



CPI EU News Presents:

State aid recovery ends where private savings begin rules General Court in *Arco* judgment

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It has been more than 10 years since Lehman Brothers went bankrupt but the consequences of the financial crisis that ensued are still with us. In Belgium the crisis led to the collapse of two of the four main banks, Fortis and Dexia, which meant that small shareholders, who believed their investments were safe, sometimes lost their entire life savings. Dexia was a peculiar case: one of its main shareholders was Arco group, a cooperative holding with close ties to Flemish Christian-democrat organizations in Belgium.

Background

In the autumn of 2008, the European Union and Belgium introduced a number of measures to increase public confidence in the banking system. One of the promises the Belgian federal government made was to extend the deposit guarantee scheme (protecting bank account deposits up to a certain level from loss in case of a bank's insolvency) to the shares of individuals in financial cooperatives. It took until October 10, 2011 for the Belgian government to formalize this promise in a Royal Decree which allowed financial cooperatives to opt in to such a form of financial protection. The three entities of the Arco group were the only financial cooperatives that did so: they made the necessary financial contributions until December 8, 2011 when the shareholders of the cooperatives decided to liquidate them.

On April 3, 2012, the Commission decided to formally investigate the aid granted by the Belgian State to Arco through the financial guarantee given to financial cooperatives, and to enjoin the Belgian State from making any payments under that guarantee.² At the end of its investigation on July 3, 2014, the Commission concluded that the guarantee given by the Belgian government (already in the form of a promise in 2008) benefitted Arco since it strengthened the confidence of its shareholders who might otherwise have withdrawn their shareholding. The guarantee therefore constituted illegal State aid, estimated according to press reports at around 150 million euro. The Commission ordered the recovery of the aid and also maintained its prohibition on any payments pursuant to the guarantee in the future.³

The Commission decision of July 3, 2014 already gave rise to two judgments by the European Courts. First of all, several individuals who directly held shareholdings in Dexia (i.e. not through Arco) had brought proceedings before Belgium's highest administrative court, the Council of State, for the annulment of the Royal Decree of October 10, 2011 since they considered that the Royal Decree unfairly favored indirect shareholdings in Dexia (through Arco) over direct shareholdings. The Council of State referred the case to the Belgian Constitutional Court which, in turn, made a preliminary reference to the Court of Justice concerning the legality of the Commission decision of July 3, 2014. On December 21, 2016, the Court of Justice ruled that there were no indications that that Commission decision was unlawful.⁴

On this basis, the General Court on February 9, 2018 also dismissed four of the five pleas from the application for an annulment brought by Arco against that same Commission decision as manifestly unfounded.⁵ Arco's fifth plea in this case was declared manifestly inadmissible. It related to the fact that the Commission decision of July 3, 2014 not only required the Belgian State to recover the aid from Arco but also prohibited it from making any further payments pursuant to the guarantee. The General Court ruled that the interests of the natural persons who could receive such payments (Arco's shareholders) was distinct from the interest of Arco and that therefore the latter did not have standing to bring this plea. The very same plea was, however, the single plea raised by the Belgian State in its application for an annulment which led to the General Court's judgment of December 7, 2018 which I'm discussing here.

Judgment of December 7, 2018

Indeed, like Arco in its fifth plea, the Belgian State in its single plea argued that Arco's shareholders were natural persons who were not undertakings so that any payments to them could not amount to State aid in the sense of Article 107 TFEU. Since the Commission's prohibition to make payments under the guarantee therefore appeared to go beyond the scope of Article 107 EU, the Belgian State argued that it was disproportionate.

Under Article 263 TFEU, EU Member States do not need to show that they have an interest in the arguments which they bring before the European Courts: they are privileged applicants and automatically have standing. The General Court could therefore not declare the Belgian State's action inadmissible for this reason. However, the Commission argued that the application brought by the Belgian State was inadmissible on another basis. Following the judgment of the Court of Justice of December 21, 2016 referred to above, the Belgian Constitutional Court and the Belgian Council of State had both taken issue with the guarantee contained in the Royal Decree of October 10, 2011 and the Council of State had formally annulled the Royal Decree. As a consequence, the Commission argued, the guarantee was no longer in force and the Belgian State's attempt to annul the prohibition of payments under the guarantee could not change that, so it was devoid of purpose.

The General Court rejected this argument, pointing out that the Belgian State was considering new measures with an equivalent effect as the guarantee to compensate the Arco shareholders for the losses they suffered from the collapse of Arco. The Commission had opposed the introduction of such measures also on the basis that they would amount to a circumvention of the Commission decision of July 3, 2014. This, of course, supposed that that decision, including the prohibition of payments under the guarantee, was lawful - which was precisely contested by the Belgian State.

The General Court then turned to the substance of the application for an annulment. It recalled that the Commission had established that the guarantee constituted State aid to the benefit of Arco because it strengthened the confidence of its shareholders who might otherwise have withdrawn their shareholding. However, Arco had been put into liquidation on December 8, 2011 and after this date shareholders could no longer withdraw their shareholding, so that the guarantee ceased to have a distortive effect on competition from that date (which was also recognized in the Commission's calculation of the amount of aid received by Arco). Any future payments under the guarantee as prohibited by the Commission decision of July 3, 2014 could therefore also not have such a distortive effect and did not amount to State aid.

The General Court also pointed out that the Belgian State had registered a claim with Arco's liquidators for the recovery of the illegal State aid. This ensured that any benefit which Arco derived from that State aid would be neutralized. According to the General Court, the prohibition to make any payments to the shareholders under the guarantee could therefore not contribute to this objective of removing the competitive advantage of the State aid.

As a consequence, the General Court considered the prohibition to make any future payments a disproportionate measure which went beyond the powers of the Commission under the State aid rules. This prohibition contained in the Commission decision of July 3, 2018 was therefore annulled.

Comment

The judgment of the General Court is well reasoned and its distinction between the recovery of the aid from the beneficiary (which is necessarily an undertaking) and measures which do not affect the beneficiary or the recovery of the aid, is dogmatically attractive.

One issue that is not dealt with in the judgment is the fact that the prohibition to make any payments under the guarantee scheme was originally introduced as an interim measure (a suspension injunction under Article 11(1) of Regulation 659/1999) in the Commission decision of April 3, 2012 opening the Commission's formal investigation. It was therefore not aimed at the recovery of the aid but merely sought to avoid that further aid would be granted. The General Court's observation that Arco had gone into liquidation and therefore did not have any economic activity was already pertinent at the time, but the Commission may have feared that Arco would be liquidated prior to any recovery of the aid granted, so that such an injunction was necessary regardless of any further distortive effects of the aid.

More fundamentally (and this also applies to the decision of July 3, 2014), any continuation of the guarantee, or any payment thereof, would retroactively confirm the promises made by the Belgian State in 2008. In the future, such promises will therefore appear to be credible and this will engender the distortive consequences which the State aid rules are meant to avoid: companies with shareholders benefiting from guarantees will find it easier to raise and maintain capital than those whose shareholders do not benefit from them. There seems to be little doubt that when the promise was made in 2008, it was not merely made to safeguard private savings, but also to affect market conditions, namely to stabilize financial markets - a distortion of ordinary competition, for better or worse.

But what would be the alternative for a Member State wishing merely to protect private savings? The Belgian State could have nationalized or propped up Dexia without the participation of Arco, resulting in the almost immediate collapse of the latter, and immediately afterwards could have offered to compensate Arco shareholders. Such a solution would not have involved any State aid to Arco, but it may have appeared even more draconian than the solutions that were implemented in the fall of 2008, when many may also have hoped that Dexia could somehow be saved and that the guarantee of the Belgian State for Arco's shareholders would, in the end, not be relied on. Not granting State aid to Arco itself may then have exacerbated fears of financial collapse and the subsequent sovereign debt crisis.

In any event, given the consequences of this judgment for State aid recovery and suspension in general, the Commission may well appeal it as a matter of principle to the Court of Justice - regardless of how it feels about the compensation of Arco shareholders in this instance. In the meantime, the judgment of the General Court provides ammunition for those who want to find an alternative solution for the Arco shareholders. Following the reasoning of this judgment, if the Belgian State enforces its recovery claim against Arco's assets in liquidation, a subsequent compensation of individual shareholders for the losses they suffered would not be prohibited by the European State aid rules.

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² Commission decision of April 3, 2012 in case SA.33927 Guarantee scheme protecting the shares of individual members of financial cooperatives (Arco).

³ Commission decision of July 3, 2014 in case SA.33927 Guarantee scheme protecting the shares of individual members of financial cooperatives (Arco).

⁴ Case C-76/15, *Vervloet and Others*, ECLI:EU:C:2016:975.

⁵ Case T-711/14, *Arcofin and Others v. Commission*, ECLI:EU:T:2018:80 (only available in French).