Financial instruments and their proportionality and consistency under EU Law

Summary of the Thesis

Financial instruments have witnessed an increasing uptake by the European Union (EU) and Member States to finance public policy objectives not just since the Covid-19 crisis, e.g. to support young and innovative SMEs in need of risk finance. Next to grants and tax exemptions, they provide an alternative tool under EU state aid law in the form of equity, quasi-equity, loans, and guarantees. They are implemented via financial intermediaries, such as banks and financial institutions, are repayable, and leverage private sector investment. As market interventions, they may create undue advantages at different levels, i.e. at that of investors, financial intermediaries and their fund managers, as well as beneficiary undertakings. As such, they are liable to distort the market, so that state aid law applies. However, the latter applies only to those instruments implemented and managed at Member State level, while those at EU level must be 'consistent with state aid law'. The Commission strives to ensure this through terms and conditions of special agreements with implementing bodies of the European Investment Bank.

Thereby, the principle of proportionality is of critical importance to state aid law, since it warrants that aid measures as market interventions are suitable, necessary, and non-disproportionate. Specifically, financial instruments must be suitable to the desired goal, necessary or least restrictive as a means, and not disproportionate to avoid market distortions. If this principle is applied inconsistently, i.e. with contradictions and not as one set of rules, legal certainty and efficiency suffer to the detriment of stakeholders. The overarching research question of this thesis is thus whether the European Commission and the legal framework of financial instruments both inside and outside state aid law ensure their proportionate application in a consistent manner in accordance with the case law of the EU Courts. The thesis addresses this question to provide improvements to the overall state aid framework of financial instruments under the urgency of the Commission's review of state aid rules. Therefore, legal texts of primary and secondary, binding and non-binding nature, the applicable case law of the EU Courts, and relevant Commission decisions were consulted, compared, and analysed.

The findings of this thesis are, firstly, that inconsistencies among the plethora of legal texts exist (chapter IV). Secondly, that it is difficult to consistently identify and quantify the advantage and risks of financial instruments in a market environment of young and innovative SMEs that is inherently risky and prone to information asymmetries (chapter V). Thirdly and importantly, that the Commission fails to adhere to the requirements of the EU Courts on proportionality in its case law on state aid: Instead of the required effects-based approach, including the balancing of positive and negative effects of financial instruments, the Commission merely applies a formalistic checklist.

Hence, the findings suggest that neither in its compatibility assessment of its decisions (chapter VI) nor in its design of financial instruments at the EU level (chapter VII) does the Commission provide tools to analyse the correspondence between the aid amount and the extent of the respective market failure or impact of the aid. Instead, it checks whether certain limitations to the aid amount, market mechanisms, and accountability methods (chapter VIII) are applied to the relevant instrument to minimise market distortions. Since the Commission does not possess tools to quantify the aid, let alone conduct the balancing exercise, the thesis recommends the introduction of so-called manifest negative effects, which are applied in other state aid areas and are apt to solve these inconsistencies: Based on the EU Courts' requirements on proportionality, they indicate with legal certainty to stakeholders which potential negative effects are disproportionally distortive, rendering the relevant instrument incompatible with the internal market.