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COMMUNICATION FROM THE COMMISSION

**Amendment to the Temporary Framework for State aid measures to support the
economy in the current COVID-19 outbreak**

Recapitalisation of non-financial undertakings

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1. INTRODUCTION

- (1) On 19 March 2020, the European Commission adopted its Communication “Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak”¹ (“the Temporary Framework”) to enable Member States to use the full range of possibilities provided by the EU State aid rules to respond to that outbreak. The Temporary Framework was first amended on 3 April 2020 to accelerate research, testing and production of COVID-19 relevant products, to protect jobs and to further support the economy.²
- (2) A targeted and proportionate application of the EU State aid rules ensures that national support measures effectively help affected undertakings during the COVID-19 outbreak, whilst limiting undue distortions to the Internal Market. This will allow the economy to recover from the current crisis, keeping in mind the importance of meeting the challenges of the green and digital twin transitions, in accordance with EU objectives.
- (3) The aim of this Communication is to identify additional temporary State aid measures that the Commission considers compatible with Article 107(3)(b) TFEU in response to the COVID-19 outbreak.
- (4) The Commission considers that non-financial undertakings subject to a temporary liquidity crisis due to the COVID-19-outbreak may also face longer-term solvency issues. For a large number of these undertakings, the emergency measures taken to control the COVID-19 outbreak have resulted in a decrease or even suspension of their production of goods and/or the provision of services, as well as a significant demand shock. The resulting losses will be reflected in a decrease of undertakings’ equity and will negatively impact their ability to borrow from financial institutions.
- (5) Reduced equity for an undertaking in a market with low demand aggravates the risk of a serious economic downturn affecting the whole EU economy for a longer period. Well-targeted public interventions providing equity and/or hybrid capital instruments to undertakings could reduce the risk for the EU economy of a significant number of insolvencies and could contribute to preserving the continuity of economic activity during the COVID-19 outbreak and supporting subsequent economic recovery.
- (6) However, the Commission notes that providing national public support in the form of equity and/or hybrid capital instruments to undertakings facing financial difficulties due to the COVID-19 outbreak, as part of schemes or in specific cases, should remain an intervention of last-resort. This is because such instruments are highly distortive for

¹ Communication from the Commission of 19 March 2020, C(2020)1863, OJ C 091I of 20.3.2020, p.1.

² Communication from the Commission on 3 April 2020, C(2020) 2215, OJ C 112I of 4.4.2020, p. 1.

competition between undertakings. Such interventions should therefore be subject to clear conditions as regards the State's entry, remuneration and exit from the undertakings concerned, governance provisions and appropriate measures to limit distortions of competition. If support were to be granted at EU level, taking into account the EU common interest, the risk of distortion to the Internal Market would be lower, and therefore require less stringent conditions to be imposed.

- (7) Separately, a number of Member States are considering taking an equity stake in strategic companies, to ensure that their contribution to the proper functioning of the EU economy is not jeopardised. In this regard, if Member States purchase existing shares of undertakings at market price or invest *pari passu* with private shareholders, this in principle does not constitute State aid. If Member States decide to purchase newly issued shares and/or provide undertakings with other types of equity support or hybrid capital instruments, this is possible only on the same conditions referred to in paragraph (6).
- (8) The Commission recalls that a number of additional tools are relevant to Member States. In its Communication issued on 25 March 2020³, the Commission called upon Member States that already have an existing foreign direct investment screening mechanism in place to make full use of such tools to prevent capital flows from non-EU countries that could undermine Europe's security or public order. The Commission also called on remaining Member States to set up a fully-fledged screening mechanism.

2. AMENDMENTS TO THE TEMPORARY FRAMEWORK

- (9) The following amendments to the Temporary Framework will take effect from [X] April 2020.
- (10) The following section is inserted:

“3.11. Recapitalisation measures

3.11.1. Applicability

44. The following conditions shall apply to recapitalisation schemes and individual recapitalisation measures of Member States for non-financial undertakings (collectively referred to as “COVID-19 recapitalisation” measures), which are not covered by section 3.1 of this Communication.
45. COVID-19 recapitalisation measures shall not be granted later than 31 December 2020.

³ Communication from the Commission - Guidance to the Member States concerning foreign direct investment and free movement of capital from third countries, and the protection of Europe's strategic assets, ahead of the application of Regulation (EU) 2019/452 (FDI Screening Regulation), C(2020) 1981 final of 25.3.2020.

3.11.2. Eligibility and entry conditions

46. The beneficiary of a COVID-19 recapitalisation measure must fulfil the following conditions:
- (a) without the State intervention it would go out of business or would face serious difficulties to maintain its operations. Such difficulties can be shown by the deterioration of, in particular, the beneficiary's debt to equity ratio or similar indicators;
 - (b) its failure would likely involve social hardship or market failure, within the meaning of point 44 of the Rescue and Restructuring Guidelines⁴;
 - (c) it has exhausted the possibilities to find financing on the markets and the horizontal measures existing in the Member State concerned to cover liquidity needs are insufficient to ensure its viability; and
 - (d) it is not an undertaking that was already in difficulty on 31 December 2019 (within the meaning of the General Block Exemption Regulation⁵).
47. Member States shall grant COVID-19 recapitalisation measures under an aid scheme approved by the Commission only following a written request for such aid by the prospective beneficiary undertaking. As regards individually notifiable aid, Member States shall provide evidence of such written request as part of the notification of the individual aid measure to the Commission.
48. The requirements of this section and sections 3.11.4, 3.11.5, 3.11.6 and 3.11.7 apply to both COVID-19 recapitalisation schemes and individual aid measures. When approving schemes, the Commission will request separate notification of individual aid above the threshold of [EUR 100] million. In relation to such notifications the Commission will assess that existing financing in the market or horizontal measures to cover liquidity needs are not sufficient to ensure the viability of the company; that the selected recapitalisation instruments and the conditions attached to them are the most appropriate to address the beneficiary's serious difficulties; that the aid is proportionate; and that the conditions in this section and sections 3.11.4, 3.11.5, 3.11.6 and 3.11.7 are complied with.

3.11.3. Types of recapitalisation measures

49. Member States can provide COVID-19 recapitalisation measures using two distinct sets of recapitalisation instruments:
- (a) equity instruments, in particular, the issuance of new common or preferred shares; and/or
 - (b) debt financing instruments with a potential equity component (referred to as 'hybrid capital instruments')⁶, in particular profit participation rights, silent participations and convertible secured or unsecured bonds.

⁴ Guidelines on State aid for rescuing and restructuring non-financial undertakings in difficulty (2014/C 249/01) OJ 249/1.

⁵ As defined in Article 2 (18) of the Commission Regulation (EU) No 651/2014 of 17 June 2014 declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty, OJ L 187 of 26.6.2014, p. 1.

50. The State intervention can take the form of any variation of the above instruments (for example non-voting shares), or a combination of equity and hybrid capital instruments. The Member State must ensure that the selected recapitalisation instruments and the conditions attached shall be the most appropriate to address the beneficiary's recapitalisation needs while at the same time being the least distortive to competition.

3.11.4. Amount of the recapitalisation

51. In order to ensure proportionality of the aid, the amount of the COVID-19 recapitalisation must not exceed the minimum needed to ensure the viability of the beneficiary, and in any event must not go beyond restoring the capital structure of the beneficiary to the one predating the COVID-19 outbreak, i.e. the situation on 31 December 2019.

3.11.5. Remuneration and exit of the State

General principles

52. The State shall receive appropriate remuneration for the investment. The closer the remuneration is to market terms, the lower the potential competition distortion caused by the State intervention.
53. The COVID-19 recapitalisation shall be redeemed when the economy stabilises. The Commission considers it appropriate to give the beneficiary sufficient time to redeem the recapitalisation. The Member State shall put a mechanism in place to incentivise redemption before 1 January 2023.
54. As of 1 January 2023, the remuneration of the State should be progressively increased in order to converge with market prices to provide incentives for the exit of the State and to minimise the risk of distortions of competition. If the beneficiary is not a publicly listed company, Member States may decide to start the progressive increase in the remuneration at a later date but no later than 1 January 2024.
55. It follows that recapitalisation measures need to contain appropriate incentives for undertakings to redeem the State recapitalisation and look for alternative capital when market conditions permit, by requiring a sufficiently high remuneration for the State recapitalisation.
56. As an alternative to the remuneration methodologies set out below, Member States may notify schemes or individual measures where the remuneration is adapted in accordance with the features and seniority of the capital instrument.

⁶ Hybrid capital instruments are instruments that have characteristics of debt as well as of equity. For instance, convertible bonds are remunerated like bonds until they are converted into equity. The assessment of the overall remuneration of hybrid capital instruments thus depends on the one hand on their remuneration while they are debt-like instruments and on the other hand on the conditions for conversion into equity-like instruments.

Remuneration of equity instruments

57. A capital injection by the State, or an equivalent intervention, should be conducted in line with the Theoretical Ex-Rights Price (TERP) method, which is based on the average share price of the beneficiary over the 30 days preceding the request for the capital injection. If the beneficiary is not publicly listed, an estimation of its market value should be established by an independent expert or other proportionate means.
58. Any recapitalisation measure shall include a step-up mechanism increasing the shareholding of the State at no additional cost, to incentivise the beneficiaries to buy back the State capital injections. As of 1 January 2023, if the State has not sold at least [40] percent of its equity participation resulting from the COVID-19 equity injection, the State will receive an additional share of ownership of the beneficiary in addition to its remaining participation resulting from the State's COVID-19 equity injection. This additional share of ownership should be a minimum of [10] percent of the remaining participation resulting from the State's COVID-19 equity injection. As of 1 January 2024, if the State has not sold in full its equity participation resulting from the State's COVID-19 equity injection, the State will receive a second additional share of ownership of the beneficiary of a minimum of [10] percent of the remaining participation resulting from the State's COVID-19 equity injection⁷. If the beneficiary is not a publicly listed company, Member States may decide to implement each of the two steps one year later, i.e. as of 1 January 2024 and 1 January 2025 respectively.
59. The Commission may accept alternative step-up mechanisms, provided they have the same incentive effects on the exit of the State and a similar impact on the State's remuneration.
60. The beneficiary shall have at any time the possibility to buy back the equity stake that the State has acquired. To ensure that the State receives appropriate remuneration for the investment, the buy-back price should be the higher amount of (i) the nominal investment by the State increased by an annual interest remuneration [500] basis points higher than presented in Table 1 below; or (ii) the market price at the moment of the buy-back.
61. As an alternative, the State may sell its equity participation at market prices to purchasers other than the beneficiary. This in principle requires an open and non-discriminatory consultation of potential purchasers or a sale on the stock exchange.

Remuneration of hybrid capital instruments

62. The overall remuneration of hybrid capital instruments needs to adequately factor in the following elements:
 - (a) characteristics of the instrument chosen, including its level of subordination, risk and all modalities of payment;
 - (b) built-in incentives for exit (such as step-up and redemption clauses); and

⁷ For instance, if the State's participation in a beneficiary is 40% as a result of its capital injection, and if the State does not sell its participation before the requested date, the State's participation should increase by at least $0,1 \times 40\% = 4\%$ to reach 44% as of 1 January 2023, and to reach 48% as of 1 January 2024, resulting in a corresponding dilution of the stakes of other shareholders.

- (c) an appropriate benchmark interest rate.
63. The minimum remuneration of hybrid capital instruments until they are converted into equity-like instruments shall be at least equal to the base rate (1 year IBOR or equivalent as published by the Commission⁸), plus the premium as set out in the table below.

Table 1: remuneration of hybrid capital instruments: 1-year IBOR +

Type of recipient	Until 31/12/2021	2022	2023	2024	2025 and after
SMEs	225 bps	350 bps	450 bps	600 bps	700 bps
Large enterprises	250 bps	400 bps	500 bps	700 bps	800 bps

64. The conversion of hybrid capital instruments into equity shall be conducted at [10] percent or more below TERP at the time of the conversion.
65. After conversion into equity, a step-up mechanism has to be included to increase the shareholding of the State to incentivise the beneficiaries to buy back the State capital injections. Two years after the conversion into equity, if the equity resulting from the State’s COVID-19 intervention is still owned by the State, the State shall receive an additional share of ownership of the beneficiary in addition to its remaining participation resulting from the State’s conversion of the COVID-19 hybrid capital instruments. This additional share of ownership shall be at a minimum [10] percent of the remaining participation resulting from the State’s conversion of the COVID-19 hybrid capital instruments. The Commission may accept alternative step-up mechanisms provided they have the same incentive effects and a similar impact on the State’s remuneration.
66. Member States may choose a pricing formula that includes additional step-up or payback clauses. Such features should be designed so that they encourage an early end to the State’s recapitalisation support of the beneficiary. The Commission may also accept alternative pricing methodologies, provided they lead to remunerations that are higher than or similar to the above methodology.
67. As the nature of hybrid instruments varies significantly, the Commission does not provide guidance for all types of instruments. Hybrid instruments shall in any event follow the principles mentioned above, with remuneration reflecting the risk of the particular instruments.

3.11.6. Governance and prevention of undue distortions of competition

68. In order to prevent undue distortions of competition beneficiaries must not engage in aggressive commercial expansion financed by State aid or beneficiaries taking excessive risks. As a general principle, the smaller the equity stake of the Member State and the higher the remuneration, the less there is a need for safeguards.

⁸ Base rates calculated in accordance with the Communication from the Commission on the revision of the method for setting the reference and discount rates (OJ C 14, 19.01.2008, p.6.), published on the website of DG Competition at https://ec.europa.eu/competition/state_aid/legislation/reference_rates.html.

69. Where the beneficiary of a COVID-19 recapitalisation measure above EUR [100] million is an undertaking with significant market power on at least one of the relevant markets in which it operates, Member States must propose additional measures to preserve effective competition in the relevant markets. In proposing such measures, Member States may in particular offer structural or behavioural commitments foreseen in Commission Notice on remedies acceptable under the Council Regulation (EC) No 139/2004 and under Commission Regulation (EC) No 802/2004.
70. Beneficiaries receiving a COVID-19 recapitalisation are prohibited from advertising it for commercial purposes.
71. As long as State aid has not been repaid or the State has not sold its participation resulting from the COVID-19 recapitalisation, beneficiaries other than SMEs shall be prevented from acquiring competitors or other operators in the same line of business, including upstream and downstream operations.
72. In exceptional circumstances, and without prejudice to merger control, such beneficiaries may acquire operators upstream or downstream in their area of operation or even competitors, only if the acquisition is necessary to maintain the viability of the beneficiary. The Commission may allow the acquisition if it is necessary to maintain the viability of the beneficiary. The acquisition may not be implemented before the Commission has reached its conclusion.
73. State aid shall not be used to cross-subsidise other economic activities of integrated undertakings that were in economic difficulties on 31 December 2019. Clear account separation shall be put in place in integrated companies to demonstrate that the recapitalisation measure does not benefit those activities.
74. As long as the State's equity resulting from the COVID-19 recapitalisation has not been fully redeemed, beneficiaries cannot make dividend payments, nor non-mandatory coupon payments, nor buy back shares, other than in relation to the State.
75. As long as the State's equity resulting from the COVID-19 recapitalisation has not been fully redeemed, the remuneration of the each member of the management of the beneficiaries must not go beyond the fixed part of his/her remuneration on 31 December 2019. For persons becoming members of the management on or after the recapitalisation, the applicable limit is the lowest fixed remuneration of any of the members of the management on 31 December 2019. Under no circumstances, bonuses, other variable or comparable remuneration elements shall be paid.

3.11.7. Exit strategy of the State from the participation resulting from the recapitalisation

76. Beneficiaries other than SMEs that have received a COVID-19 recapitalisation of more than [20] percent of equity at the moment of intervention have to demonstrate a credible exit strategy for the participation of the Member State, unless the State's intervention is reduced below the level of [20] percent of equity within [6] months from the date of the granting of the aid.⁹

⁹ Hybrid instruments should be counted as equity for this purpose.

77. The exit strategy shall lay out:
 - (a) the plan of the beneficiary on the continuation of its activity and the use of the funds invested by the State, including a payment schedule of the remuneration and of the redemption of the State investment (together 'the repayment schedule'); and
 - (b) the measures that the beneficiary and the State will take to abide by the schedule.
78. The exit strategy should be prepared and submitted to the Member State within [6] months after the granting of the aid and needs to be endorsed by the Member State.
79. Beyond the obligation set out in points 76 to 78, beneficiaries have to report to the Member State about the progress in the implementation of the repayment schedule and the compliance with the conditions in section 3.11.6 within [6] months of the schedule's presentation, and thereafter periodically every [6] months.
80. The Member State should report to the Commission annually about the implementation of the repayment schedule and compliance with the conditions in section 3.11.6.
81. If by [31 December 2024] the State's intervention under the Temporary Framework has not been reduced below [15] percent of equity, a restructuring plan in accordance with the Rescue and Restructuring Guidelines shall be notified to the Commission for approval. The Commission will assess whether the actions contemplated in the restructuring plan ensure the viability of the beneficiary, also with a view of EU and national obligations linked to the green and digital transformation, and the exit of the State without adversely affecting trade to an extent contrary to the common interest. If the beneficiary is not a publicly listed company, Member States may decide to notify a restructuring plan only if the State's intervention has not been reduced below the level of [15] percent of equity by [31 December 2025].