

Tackling Legal Uncertainty of State Aid and Compensations for Public Service Obligations in the Social and Solidarity Economy

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Abstract: Pursuant to Article 107(1) of the Treaty on the Functioning of the European Union, “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”. Article 107(2) sets a limitative list of exemptions to this rule while Article 107(3) imposes an *ex ante* control procedure of compatibility with the internal market. The purpose of the EU lawmaker is to have less but better targeted state aids to boost the European Economy.

This paper aims at demonstrating that a distinction should be made between, on the one hand, state aids granted for the sake of social utility of social enterprises (and thus in view of their social impact) and, on the other hand, compensations for public service obligations. The former should be declared lawful under Article 107(2), subject to the demonstration of their social utility through social impact assessment. The latter should be considered as a price owed by national public authorities, subject to the various management controls required in national Public Law.

Introduction

On 3 September 2020, the French Government released a € 100 billion post-Covid 19 recovery plan, € 1,3 billion of which is dedicated to Social and Solidarity Economy, mostly in the form of “state aids”. These can be tax advantages (such as tax incentives for donations or the right to receive manual gifts, donations and legacies without paying transfer duties), reductions in social security contributions, subsidies, voluntary work, community service, civic service for young people, subsidised labour contract, free provision of premises, etc.

As they constitute a risk of competition distortion, state aids are in principle prohibited in the European Union in Article 107(1) of the Treaty on the Functioning of the European Union (TFEU) even for social enterprises, no matter if the potential distortion of competition would only affect a single domestic market (as Social Economy is most likely locally rooted, except in fair trade and humanitarian assistance) as soon as social enterprises fit in the legal definition of enterprise (or undertaking) in European Law, meaning that they shall be units producing goods or services with a certain degree of autonomy in decision-making (especially towards public authorities)¹. This is automatically the case for any undertaking legally classified as social enterprise pursuant to Article 2(2) of Regulation (EU) No. 346/2013 of the European Parliament and of the Council of 17 April 2013 on European social entrepreneurship funds, which adds three cumulative distinctive criteria of Social and Solidarity Economy: a social enterprise is an enterprise with (i) social utility, with (ii) a not-for-profit purpose (associations, foundations, endowment funds) or limited lucrativeness and with (iii) democratic governance.

Which reforms of European Law could be proposed to secure the state aids granted to social enterprises? Our approach consists in circumventing the prohibition of Article 107(1) of the Treaty by enhancing the social utility **(I)** and public interest **(II)** that underly in Social Economy and thus, such state aids could be legitimated on the ground of other articles of the Treaty.

I. Securing state aids for the sake of social utility

Social utility of social enterprises not only justifies that they benefit from the existing block exemptions provided by Article 107(2) of the Treaty **(1.1)**, but also that a new one is specifically created for Social and Solidarity Economy **(1.2)**.

¹ ECJ, 13 July 1962, *Mannesmann*, C-19/61, EU:C:1962:31, paragraph 705: “an undertaking is constituted by a single organisation of personal tangible and intangible elements, united in an autonomous legal entity pursuing a given long-term economic aim”.

1.1. The current main exemptions from the prohibition in Article 107 (1) that apply to Social and Solidarity Economy

Many social enterprises are entitled to benefit from one or more exemptions set forth in Article 107(2)(3) and in Commission Regulation (EU) No. 651/2014 of 17 June 2014 declaring certain categories of aid compatible with the internal market which notably legitimate:

- (a) aids to promote the economic development of areas where the standard of living is abnormally low
- (b) aids to remedy a serious disturbance in the economy of a Member State (and we believe that the state aids of the French post-Covid 19 recovery plan fall into this category)
- (c) aids to facilitate the development of certain economic activities or of certain economic areas
- (d) aids to promote culture and heritage conservation
- (e) aids to small and medium-sized enterprises (SMEs) in the form of investment aid, operating aid and SMEs' access to finance
- (f) aids for environmental protection
- (g) aids for research and development and innovation
- (h) training aid
- (i) recruitment and employment aids for disadvantaged workers and workers with disabilities
- (j) aids for sport and multifunctional recreational infrastructure².

² In comparison, Article 5(1) of the Slovenian Act No. 300-01/10-53/162 of 7 March 2011 on social entrepreneurship provides:

“Social entrepreneurship activities are performed in the following areas:

- social protection,
- family care,
- protection of the disabled,
- science, research, education and training,
- youth work,
- health protection and promotion,
- social inclusion, promoting employment and vocational training for the unemployed or for people at risk of unemployment,
- employment of disadvantaged workers, severely disadvantaged workers and disabled workers,
- organic food production,
- nature conservation, regulation and protection of the environment and protection of animals,
- renewable energy sources and green economy,

Furthermore, Commission Regulation (EU) No. 1407/2013 of 18 December 2013 also allows each Member State to grant a maximum of € 200,000 state aid to a single enterprise over three years (the “*de minimis*” aid) without having to go through the process of *ex ante* assessment by the European Commission of compatibility with the internal market set forth in Article 107(3).

1.2. Advocacy for a block exemption for Social and Solidarity Economy in Article 107(2)

Although the current state of law seems supportive of social enterprises, we would stand in favour of a review of Article 107(2) that would create a specific block exemption for Social and Solidarity Economy, for several reasons.

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- tourism for people whose living conditions prevent or impede access to tourist services, in a way that respects the values of sustainability, accessibility and solidarity (social tourism),
 - trade for socially disadvantaged people (social trade) and trade that ensures the sale of products of small producers from the most economically underdeveloped environments on the basis of ethical, transparent and equal business relations between producers and traders, aimed primarily at ensuring fair payment of producers and thus their survival (fair trade) and trade in services and products from social entrepreneurship,
 - culture, technical culture and the preservation of cultural, technical and natural heritage,
 - amateur sports and physical education, the purpose of which is recreation and socialisation,
 - development of local communities,
 - support services for social enterprises”.

Article 2 of the French Act No. 2014-856 of 31 July 2014 on Social and Solidarity Economy, defining social utility, provides:

“Undertakings shall be regarded as pursuing social utility within the meaning of this law if their purpose primarily meets at least one of the following four conditions:

1° Their objective is to provide, through their activity, support to people in a situation of vulnerability either because of their economic or social situation, or because of their personal situation and particularly their needs in terms of social, medico-social or health support, or to contribute to the fight against their exclusion. These persons may be employees, users, clients, members or beneficiaries of the enterprise;

2° They are intended to contribute to the preservation and development of social links or to the maintenance and strengthening of territorial cohesion;

3° They are intended to contribute to citizenship education, especially through community education and the implementation of participation modes involving, in the territories concerned, the beneficiaries of these activities. In this way, they contribute to the reduction of social and cultural inequalities, especially between women and men;

4° They aim to contribute to sustainable development, energy transition, cultural promotion or international solidarity, provided that their activity also contributes to producing an impact either by supporting vulnerable groups, or by maintaining or recreating territorial solidarity, or by participating in citizenship education”.

First, the *rationale* behind the prohibition of state aids in Article 107(1) is the need to curb the risk of competition distortion in the internal market. Yet, because of their social utility, social enterprises tend to address social needs unmet or inadequately met under current market conditions or through public policies. In other words, social enterprises either have a non-profitable activity or they position themselves on a low-profit market by targeting an insolvent public. Therefore, the risk of a competition distortion by social enterprises is quite insignificant³.

Second, such a review would drastically simplify and clarify the European Law for social enterprises: by amending the Treaty (or “primary EU Law”), this review would provide state aids for social enterprises with the highest degree of legal certainty.

Third, this review would secure vital resources for social enterprises. This is an even more important point since state aids can have a leverage effect in co-investments gathering public and private investors⁴.

Last but not least, making all state aids to social enterprises compatible with the internal market would be a concrete act of acknowledgment of the fundamental role of Social and Solidarity Economy in our “social market economy”, to which Article 3 of the Treaty refers while defining the purpose of the European Union:

“1. The Union's aim is to promote peace, its values and the well-being of its peoples [...].

3. The Union shall establish an internal market. It shall work for the sustainable development of Europe based on balanced economic growth and price stability, a highly competitive **social market economy**, aiming at full employment and social progress, and a high level of protection and improvement of the quality of the environment. It shall promote scientific and technological advance.

³ By the way, this is the reason why the European Court of Justice did not rule invalid a state aid granted by the Italian Government to co-operatives in the following case: ECJ, 8 September 2011, *Paint Graphos*, EU:C:2011:550, paragraph 61 to 63.

⁴ Commission Expert Group on Social Entrepreneurship (2016), *Social enterprises and the social economy going forward. A call for action from the Commission Expert Group on Social Entrepreneurship*, 31 October 2016, p. 62, http://ec.europa.eu/growth/tools-databases/newsroom/cf/itemdetail.cfm?item_id=9024.

It shall combat social exclusion and discrimination, and shall promote social justice and protection, equality between women and men, solidarity between generations and protection of the rights of the child.

It shall promote economic, social and territorial cohesion, and solidarity among Member States [...].

5. In its relations with the wider world, the Union shall uphold and promote its values and interests and contribute to the protection of its citizens. It shall contribute to peace, security, the sustainable development of the Earth, solidarity and mutual respect among peoples, free and fair trade, eradication of poverty and the protection of human rights [...].”

Such a reform of Article 107(2) of the TFEU would also be in line with paragraph 33 of the European Parliament Resolution No. 2014/2236 of 10 September 2015 on Social Entrepreneurship and Social Innovation in combating unemployment, which provides:

“[The Parliament] points out that the state aid rules should not constitute an impediment for public funding to social and solidarity-based economy enterprises and social services; in this sense, [the Parliament] calls on the Commission to be flexible in the application of state aid rules for such enterprises and services, and to help ensure that local and regional authorities understand and apply correctly state aid targeted thereon”.

II. Securing subsidies in consideration of public interest

In the current state of law, when Article 107(2) is not applicable, the compliance of state aids with the EU Competition Law is questioned while many of them should be legally classified as compensations for services of general economic interest, which are compatible with the internal market pursuant to Article 106(2) of the Treaty **(2.1)**. This finding should lead to a revision of Article 106 of the Treaty **(2.2)**.

2.1. The relevance and benefit of classifying subsidies as compensation for services of general economic interest

In its 2003 “Altmark” judgment⁵, which also provides the initial definition of state aid, the European Court of Justice sets out four cumulative conditions for public resources to escape the classification of state aid and be qualified as compensations for services of general economic interest under Article 106(2) of the Treaty. These four conditions are detailed in the Communication from the Commission on the application of the European Union State aid rules to compensation granted for the provision of services of general economic interest No. 2012/C 8/02 of 11 January 2012. These four cumulative criteria are:

1. the existence of a Service of general economic interest (SGEI), the mission of which is clearly defined by the Member State
2. the existence of a mandate entrusting this SGEI to one or more companies (“entrustment act”)
3. the absence of overcompensation
4. the selection of the undertaking that shall “either be the result of a public procurement procedure which allows for selection of the tenderer capable of providing those services at the least cost to the community, or the result of a benchmarking exercise with a typical undertaking, well run and adequately provided with the necessary means”.

The main public resource in Social and Solidarity Economy is subsidy, especially when it comes to non-profit organisations (NPOs). Are subsidies some compensations for SGEIs?

Here, the most questionable distinctive criterion of compensation for SGEIs is the second one: the existence of an entrustment act. In French Law, an entrustment act is in principle an “official, prior, injunctive [positive] act”⁶, resulting from a law, a regulation

⁵ ECJ, 24 July 2003, *Altmark*, C-280/00, EU:C:2003:415, paragraph 95.

⁶ CHAUVIERE, M., HENRY, J. (2011), « Quel statut pour les services sociaux dans l'Union européenne ? », *RDSS*, 2011, p. 1043-1058.

or a unilateral administrative act (decree or decision), but it may also be an agreement (public service delegation agreement, public procurement contract, annual or multiannual agreement on objectives⁷).

Article 59, paragraph 1 of French Act No. 2014-856 of 31 July 2014 on Social and Solidarity Economy provides:

"Subsidies constitute optional contributions of any kind, decided by the public authorities and the institutions in charge of the management of an industrial and commercial public service, justified by a public interest and aimed at the realisation of an action or an investment project, at the development of activities or at the overall financing of the activity of the beneficiary private entity. These actions, projects or activities shall be initiated, defined and implemented by beneficiary private entities".

Thus, the granting of a subsidy should be regarded as an *ex post* and tacit acknowledgement of the existence of a public contract initiated by the private entity (here, the social enterprise) and therefore, as an entrustment act.

Is the discretionary (“*optional*”) nature of the subsidy an obstacle to such legal classification? Actually, we believe that since the pursuit of a general economic interest by a social enterprise is acknowledged by a public authority or by an institution in charge of the management of an industrial and commercial public service, the subsidy that comes from this acknowledgement should no longer be discretionary, but should be regarded as a price and, in other words, as a debt for such public authority or institution toward the social enterprise until the activity of public interest ends and until complete payment of the sums due.

Such an interpretation of Article 59 would lead not only to making subsidies sustainable financial resources (which is really not the case at present), but also, indirectly, to unleashing the social innovation potential of social enterprises. Indeed, social

⁷ HCVA (the French High Commissioner for the Third Sector), *Avis du HCVA sur le Paquet Almunia*, 15 November 2012, http://www.associations.gouv.fr/IMG/pdf/hcva_paquet_Almunia.pdf

enterprises would feel encouraged to spontaneously take over SGEIs even where users are insolvent, thanks to the assurance of receiving compensation.

This would also limit the dissolution and liquidation of associations that are too small to be able to offer a competitive response to calls for tenders and *“insufficiently equipped to bid for public contracts, even though they contribute to social cohesion”*⁸.

2.2. The necessary amendment of Article 106(2)

Compensations which do not meet the criteria of Communication No. 2012/C 8/02 may still be declared compatible with Article 107 of the Treaty on the ground of the Commission Regulation (EU) of 25 April 2012 on the application of Articles 107 and 108 to *de minimis* aid granted to undertakings providing SGEI. This text sets a higher threshold than Regulation (EU) No. 1407/2013: below € 500,000 (instead of € 200,000 for other state aid), compensations for SGEI do not have to be notified in advance to the European Commission.

Once again, we would rather suggest a review of Article 106 that would define subsidies the way French Law does and that would expressly classify reasonable subsidies as compensations for SGEI under Article 106(2) of the Treaty. Our arguments for this reform are quite the same as for the review of Article 107(2)⁹.

Conclusion

In brief, this paper supports two reforms of the European Law on state aids for social enterprises.

The lesser one would consist in considering the main public resources for social enterprises – subsidies – as compensations for SGEI under Article 106(2) since they are tangible and public acknowledgement of the pursuit of public interest provided, however, that there is no overcompensation.

⁸ HCVA, prec.

⁹ See Section 1.2 above.

The greater reform would lead to grant social enterprises a block exemption under Article 107(2) for all state aids, regardless of their legal classification, by virtue of the social utility of social enterprises (which is a broader notion than public interest).

In consideration of these reforms, social enterprises would have to endure an assessment of their social utility (for state aids) or public interest (for compensations for SGEI). By such concession, they would not submit to the postmodern injunction of ever increased performance that gave birth to the New Public Management theory and to the various management controls required in national Public Law, but they would rather take the chance to display an exemplary accountability for the management of public resources.

The enterprises that would succeed in demonstrating their social utility or their public interest and their compliance with the other criteria of Article 2(2) of Regulation (EU) No 346/2013 above mentioned – not-for-profit purpose or limited lucrativeness and democratic governance – would be granted with the “Social Enterprise” label which would give them access to all public and private financial resources dedicated to Social and Solidarity Economy. Following the Parliament Resolution No. 2016/2237 of 5 July 2018 with recommendations to the Commission on a statute for social and solidarity-based enterprises, the European Union will hopefully create such a label.