

## Community guidelines on State aid for environmental protection

(2001/C 37/03)

### A. INTRODUCTION

1. In 1994 the Commission adopted the Community guidelines on State aid for environmental protection <sup>(1)</sup>, which expired on 31 December 1999. In accordance with point 4.3 of the guidelines, it conducted a review in 1996 and concluded that there was no need to make any amendments in the meantime. On 22 December 1999 it decided to extend the validity of the guidelines until 30 June 2000 <sup>(2)</sup>. On 28 June 2000 the Commission decided to extend the validity of the guidelines to 31 December 2000 <sup>(3)</sup>.
2. Since the guidelines were adopted in 1994, action in the field of the environment has evolved at the initiative of the Member States and the Community and at world level, in particular following the adoption of the Kyoto Protocol. Member States are granting State aid more frequently in the energy sector, for example, and the aid they provide is frequently in forms which have been rather uncommon until recently, such as tax reductions and exemptions. New forms of operating aid are also on the increase. The Commission ought therefore to adopt new guidelines, which will be needed in order to familiarise Member States and firms with the criteria that it will apply in deciding whether or not aid measures planned by the Member States are compatible with the common market.
3. Under Article 6 of the EC Treaty, environmental policy objectives must be integrated into the Commission's policy on aid controls in the environmental sector, in particular with a view to promoting sustainable development. Accordingly, competition policy and environmental policy are not mutually antagonistic, but the requirements of environmental protection need to be integrated into the definition and implementation of competition policy, in particular so as to promote sustainable development <sup>(4)</sup>.
4. However, taking long-term environmental requirements into account does not mean that all aid must be authorised. Consideration has to be given to the effects the aid may have in terms of sustainable development and full application of the 'polluter pays' principle. Some forms of aid certainly do satisfy these tests, particularly where they make it possible to achieve a high level of environmental protection while avoiding any conflict with the principle of the internalisation of costs. But other forms of aid, as well as having adverse effects on

trade between Member States and on competition, may run counter to the 'polluter pays' principle and may hinder the establishment of a process of sustainable development. This might be the case, for example, where aid is designed merely to facilitate compliance with new mandatory Community standards.

5. The Commission's approach in these guidelines therefore consists in determining whether, and under what conditions, State aid may be regarded as necessary to ensure environmental protection and sustainable development without having disproportionate effects on competition and economic growth. This analysis must be carried out in the light of the lessons that can be drawn from the functioning of the 1994 guidelines and in the light of the changes in environmental policy that have occurred since then.

### B. DEFINITIONS AND SCOPE

6. The concept of environmental protection: for the purposes of these guidelines, the Commission takes 'environmental protection' to mean any action designed to remedy or prevent damage to our physical surroundings or natural resources, or to encourage the efficient use of these resources.

The Commission regards energy-saving measures and the use of renewable sources of energy as action to protect the environment. Energy-saving measures should be understood as meaning among other things action which enables companies to reduce the amount of energy used in their production cycle. The design and manufacture of machines or means of transport which can be operated with fewer natural resources are not covered by these guidelines. Action taken within plants or other production units with a view to improving safety or hygiene is important and may be eligible for certain types of aid, but it is not covered by these guidelines.

The concept of the internalisation of costs: in these guidelines the 'internalisation of costs' means the principle that all costs associated with the protection of the environment should be included in firms' production costs.

The 'polluter pays' principle: this is the principle that the costs of measures to deal with pollution should be borne by the polluter who causes the pollution.

Polluter: a polluter is someone who directly or indirectly damages the environment or who creates conditions leading to such damage <sup>(5)</sup>.

<sup>(1)</sup> OJ C 72, 10.3.1994, p. 3.

<sup>(2)</sup> OJ C 14, 19.1.2000, p. 8.

<sup>(3)</sup> OJ C 184, 1.7.2000, p. 25.

<sup>(4)</sup> The Commission also set out its commitment to integrating environmental policy into other policy areas in its working paper of 26 May 1999 entitled 'Integrating environmental aspects into all relevant policy areas' and in its report to the Helsinki European Council on integrating environmental concerns and sustainable development into Community policies (SEC(1999) 1941 final).

<sup>(5)</sup> Council Recommendation of 3 March 1975 regarding cost allocation and action by public authorities on environmental matters (OJ L 194, 25.7.1975, p. 1).

Prices to reflect costs: this principle states that the prices of goods or services should incorporate the external costs associated with the negative impact on the environment of their production and marketing.

Community standard: mandatory Community standard setting the levels to be attained in environmental terms and the obligation under Community law to use the best available techniques (BAT) <sup>(6)</sup> which do not entail excessive costs.

Renewable energy sources: renewable non-fossil energy sources, viz. wind energy, solar energy, geothermal energy, wave energy, tidal energy, hydroelectric installations with a capacity below 10 MW and biomass, where biomass is defined as products from agriculture and forestry, vegetable waste from agriculture, forestry and the food production industry, and untreated wood waste and cork waste <sup>(7)</sup>.

Electric power generated from renewable energy sources: electric power generated by plant using only renewable energy sources, and that share of electric power generated from renewable energy sources in hybrid plant using traditional energy sources, in particular for contingency purposes <sup>(8)</sup>.

Environmental tax: 'One likely feature for a levy to be considered as *environmental* would be that the taxable base of the levy has a clear negative effect on the environment. However, a levy could also be regarded as environmental if it has a less clear, but nevertheless discernible positive environmental effect. [...] In general, it is up to the Member State to show the estimated environmental effect of the levy [...]'. <sup>(9)</sup>

<sup>(6)</sup> The concept of best available techniques was introduced into Community legislation by Council Directive 76/464/EEC of 4 May 1976 on pollution caused by certain dangerous substances discharged into the aquatic environment of the Community (OJ L 129, 18.5.1976, p. 23) and appeared again, in slightly amended form, in Council Directive 84/360/EEC of 28 June 1984 on the combating of air pollution from industrial plants (OJ L 188, 16.7.1984, p. 20). Council Directive 96/61/EEC of 24 September 1996 concerning integrated pollution prevention and control (OJ L 257, 10.10.1996, p. 26; 'the IPPC Directive') developed and confirmed this concept. The scope of the IPPC Directive covers industrial installations with a high pollution potential. The Directive has applied since November 1999 to new installations or existing installations which have undergone substantial changes. Existing installations must comply with the rules of the IPPC Directive by October 2007. Until that date the provisions of the two abovementioned directives relating to the concept of BAT continue to apply. As a rule, the concrete standards — i.e. the emission or consumption limit values based on the use of the best available techniques — are not set by the Community but by the national authorities.

<sup>(7)</sup> This definition is contained in the Commission proposal for a Parliament and Council Directive on the promotion of electricity from renewable sources in the internal electricity market (OJ C 311 E, 31.10.2000, p. 320). Once the Directive has been adopted by Parliament and the Council, the Commission will apply the definition given in the final text.

<sup>(8)</sup> Same observation as for footnote 7.

<sup>(9)</sup> Environmental taxes and charges in the single market (COM(97) 9 final, 26.3.1997).

7. Scope: These guidelines apply to aid <sup>(10)</sup> to protect the environment in all sectors governed by the EC Treaty, including those subject to specific Community rules on State aid (steel processing <sup>(11)</sup>, shipbuilding, motor vehicles, synthetic fibres, transport, and fisheries), but excluding the field covered by the Community guidelines for State aid in the agriculture sector <sup>(12)</sup>. These guidelines apply to fisheries and aquaculture, without prejudice to the application of the provisions set out in Council Regulation (EC) No 2792/99 of 17 December 1999 laying down the detailed rules and arrangements regarding Community structural assistance in the fisheries sector <sup>(13)</sup> and in the guidelines for examining State aid in the fisheries and aquaculture sector <sup>(14)</sup>. State aid for R & D in the environmental field is subject to the rules set out in the Community framework for State aid for research and development <sup>(15)</sup>. Similarly, the Commission considers that the characteristics of aid for environmental training activities do not justify such aid being treated separately, and it will therefore examine it in accordance with the provisions of Commission Regulation (EC) No 68/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to training aid <sup>(16)</sup>.

By virtue of Article 3 of Commission Decision No 2496/96/ECSC of 18 December 1996 establishing Community rules for State aid to the steel industry <sup>(17)</sup>, aid for environmental protection in the steel industry will continue to be analysed in accordance with the Community guidelines on State aid for environmental protection published in Official Journal C 72 of 10 March 1994 until the expiry of the ECSC Treaty.

These guidelines do not apply to stranded costs, which will be dealt with separately <sup>(18)</sup>. The Commission would point out that, by virtue of Commission Regulation (EC) No 69/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to *de minimis* <sup>(19)</sup> aid, aid of not more than EUR 100 000 granted to a firm for a period of three years is not caught by Article 87. That Regulation does not, however, apply to agriculture, fisheries, and transport, nor to the sectors covered by the ECSC Treaty.

<sup>(10)</sup> The purpose of these guidelines is not to discuss the concept of State aid, which derives from Article 87(1) of the EC Treaty and from the case law of the Court of Justice and the Court of First Instance.

<sup>(11)</sup> Within the limits laid down in the second paragraph of point 7.

<sup>(12)</sup> OJ C 28, 1.2.2000, p. 2.

<sup>(13)</sup> OJ L 337, 30.12.1999, p. 10.

<sup>(14)</sup> The Commission would point out that these guidelines concern only environmental aid, without prejudice to the applicability of other provisions governing State aid, subject to the limitations of the rules on combinations of aid in point 74 below.

<sup>(15)</sup> OJ C 45, 17.2.1996, p. 5.

<sup>(16)</sup> OJ L 10, 13.1.2001, p. 20.

<sup>(17)</sup> OJ L 338, 28.12.1996, p. 42.

<sup>(18)</sup> Stranded costs are costs which firms must bear because of commitments they made and are no longer able to honour as a result of the liberalisation of the sector in question.

<sup>(19)</sup> OJ L 10, 13.1.2001, p. 30.

### C. POLICY FOR CONTROLLING STATE AID AND ENVIRONMENTAL POLICY

8. During the 1970s and 1980s Community policy on the environment took an essentially corrective approach. The emphasis was on standards intended to reflect the main concerns of environmental policy.
9. The fifth action programme on the environment, entitled 'Towards sustainability' and adopted in 1993 <sup>(20)</sup>, represents something of a break with that approach. It emphasises the need to conduct a long-term policy with the aim of promoting sustainable development. The objective is to reconcile on a lasting basis the development of the European economy with the need to protect the environment. Community action must no longer be limited to reacting to environmental problems but, as explicitly provided for in Article 6 of the EC Treaty as amended by the Treaty of Amsterdam, environmental protection requirements must be integrated into the definition and implementation of all Community policies and activities, and must foster the active involvement of socio-economic operators.
10. Article 174 of the Treaty also provides for Community policy to be based on the 'polluter pays' principle. The costs associated with protecting the environment should be internalised by firms just like other production costs. In order to implement this policy, the Community will have to use a series of instruments: regulation, and in particular the adoption of standards, but also voluntary agreements or economic instruments.
11. In 1996 the Commission drew up a progress report on the fifth action programme on the environment. The report states that the programme's overall strategy and objectives are still valid. There can be no doubt that progress has been made in integrating environmental and sustainability aspects into the other Community policies. However, what has still not occurred is a genuine change in attitude on the part of all the interested parties: policymakers, firms and the general public. It is important to develop the concept of shared responsibility for the environment and to make the general public aware of the issues at stake.
12. In 1999 the Commission adopted a global assessment of the fifth action programme. The assessment noted that, although the programme raised awareness of the need for stakeholders, citizens and decision-makers in other sectors to pursue environmental objectives actively, less progress had been made overall in changing economic trends and modes of conduct which were harmful to the environment.
13. The assessment also noted that 'it is increasingly clear that damages to the environment have costs to society as a whole and, conversely, that environmental action can generate benefits in the form of economic growth, employment and competitiveness' and that 'the effective application of the "polluter pays" principle and the full internalisation of environmental costs onto polluters remains a critical process' <sup>(21)</sup>.
14. The Commission's policy on the control of State aid for environmental purposes therefore needs to satisfy a double imperative:
- (a) to ensure the competitive functioning of markets, while promoting the completion of the single market and increased competitiveness in firms;
  - (b) to ensure that the requirements of environmental protection are integrated into the definition and implementation of competition policy, in particular in order to promote sustainable development. The Commission here believes that internalisation of costs is a priority objective that can be achieved in various ways, including by way of instruments based on market laws or those based on a regulatory approach, these being the most effective tools for achieving the objectives described above.
15. Cost internalisation helps to ensure that prices accurately reflect costs in so far as economic operators allocate their financial resources on the basis of the prices of the goods and services they wish to buy. The progress report on the fifth programme emphasises that this aim has not been realised because prices do not reflect ecological costs. This in turn makes it more difficult to raise public awareness and promotes overexploitation of natural resources.
16. Ensuring that prices reflect costs at all stages of the economic process is the best way of making all parties aware of the cost of protecting the environment. Apart from its potentially adverse effects on trade and competition, State aid generally undermines that aim because it enables certain firms to reduce costs artificially and not to reveal the costs of environmental protection to consumers. In the long term, therefore, some forms of State aid run counter to the objectives of sustainable development.
17. The Community guidelines on State aid adopted by the Commission in 1994 form an integral part of this Community policy. In general, the 'polluter pays' principle and the need for firms to internalise the costs associated with protecting the environment would appear to militate against the granting of State aid.
18. Nevertheless, the guidelines state that aid can be justified in two instances:
- (a) in certain specific circumstances in which it is not yet possible for all costs to be internalised by firms and the aid can therefore represent a **temporary second-best solution** by encouraging firms to adapt to standards;

<sup>(20)</sup> OJ C 138, 17.5.1993, p. 1.

<sup>(21)</sup> Europe's environment: what directions for the future? The global assessment of the European Community programme of policy and action in relation to the environment and sustainable development, 'Towards sustainability' (COM(1999) 543 final of 24.11.1999).

- (b) the aid may also act as an **incentive** to firms to improve on standards or to undertake further investment designed to reduce pollution from their plants.
19. In the Community guidelines adopted in 1994, the Commission took the view that, in certain cases, total cost internalisation was not yet possible and that aid might be necessary on a temporary basis. The following changes have nevertheless taken place since 1994:
- (a) since the adoption of the fifth action programme on the environment, which was already based on the 'polluter pays' principle and cost internalisation, firms have had seven years in which to adapt to the gradual application of the principle;
- (b) the Commission's 1996 progress report on the fifth action programme and the 1999 evaluation report restate the need to provide for cost internalisation and to use market instruments in order to make significant progress in improving the environment;
- (c) the use of market instruments and proper pricing is also advocated by the Kyoto Protocol on climate change.
20. The Commission's position is therefore that aid should no longer be used to make up for the absence of cost internalisation. If environmental requirements are to be taken into account in the long term, prices must accurately reflect costs and environmental protection costs must be fully internalised. Consequently, the Commission takes the view that aid is not justified in the case of investments designed merely to bring companies into line with new or existing Community technical standards. In its view, however, in order to address the special difficulties encountered by SMEs, it should be possible to grant them aid for adapting to new Community standards for a period of three years from the adoption of such standards. Aid may though be useful where it serves as an incentive to achieve levels of protection which are higher than those required by Community standards. This is the case when a Member State decides to adopt standards which are more stringent than the Community standards so as to achieve a higher level of environmental protection. It will also apply when a firm invests in environmental protection over and above the strictest existing Community standards or where no Community standards exist.
21. However, it has not been shown that aid has an incentive effect of this kind where it is designed merely to help firms to comply with existing or new Community technical standards. Such standards constitute the ordinary law with which firms must comply, and it is not necessary to provide them with aid in order to encourage them to obey the law <sup>(22)</sup>.

### Specific case of the energy sector and tax reductions

22. Since the guidelines were adopted in 1994, the energy sector has undergone major changes which need to be taken into consideration.
23. Certain Member States have adopted, are in the process of adopting or might consider adopting taxes the effects of which are conducive to environmental protection. In some cases, exemptions from or reductions in taxes are granted to firms in particular categories in order to avoid placing them in a difficult competitive situation. The Commission takes the view that such measures may constitute State aid within the meaning of Article 87 of the Treaty. However, the adverse effects of such aid can be offset by the positive effects of adopting taxes. Accordingly, if such exemptions are necessary to ensure the adoption or continued application of taxes applicable to all products, the Commission takes the view that they are acceptable, subject to certain conditions and for a limited period of time. This period may last for 10 years if the conditions are met. Thereafter, Member States will remain free to renotify the measures in question to the Commission, which could adopt the same approach in its analysis while taking into consideration the positive results obtained in environmental terms.
24. Member States have also taken action in recent years to promote the use of renewable sources of energy and combined heat and energy production, which has the encouragement of the Commission given the major advantages for the environment. The Commission therefore takes the view that, where measures to promote renewable sources of energy and the combined production of electric power and heat constitute State aid, they are acceptable subject to certain conditions. It must be certain, however, that such aid is not in breach of other provisions of the Treaty or secondary legislation.

### D. RELATIVE IMPORTANCE OF ENVIRONMENTAL AID

25. The data in the eighth survey on State aid in the European Union in the manufacturing and certain other sectors <sup>(23)</sup> show that between 1996 and 1998 environmental aid accounted on average for only 1,85 % of total aid granted to the manufacturing and service sectors.
26. In the period 1994-1999 environmental aid was provided predominantly in the form of grants. Proportionally speaking, little use was made of the other forms of aid: low-interest loans, State guarantees, etc.
27. As to the sectors receiving aid, the period 1998-1999 saw an increase in aid for measures in the energy sector, whether in support of energy saving or to promote the use of new or renewable sources of energy, especially in the form of ecotaxes.

<sup>(22)</sup> With the exception of SMEs, as provided for in point 20.

<sup>(23)</sup> COM(2000) 205 final, 11.4.2000.

## E. GENERAL CONDITIONS FOR AUTHORISING ENVIRONMENTAL AID

### E.1. Investment aid

#### E.1.1. *Transitional investment aid to help SMEs adapt to new Community standards*

28. For a period of three years from the adoption of new compulsory Community standards, investment aid to help SMEs meet new standards may be authorised up to a maximum of 15 % gross of eligible costs.

#### E.1.2. *General conditions for authorising investment aid to firms improving on Community standards*

29. Investment aid enabling firms to improve on the Community standards applicable may be authorised up to not more than 30 % gross of the eligible investment costs as defined in point 37. These conditions also apply to aid where firms undertake investment in the absence of mandatory Community standards or where they have to undertake investment in order to comply with national standards that are more stringent than the applicable Community standards.

#### E.1.3. *Investment in energy*

30. Investments in energy saving as defined in point 6 are deemed equivalent to investments to promote environmental protection. Such investments play a major role in achieving economically the Community objectives for the environment<sup>(24)</sup>. They are, therefore, eligible for investment aid at the basic rate of 40 % of eligible costs.

31. Investments in the combined production of electric power and heat may also qualify under these guidelines if it can be shown that the measures beneficial in terms of the protection of the environment because the conversion efficiency<sup>(25)</sup> is particularly high, because the measures will allow energy consumption to be reduced or because the production process will be less damaging to the environment. In this connection, the Commission will take into particular consideration the type of primary energy used in the production process. It should also be borne in mind that increased energy use from combined production of heat and power is a Community priority for the environment<sup>(26)</sup>. Such investment may, therefore, be given aid at the basic rate of 40 % of eligible cost.

<sup>(24)</sup> Action plan to improve energy efficiency in the European Community (COM (2000) 247 final, 26.4.2000).

<sup>(25)</sup> By 'conversion efficiency' is meant the ratio between the quantity of primary energy used to produce a secondary form of energy and the quantity of secondary energy actually produced. It is calculated as follows: electric energy produced + thermal energy produced/energy used.

<sup>(26)</sup> Council Resolution of 18 December 1997 on a Community strategy to promote combined heat and power (OJ C 4, 8.1.1998, p. 1).

32. Investments to promote renewable sources of energy are deemed equivalent to environmental investments undertaken in the absence of mandatory Community standards. It should also be borne in mind that measures in support of renewable sources of energy are one of the Community's environmental priorities<sup>(27)</sup> and one of the long-term objectives that should be encouraged most. The rate of aid for investment in support of these forms of energy is therefore 40 % of eligible costs.

The Commission takes the view that renewable energy installations serving all the needs of an entire community such as an island or residential area should also benefit. Investments made in this connection may qualify for a bonus of 10 percentage points on top of the basic rate of 40 % of eligible costs.

The Commission considers that, where it can be shown to be necessary, Member States will be able to grant investment aid to support renewable energy, up to 100 % of eligible costs. The installations concerned will not be entitled to receive any further support.

#### E.1.4. *Bonus for firms located in assisted regions*

33. In regions which are eligible for national regional aid, firms may receive aid to promote regional development. To encourage them to invest further in the environment, it should be possible, where appropriate, to provide additional aid towards any environmental investment carried out in accordance with point 29<sup>(28)</sup>.

34. Consequently, in regions eligible for regional aid, the maximum rate of environmental aid applicable to eligible costs as defined in point 37 below is determined as follows.

In assisted regions the maximum rate of aid applicable is the higher of the following two options:

(a) either the basic rate for environmental investment aid, i.e. 30 % gross (standard system), 40 % gross (investments in energy saving, in renewable sources of energy or to promote the combined production of electric power and heat) or 50 % gross (investments in renewable sources of energy that supply an entire community), plus 5 percentage points gross in the regions covered by Article 87(3)(c) and 10 percentage points in the regions covered by Article 87(3)(a)<sup>(29)</sup>;

<sup>(27)</sup> Council Resolution of 8 June 1998 on renewable sources of energy (OJ C 198, 24.6.1998, p. 1).

<sup>(28)</sup> These bonuses are not available where the Member State grants investment aid in accordance with the third paragraph of point 32 (aid of up to 100 % of eligible costs).

<sup>(29)</sup> Investments in assisted regions are eligible for investment aid if the conditions of the guidelines on regional State aid (OJ C 74, 10.3.1998, p. 9) are met.

- (b) or the regional aid rate plus 10 percentage points gross.

#### E.1.5. *Bonus for SMEs*

35. Where investments of the kind referred to in points 29 to 32 are carried out by small or medium-sized enterprises, an increase of 10 percentage points gross may be authorised<sup>(30)</sup>. For the purposes of these guidelines, the definition of SMEs is that given by the relevant Community texts<sup>(31)</sup>.

The above bonuses for assisted regions and SMEs may be combined, but the maximum rate of environmental aid may never exceed 100 % gross of the eligible costs. SMEs do not qualify for a double bonus either under the provisions applicable to regional aid or under those applicable in the environmental field<sup>(32)</sup>.

#### E.1.6. *The investments concerned*

36. The investments concerned are investments in land which are strictly necessary in order to meet environmental objectives, investments in buildings, plant and equipment intended to reduce or eliminate pollution and nuisances, and investments to adapt production methods with a view to protecting the environment.

Spending on technology transfer through the acquisition of operating licences or of patented and non-patented know-how may also qualify. But any such intangible asset must satisfy the following tests:

- (a) it must be regarded as a depreciable asset;
- (b) it must be purchased on market terms, from a firm in which the acquirer has no power of direct or indirect control;
- (c) it must be included in the assets of the firm, and remain in the establishment of the recipient of the aid and be used there for at least five years. This condition does not apply if these intangible assets are technically out of date. If it is sold during those five years, the yield from the sale must be deducted from the eligible costs and all or part of the amount of aid must, where appropriate, be reimbursed.

<sup>(30)</sup> This bonus is not available where the Member State grants investment aid in accordance with the third paragraph of point 32 (aid of up to 100 % of eligible costs).

<sup>(31)</sup> Commission Recommendation 96/280/EC of 3 April 1996 concerning the definition of small and medium-sized enterprises (OJ L 107, 30.4.1996, p. 4).

<sup>(32)</sup> Investments by SMEs are eligible for investment aid under the provisions of Commission Regulation (EC) No 70/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to State aid for small and medium-sized enterprises (OJ L 10, 13.1.2001, p. 33).

#### E.1.7. *Eligible costs*

37. Eligible costs must be confined strictly to the extra investment costs necessary to meet the environmental objectives.

This has the following consequences: where the cost of investment in environmental protection cannot be easily identified in the total cost, the Commission will take account of objective and transparent methods of calculation, e.g. the cost of a technically comparable investment that does not though provide the same degree of environmental protection.

In all cases, eligible costs must be calculated net of the benefits accruing from any increase in capacity, cost savings engendered during the first five years of the life of the investment and additional ancillary production during that five-year period<sup>(33)</sup>.

For renewable energy, eligible investment costs are normally the extra costs borne by the firm compared with a conventional power plant with the same capacity in terms of the effective production of energy.

Where SMEs adapt to new Community standards, eligible costs include additional investments needed to attain the level of environmental protection required by those standards.

Where the firm is adapting to national standards adopted in the absence of Community standards, the eligible costs consist of the additional investment costs necessary to achieve the level of environmental protection required by the national standards.

Where the firm is adapting to national standards which are more stringent than the Community standards or undertakes a voluntary improvement on Community standards, the eligible costs consist of the additional investment costs necessary to achieve a level of environmental protection higher than the level required by the Community standards. The cost of investments needed to reach the level of protection required by the Community standards is not eligible.

Where no standards exist, eligible costs consist of the investment costs necessary to achieve a higher level of environmental protection than that which the firm or firms in question would achieve in the absence of any environmental aid.

<sup>(33)</sup> If the investments are concerned solely with environmental protection without any other economic benefits, no additional reduction will be applied in determining the eligible costs.

### E.1.8. *Rehabilitation of polluted industrial sites*

38. Interventions made by firms repairing environmental damage by rehabilitating polluted industrial sites may come within the scope of these guidelines<sup>(34)</sup>. The environmental damage concerned may be damage to the quality of the soil or of surface water or groundwater<sup>(35)</sup>.

Where the person responsible for the pollution is clearly identified, that person must finance the rehabilitation in accordance with the 'polluter pays' principle, and no State aid may be given. By 'person responsible for the pollution' is meant the person liable under the law applicable in each Member State, without prejudice to the adoption of Community rules in the matter.

Where the person responsible for the pollution is not identified or cannot be made to bear the cost, the person responsible for the work may receive aid<sup>(36)</sup>.

Aid for the rehabilitation of polluted industrial sites may amount to up to 100 % of the eligible costs, plus 15 % of the cost of the work. The eligible costs are equal to the cost of the work less the increase in the value of the land.

The total amount of aid may under no circumstances exceed the actual expenditure incurred by the firm.

### E.1.9. *Relocation of firms*

39. The Commission takes the view that as a rule the relocation of firms to new sites does not constitute environmental protection and does not therefore give entitlement to aid under these guidelines.

The granting of aid may, however, be justified when a firm established in an urban area or in a Natura 2000 designated area lawfully carries on an activity that creates major pollution and must, on account of this location, move from its place of establishment to a more suitable area.

All the following criteria must be satisfied at the same time:

(a) The change of location must be dictated on environmental protection grounds and must have been ordered by administrative or judicial decision.

<sup>(34)</sup> The Commission would point out that rehabilitation work carried out by public authorities is not as such caught by Article 87 of the Treaty. Problems of State aid may, however, arise if the land is sold after rehabilitation at a price below its market value.

<sup>(35)</sup> All expenditure incurred by a firm in rehabilitating its site, whether or not such expenditure can be shown as a fixed asset on its balance sheet, ranks as eligible investment in the case of the rehabilitation of polluted sites.

<sup>(36)</sup> The person responsible for performing the work need not necessarily be the person responsible for the pollution in the meaning in which that expression is used here.

(b) The firm must comply with the strictest environmental standards applicable in the new region where it is located.

A firm satisfying the above conditions may receive investment aid in accordance with point 29. The provisions of point 35 concerning the granting of a bonus for SMEs will apply.

In order to determine the amount of eligible costs in the case of relocation aid, the Commission will take into account the yield from the sale or renting of the plant or land abandoned, the compensation paid in the event of expropriation and the costs connected with the purchase of land or the construction or purchase of new plant of the same capacity as the plant abandoned. Account may also be taken of any other gains connected with the transfer of the plant, notably gains resulting from an improvement, on the occasion of the transfer, in the technology used and accounting gains associated with better use of the plant. Investments relating to any capacity increase may not be taken into consideration in calculating the eligible costs conferring entitlement to the granting of environmental aid.

If the administrative or judicial decision ordering the change of location results in the early termination of a contract for the renting of land or buildings, any penalties imposed on the firm for having terminated the contract may be taken into consideration in calculating the eligible costs.

### E.1.10. *Common rules*

40. Aid for investment to improve on Community standards or undertaken where no Community standards exist may not be granted where such improvements merely bring companies into line with Community standards already adopted but not yet in force. A firm may be given aid to enable it to comply with national standards which are more stringent than Community standards or where no Community standards exist only if it complies with the national standards by the final date laid down in the relevant national measures. Investments carried out after that date do not qualify<sup>(37)</sup>.

### E.2. *Aid to SMEs for advisory/consultancy services in the environmental field*

41. Advisory/consultancy services play an important part in helping SMEs to make progress in environmental protection. The Commission therefore takes the view that aid may be granted under the provisions of Regulation (EC) No 70/200138<sup>(38)</sup>.

<sup>(37)</sup> The rules set out in this point are without prejudice to point 28 concerning aid for SMEs.

<sup>(38)</sup> Reference given in footnote 32.

### E.3. Operating aid

#### E.3.1. Rules applicable to all operating aid to promote waste management and energy saving

42. The following rules apply to two types of operating aid, namely:

(a) aid for the management of waste where such management is in line with the hierarchical classification of the principles of waste management <sup>(39)</sup>;

(b) aid in the energy-saving field.

43. Where such aid is shown to be absolutely necessary, it should be strictly limited to compensating for extra production costs by comparison with the market prices of the relevant products or services <sup>(40)</sup>. Such aid must also be temporary and, as a general rule, must be wound down over time, so as to provide an incentive for prices to reflect costs reasonably rapidly.

44. The Commission takes the view that firms should normally bear the costs of treating industrial waste in accordance with the 'polluter pays' principle. However, operating aid may be necessary where national standards are introduced which are more stringent than the applicable Community rules, or where national standards are introduced in the absence of Community rules, so that firms temporarily lose competitiveness at international level.

Firms receiving operating aid towards the treatment of industrial or non-industrial waste must finance the service provided in proportion to the amount of waste they produce and/or the cost of treatment.

45. All such operating aid is subject to a limited duration of five years where the aid is 'degressive'. Its intensity may amount to 100 % of the extra costs in the first year but must have fallen in a linear fashion to zero by the end of the fifth year.

46. In the case of 'non-degressive' aid, its duration is limited to five years and its intensity must not exceed 50 % of the extra costs.

<sup>(39)</sup> Classification given in the Community strategy for waste management (COM(96) 399 final of 30.7.1996). In this communication, the Commission recalls that waste management is a priority objective for the Community in order to reduce the risks to the environment. The concept of waste treatment must be looked at from three angles: re-utilisation, recycling and recovery. Waste whose production is unavoidable must be treated and eliminated without danger.

<sup>(40)</sup> The concept of production costs must be understood as being net of any aid but inclusive of a normal level of profit.

#### E.3.2. Rules applicable to all operating aid in the form of tax reductions or exemptions

47. When adopting taxes that are to be levied on certain activities for reasons of environmental protection, Member States may deem it necessary to make provision for temporary exemptions for certain firms notably because of the absence of harmonisation at European level or because of the temporary risks of a loss of international competitiveness. In general, such exemptions constitute operating aid caught by Article 87 of the EC Treaty. In analysing these measures, it has to be ascertained among other things whether the tax is to be levied as the result of a Community decision or an autonomous decision on the part of a Member State.

48. If the tax is to be levied as the result of an autonomous decision on the part of a Member State, the firms affected may have some difficulty in adapting rapidly to the new tax burden. In such circumstances there may be justification for a temporary exemption enabling certain firms to adapt to the new situation.

49. If the tax is to be levied as the result of a Community directive, there are two possible scenarios:

(a) a Member State applies tax to certain products at a rate higher than the minimum rate laid down in the Community directive and grants an exemption to certain firms, which, as a result, pay tax at a rate which is lower but nevertheless at least equal to the minimum rate set by the directive. The Commission takes the view that, in those circumstances, a temporary exemption may be justified to enable firms to adapt to higher taxation and to provide them with an incentive to act in a more environmentally friendly manner;

(b) a Member State applies tax to certain products at the minimum rate laid down in the Community directive and grants an exemption to certain firms, which are thus subject to taxation at a rate below the minimum rate. If such an exemption is not authorised by the directive in question, it will constitute aid which is incompatible with Article 87 of the Treaty. If it is authorised by the directive, the Commission may take the view that it is compatible with Article 87 in so far as it is necessary and is not disproportionate in the light of the Community objectives pursued. The Commission will be specially concerned to ensure that any such exemption is strictly limited in time.

50. In general, the tax measures in question should make a significant contribution to protecting the environment. Care should be taken to ensure that the exemptions do not, by their very nature, undermine the general objectives pursued.

51. These exemptions can constitute operating aid which may be authorised on the following conditions:

1. When, for environmental reasons, a Member State introduces a **new tax** in a sector of activity or on products in respect of which no Community tax harmonisation has been carried out or when the tax envisaged by the Member State exceeds that laid down by Community legislation, the Commission takes the view that exemption decisions covering a 10-year period with no degressivity may be justified in two cases:

(a) these exemptions are conditional on the conclusion of agreements between the Member State concerned and the recipient firms whereby the firms or associations of firms undertake to achieve environmental protection objectives during the period for which the exemptions apply or when firms conclude voluntary agreements which have the same effect. Such agreements or undertakings may relate, among other things, to a reduction in energy consumption, a reduction in emissions or any other environmental measure. The substance of the agreements must be negotiated by each Member State and will be assessed by the Commission when the aid projects are notified to it. Member States must ensure strict monitoring of the commitments entered into by the firms or associations of firms. The agreements concluded between a Member State and the firms concerned must stipulate the penalty arrangements applicable if the commitments are not met.

These provisions also apply where a Member State makes a tax reduction subject to conditions that have the same effect as the agreements or commitments referred to above;

(b) these exemptions need not be conditional on the conclusion of agreements between the Member State concerned and the recipient firms if the following alternative conditions are satisfied:

— where the reduction concerns a Community tax, the amount effectively paid by the firms after the reduction must remain higher than the Community minimum in order to provide the firms with an incentive to improve environmental protection,

— where the reduction concerns a domestic tax imposed in the absence of a Community tax, the firms eligible for the reduction must nevertheless pay a significant proportion of the national tax.

2. The provisions in point 51.1 may be applied to existing taxes if the following two conditions are satisfied at the same time:

(a) the tax in question must have an appreciable positive impact in terms of environmental protection;

(b) the derogations for the firms concerned must have been decided on when the tax was adopted or must have become necessary as a result of a significant change in economic conditions that placed the firms in a particularly difficult competitive situation. In the latter instance, the amount of the reduction may not exceed the increase in costs resulting from the change in economic conditions. Once there is no longer any increase in costs, the reduction must no longer apply.

3. Member States may also encourage the development of processes for producing electric power from conventional energy sources such as gas that have an energy efficiency very much higher than the energy efficiency obtained with conventional production processes. In such cases, given the importance of such techniques for environmental protection and provided that the primary energy used reduces significantly the negative effects in terms of environmental protection, the Commission takes the view that total exemptions from taxes may be justified for a period of five years where aid is non-degressive. Derogations for 10 years may also be granted in accordance with the conditions set out in points 51.1 and 51.2.

52. Where an existing tax is increased significantly and where the Member State concerned takes the view that derogations are needed for certain firms, the conditions set out in point 51.1 as regards new taxes are applicable by analogy.

53. When the reductions concern a tax that has not been harmonised at Community level and when the domestic tax is lower than or equal to the Community minimum, the Commission takes the view that long-term exemptions are not justified. In this case, any exemptions granted must satisfy the conditions laid down in points 45 and 46 and must, in any event, be covered by an express authorisation to derogate from the Community minimum.

In all cases of reduction of tax, the Member State may grant operating aid in accordance with points 45 and 46.

#### **E.3.3. Rules applicable to operating aid for renewable energy sources**

54. As regards the production of renewable energy, operating aid will usually be allowable under these guidelines.

55. The Commission takes the view that such aid qualifies for special treatment because of the difficulties these sources of energy have sometimes encountered in competing effectively with conventional sources. It must also be borne in mind that it is Community policy to encourage the development of these sources of energy, notably on environmental grounds. Aid may be necessary in particular where the technical processes available do not allow energy to be produced at unit costs comparable to those of conventional sources.
56. Operating aid may be justified here in order to cover the difference between the cost of producing energy from renewable energy sources and the market price of that energy. The form of such aid may vary depending on the kind of energy involved and the support mechanism worked out by the Member State. Moreover, when studying cases, the Commission will take account of the competitive position of each form of energy involved.
57. Member States may grant aid for renewable energy sources as follows:

#### E.3.3.1. Option 1

58. In the renewable energy field, unit investment costs are particularly high and generally account for a significant proportion of firms' costs and do not allow firms to charge competitive prices on the markets where they sell energy.
59. In order to take better account of this market-access barrier for renewable energies, Member States may grant aid to compensate for the difference between the production cost of renewable energy and the market price of the form of power concerned. Any operating aid may then be granted only for plant depreciation. Any further energy produced by the plant will not qualify for any assistance. However, the aid may also cover a fair return on capital if Member States can show that this is indispensable given the poor competitiveness of certain renewable energy sources.

In determining the amount of operating aid, account should also be taken of any investment aid granted to the firm in question in respect of the new plant.

When notifying aid schemes to the Commission, Member States must state the precise support mechanisms and in particular the methods of calculating the amount of aid. If the Commission authorises the scheme, the Member State must then apply those mechanisms and methods of calculation when it comes to granting aid to firms.

60. Unlike most other renewable sources of energy, biomass requires relatively less investment but brings higher

operating costs. The Commission will, therefore, be amenable to operating aid exceeding the amount of investment where Member States can show that the aggregate costs borne by the firms after plant depreciation are still higher than the market prices of the energy.

#### E.3.3.2. Option 2

61. Member States may grant support for renewable energy sources by using market mechanisms such as green certificates or tenders. These systems allow all renewable energy producers to benefit indirectly from guaranteed demand for their energy, at a price above the market price for conventional power. The price of these green certificates is not fixed in advance but depends on supply and demand.
62. Where they constitute State aid, these systems may be authorised by the Commission if Member States can show that support is essential to ensure the viability of the renewable energy sources concerned, does not in the aggregate result in overcompensation for renewable energy and does not dissuade renewable energy producers from becoming more competitive. With a view to verifying that these criteria are met, the Commission intends to authorise these aid systems for a period of ten years, after which it will have to be assessed whether the support measure needs to be continued.

#### E.3.3.3. Option 3

63. Member States may grant operating aid to new plants producing renewable energy that will be calculated on the basis of the external costs avoided. These are the environmental costs that society would have to bear if the same quantity of energy were produced by a production plant operating with conventional forms of energy. They will be calculated on the basis of the difference between, on the one hand, the external costs produced and not paid by renewable energy producers and, on the other hand, the external costs produced and not paid by non-renewable energy producers. To carry out these calculations, the Member State will have to use a method of calculation that is internationally recognised and has been communicated to the Commission. It will have to provide among other things a reasoned and quantified comparative cost analysis, together with an assessment of competing energy producers' external costs, so as to demonstrate that the aid does genuinely compensate for external costs not covered.

At any event, the amount of the aid thus granted to the renewable energy producer must not exceed EUR 0,05 per kWh.

Furthermore, the amount of aid granted to producers that exceeds the amount of aid resulting from option 1 must be reinvested by the firms in renewable sources of energy. It will be taken into account by the Commission if this activity also qualifies for State aid.

64. If Option 3 is to remain consistent with the general rules on competition, the Commission must be certain that the aid does not give rise to any distortion of competition contrary to the common interest. In other words, it must be certain that the aid will result in an actual overall increase in the use of renewable energy sources at the expense of conventional energy sources, and not in a simple transfer of market shares between renewable energy sources. The following conditions will therefore have to be met:

- aid granted under this option must form part of a scheme which treats firms in the renewable energy sector on an equal footing;
- the scheme must provide for aid to be granted without discrimination as between firms producing the same renewable energy;
- the scheme must be re-examined by the Commission every five years.

#### E.3.3.4. Option 4

65. Member States may still grant operating aid in accordance with the general rules governing such aid in points 45 and 46.

#### E.3.4. Rules applicable to operating aid for the combined production of electric power and heat

66. The Commission takes the view that operating aid for the combined production of electric power and heat may be justified provided that the conditions set out in point 31 are met. Such aid may be granted to firms distributing electric power and heat to the public where the costs of producing such electric power or heat exceed its market price. In similar circumstances, operating aid may be granted in accordance with the rules in points 58 to 65. The decision as to whether the aid is essential will take account of the costs and revenue resulting from the production and sale of the electric power or heat.

67. Operating aid may be granted on the same conditions as for the industrial use of the combined production of electric power and heat where it can be shown that the production cost of one unit of energy using that technique exceeds the market price of one unit of conventional energy. The production cost may include the plant's normal return on capital, but any gains by the firm in terms of heat production must be deducted from production costs.

#### F. POLICIES, MEASURES AND INSTRUMENTS FOR REDUCING GREENHOUSE GASES

68. The Kyoto Protocol, signed by the Member States and by the Community, provides that the parties undertake to limit or reduce greenhouse gas emissions during the period 2008-2012. For the Community as a whole, the

target is to reduce greenhouse gas emissions by 8 % of their 1990 level.

69. Member States and the Community, as parties to the Protocol, will have to achieve the greenhouse gas reductions by means of common and coordinated policies and measures<sup>(41)</sup>, including economic instruments, and also by means of the instruments established by the Kyoto Protocol itself, namely international emissions trading, joint implementation, and the clean development mechanism.

70. In the absence of any Community provisions in this area and without prejudice to the Commission's right of initiative in proposing such provisions, it is for each Member State to formulate the policies, measures and instruments it wishes to adopt in order to comply with the targets set under the Kyoto Protocol.

71. The Commission takes the view that some of the means adopted by Member States to comply with the objectives of the Protocol could constitute State aid but it is still too early to lay down the conditions for authorising any such aid.

#### G. BASIS OF EXEMPTION FOR ALL PROJECTS EXAMINED BY THE COMMISSION

72. Subject to the limits and conditions set out in these guidelines, environmental aid will be authorised by the Commission pursuant to Article 87(3)(c) of the EC Treaty for 'aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest'.

73. Aid to promote the execution of important projects of common European interest which are an environmental priority and will often have beneficial effects beyond the frontiers of the Member State(s) concerned can be authorised under the exemption provided for in Article 87(3)(b) of the EC Treaty. However, the aid must be necessary for the project to proceed, and the project must be specific, well defined and qualitatively important and must make an exemplary and clearly identifiable contribution to the common European interest. When this exemption is applied, the Commission may authorise aid at higher rates than the limits laid down for aid authorised pursuant to Article 87(3)(c).

#### H. OVERLAPPING AID FROM DIFFERENT SOURCES

74. The aid ceilings stipulated in these guidelines are applicable irrespective of whether the aid in question is financed wholly or in part from State resources or from Community resources. Aid authorised under these guidelines may not be combined with other forms of State aid within the meaning of Article 87(1) of the Treaty or with other forms of Community financing if such overlapping produces an aid intensity higher than that laid down in these guidelines.

<sup>(41)</sup> For details of common and coordinated policies and measures see in particular 'Preparing for Implementation of the Kyoto Protocol' (COM(1999) 230 of 19.5.1999).

In the case of aid serving different purposes and involving the same eligible costs, the most favourable aid ceiling will apply.

#### I. 'APPROPRIATE MEASURES' WITHIN THE MEANING OF ARTICLE 88(1) OF THE EC TREATY

75. Acting under Article 88(1) of the Treaty, the Commission will propose the following appropriate measures to the Member States in respect of their existing systems of aid.
76. In order to enable it to assess any substantial amounts of aid granted under authorised schemes and to decide whether such aid is compatible with the common market, the Commission will propose, as an appropriate measure under Article 88(1) of the Treaty, that Member States should notify it in advance of any individual case of investment aid granted under an authorised scheme where the eligible costs exceed EUR 25 million and where the aid exceeds the gross grant equivalent of EUR 5 million. Notification will be given by means of the form of which a model is shown in the Annex.
77. The Commission will also propose, as an appropriate measure under Article 88(1), that Member States should bring their existing environmental aid schemes into line with these guidelines before 1 January 2002.
78. The Commission will ask the Member States to confirm within one month of receipt of the proposed measures referred to in points 75 to 77 that they agree to the proposals. In the absence of any reply, the Commission will take it that the relevant Member State does not agree.
79. The Commission would point out that, with the exception of aid classed as *de minimis* aid under Regulation (EC) No 69/2001<sup>(42)</sup>, these guidelines do not affect the obligation incumbent on Member States under Article 88(3) of the Treaty to notify any aid schemes, any changes to those schemes and any individual aid granted to firms outside the framework of authorised schemes.
80. The Commission intends to ensure that any authorisation for a future scheme complies with these guidelines.

#### J. APPLICATION OF THE GUIDELINES

81. These guidelines will become applicable when they are published in the *Official Journal of the European Communities*. They will cease to be applicable on 31 December 2007. After consulting the Member States, the Commission may amend them before that date on the basis of important competition policy or environmental policy considerations or in order to take account of other Community policies or international commitments.
82. The Commission will apply these guidelines to all aid projects notified in respect of which it is called upon to take a decision after the guidelines are published in the *Official Journal*, even where the projects were notified prior to their publication.

In the case of non-notified aid, the Commission will apply:

- (a) these guidelines if the aid was granted after their publication in the *Official Journal of the European Communities*;
- (b) the guidelines in force when aid is granted in all other cases.

#### K. INTEGRATION OF ENVIRONMENTAL POLICY INTO OTHER STATE AID GUIDELINES

83. Article 6 of the Treaty states that:

'Environmental protection requirements must be integrated into the definition and implementation of the Community policies and activities referred to in Article 3, in particular with a view to promoting sustainable development.'

When the Commission adopts or revises other Community guidelines or frameworks on State aid, it will consider how those requirements can best be taken into account. It will also examine whether it would not be expedient to ask the Member States to provide an environmental impact study whenever they notify it of an important aid project, irrespective of the sector involved.

<sup>(42)</sup> OJ L 10, 13.1.2001, p. 30.

## ANNEX

**ADDITIONAL INFORMATION ORDINARILY TO BE SUPPLIED WHEN NOTIFYING STATE AID FOR ENVIRONMENTAL PURPOSES UNDER ARTICLE 88(3) OF THE TREATY****(Schemes, cases of aid granted under an approved scheme, and one-off aid measures)**

To be attached to the general questionnaire in Section A of Annex II to the Commission letter to Member States of 2 August 1995 on notifications and standardised annual reports:

## 1. Objectives.

Detailed description of the objectives of the measure, and of the type of environmental protection it is intended to promote.

## 2. Description of the measure.

Detailed description of the measure and of the recipients.

Description of the total costs of the investments involved and of the eligible costs.

If the measure in question has already been applied in the past, what environmental results have been obtained?

If the measure is a new one, what environmental results are anticipated, and over what period?

If the aid is to be granted towards an improvement on standards, what are the standards applicable, and in what way does the measure allow an appreciably higher level of environmental protection to be achieved?

If the aid is to be granted in the absence of mandatory standards, please give a detailed description of the way.

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