plan is not compatible with the common market having regard to Article 87, it shall without delay initiate the procedure provided for in paragraph 2. The Member State concerned shall not put its measures into effect until this procedure has resulted in a final decision.'

⁵ Guidelines (n 2); the Guidelines are intended to replace a similar set of guidelines published in 1997 (OJ 1997 C 205 p 5).

⁶ *ibid* para 3.1 p 6.

and every one of the measures in question. A discussion with the Commission generally of the measures taken collectively was not enough.

The Commission also argued that under Regulation 659/1999⁷ on procedure in state aid cases, in the case of new aid not notified but implemented,⁸ the procedure in Article 88(2) did not need to be preceded by correspondence with the Member State concerned. It contended that although Article 10(2) of that Regulation may indeed allow the Commission to seek information from the State in advance, that was not a legal obligation. That provision states that the 'Commission, if necessary, shall request information from the Member States concerned'. As far as the ECJ is concerned, that provision should not be read as releasing the Commission from the obligation to discuss a measure with the Member State concerned. It merely expresses a reservation regarding cases in which the Commission has already adequately discussed the measure at issue with the Member State. The Court considered, for example, 'if it is the [Member State] itself that informed the Commission of the existence of that measure',⁹ then the Commission may decide that there was nothing more to be achieved from a discussion with the Member State concerned. In so holding, the ECJ declined to imply a stronger element of discretion into the provision, thereby confining the provision to the position prior to the Regulation.¹⁰

As regards the complaint that the Italian Government had given the Tirrenia group special tax advantages, the ECJ found that the Commission had not properly consulted with the Member State and, as such, the Decision was to be annulled to the extent that it entailed the suspension of the tax treatment to the group for supplies of fuel and lubricating oils for its vessel.

On the subsidies, however, the Court found that it was apparent from the correspondence that those matters were dealt with by both the Commission staff and the Italian authorities. It could not therefore be claimed that Italy had not been given the opportunity to put its views to the Commission prior to the Decision being taken. That part of the Decision would therefore not be annulled on the basis of lack of consultation.

A related question, in the maritime context, is to what extent the Guidelines on State aid to maritime transport might be relevant to an assessment of the Member State's right to be consulted. Paragraph 12 of the Communication requires Member States to communicate to the Commission, with reference to all existing or new aid schemes falling within the scope of the Communication, an assessment of their effects during the sixth year of implementation. It is obvious that the Commission is keen to shift the responsibility for information collecting to the Member States. The Communication clearly carries no mandatory legal effect; as such, it would be interesting to see how the Court would respond to Member States failing to provide such information. How should paragraph 12 of the Communication be read with Article 10 of the Regulation on procedure in state aid cases, in the case of new aid? One guiding principle might be said to be the spirit of cooperation between Member States and the Commission, as has frequently been alluded to by the ECJ in state aid cases. On that basis, it might be suggested that the net effect is that Member States are required to provide relevant information, but that it is not a right of the Commission to decline to consult.

Misuse of powers

Italy also submitted that the Commission was guilty of misuse of powers. That defence is increasingly popular, both in competition law and state aid cases, but the Court has been exceedingly careful not to distend the application of the principle beyond that which, in its mind, is consistent with the *raison*

⁷ OJ 1999 L 83 p 1 (22 March 1999).

⁸ The so-called 'unlawful aid' referred to in Ch III of the regulation. It was common ground that the Italian Government had not notified the Commission of the special tax treatment and subsidies conferred on the Tirrenia group.

⁹ Para 30 of the judgment.

¹⁰ *France v Commission (Boussac)* [1990] ECR I-307; following the Court's decision there, the Commission then adopted a procedure where the Member State would be written to and an explanation of the aid measures sought, within 30 days or fewer depending on the urgency of the case. The Member State was given an expectation, if not a right, to be consulted.

d'être of the Commission's discretionary powers and the objectives of the single market. A decision would only amount to a misuse of powers 'if it appears, on the basis of objective, relevant and consistent facts, to have been taken for purposes other than those stated'.¹¹ Although evidence of bad faith is not necessarily sought by the Court, the evidence should be such that some sort of malfeasance¹² or excess of powers is present. In the present case, according to the ECJ, misuse of powers could only have been established if it could be shown that the Commission had deliberately classified as new aid measures which were obviously existing aid measures or not state aid measures at all. In the light of the information available to the Commission at the time the Decision was taken, it could not be said that it was beyond doubt that the subsidies paid to the Tirrenia group constituted existing aid or measures not being state aid at all.¹³ The question is always one of proof and the persuasiveness of the evidence. There are no guidelines, but from the facts, it would seem that as the subsidies given were obviously in excess of the net additional costs lined with the provision of public services by the beneficiary, the Tirrenia group, the Commission could not be said to have acted inappropriately in its classification of the measure as a new state aid.

Misuse of powers is a defence principally dependent on the characterisation of the objectives to be achieved by the Commission. In this regard, it is necessary to observe that the new Guidelines on State aid to maritime transport refer to the following objectives:

- improving a safe, efficient, secure and environment friendly maritime transport
- encouraging the flagging or re-flagging to Member States' registers
- contributing to the consolidation of the maritime cluster in the Member States while maintaining an overall competitive fleet on world markets
- maintaining and improving maritime know-how and protecting and promoting employment for European seafarers
- contributing to short sea shipping.¹⁴

In this connection, it is clear that the Commission's objectives extend beyond the economic to social, technological and environmental concerns. Thus, given the wide range of objectives the Commission is entrusted to achieve in the context of State aid for maritime transport, the defence of misuse of powers is unlikely to succeed.

New aid or existing aid

The distinction between new aid (that is to say, the grant of an aid not previously there or the modification of a pre-existing aid) and existing aid is not entirely free from controversy. Take, for example, the variation of certain tax thresholds in a pre-existing tax regime applicable to maritime operators. That might at first glance appear to be new aid; but it might be shown the implications of the change are not appreciable or that the general scheme remains unchanged, only certain thresholds have been modified. Similarly, in the present case the Italian Government argued that, as the subsidies had been paid out as compensation for public service contracts, they were governed by Regulation 3577/92 applying the freedom to provide services to maritime transport within Member States.¹⁵ They then relied on Article 4(3) of that Regulation which allows public service contracts already existing at the date of entry into force of the Regulation to remain in force until their respective expiry dates. Italy argued that as the subsidies had been paid long before the Maritime Cabotage Regulation was in existence (and indeed, in some payments, long before even the Treaty of Rome was signed), Article 4(3) presumes that the Commission has notice of such measures. It thus followed that authorisation for those measures may be implied from the Commission's lack of objection and presumed knowledge.

¹¹ Para 38 of the judgment see also *Joined Cases 18/65 and 35/65 Guttman* [1966] ECR 103.

¹² Not used as a term of art.

¹³ Para 40 of the judgment.

¹⁴ Guidelines (n 2) para 2.2.

¹⁵ OJ 1992 L364 p 7 (the Maritime Cabotage Regulation).

The remit of Article 4(3), Maritime Cabotage Regulation is particularly interesting. The ECJ held that the provision relates to public service contracts with maritime companies involved in regular services to and from islands and between islands. Contracts of that type by their nature contain financial provisions needed to cover the public service obligations for which they provide. The Court then said:

In so far as the wording of Article 4(3) . . . concerns the continuation of the contracts at issue, without limiting the scope of that provision to certain aspects of those contracts, the financial provisions necessary to cover the public service obligations mentioned therein are covered by the said Article 4(3). The Commission is therefore wrong to assert that that provision does no more than authorise the possible maintenance of exclusive or special rights deriving from such contracts.

That said, however, the ECJ found that any aid *in excess* of what is necessary to cover the public service obligations could not come within Article 4(3). As such, the Decision in so far as it relates to such payment which is not commensurate with the actual cost of providing a public service obligation must be upheld.

As regards the Commission's powers, the Court opined that the Commission should not be criticised for commencing proceedings, despite its uncertainty as to the status of the aid measures. Nonetheless, it required the Commission to undertake an adequate examination of the question, even if the outcome of that examination is a non-definitive classification of the measure examined.¹⁶

Conclusion

The present case is a good example of how general principles of procedure in State aid might be read and applied in a maritime context. The maritime context requires an enhanced reading of the principles of State aid;¹⁷ indeed, as the present case demonstrates, there is, additionally, the interplay between State aid rules and freedom of maritime services rules (such as those contained in the Cabotage Regulation) which should be properly accommodated. The present case is also significant in how the Court approached the matter of procedural fairness – especially, the right of Member States to be heard. The Court was clearly unwilling to extend the categories of what constitutes misuse of power but, in relation to the right to be heard, it was equally firm that the new procedural guidance in Regulation 659/1999 was not intended to do away with such a requirement, even in a case of an unnotified aid. That said, it should not be forgotten that with the new Guidelines, there is in relation to a large number of State aid measures a duty¹⁸ on Member States to update the Commission on their effects in the light of the Guidelines' objectives.¹⁹

¹⁶ Para 54 of the judgment.

¹⁷ As the Commission stresses in the Guidelines (supra n 2) at p.4 (of the OJ report), "even though as a matter of principle operating aid should be exceptional, temporary and degressive, the Commission estimates that State aid to the European shipping industry is still justified".

¹⁸ Guidelines (n 2) para 12.

¹⁹ Guidelines (n 2) para 2.2.