State Aids in Switzerland: The Air Transport Agreement between the EU and Switzerland

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I. Introduction

The following article investigates the extent to which EU regulations relating to the law on State aid apply in Switzerland in the aftermath of the conclusion of the bilateral agreements between Switzerland and the EU. In addition, specific consideration is given within this remit to the State measures implemented in relation to the "Swiss" airline.

1. The bilateral agreements

On 23 June 1999, Switzerland entered into seven sectoral agreements[3] with the EU with a view to maintaining competitiveness and securing the quality of Switzerland as a business location. By concluding these bilateral agreements, in force since June 2002, Switzerland's legislative autonomy has to a large extent been preserved. This would not have been the case had it acceded to the EEA Agreement.

The Agreement on Air Transport (hereinafter "AAT"), which is relevant to the issue of aid in the civil aviation sector, is somewhat exceptional in comparison with the other agreements in that it is partly an integration agreement. Switzerland had expressed its willingness in this area to accept certain regulations under EC law, whereby each of the contracting parties are themselves required in principle to ensure that the contractual regulations are complied with on their own sovereign territory[4]. This is of particular relevance to the State aid regulations in Articles 13 and 14 of the AAT.

2. No State aid provisions under Swiss law

Swiss law has no provisions on State aids. The Federal Act on Financial Aid and Payments[5] covers subsidies only and makes no use of the term "State aid". The term "subsidy" as used in the Subsidies Act covers financial aid and payments. According to Article 3 paragraph 1 of the Subsidies Act, "financial aid" means advantages with a monetary value that are granted to recipients outside the Federal Administration in order to assist in the fulfilment or continuation of a task appointed by the recipient. Payments are made to recipients outside the Federal Administration to reduce or compensate for financial burdens that arise from fulfilling public duties.

However, the Subsidies Act must be further distinguished from State aid provisions in that it is designed to specify formal requirements for granting subsidies, but not to prevent the negative effects on competition that may result from the granting of aid.

3. The AAT in general and the State aid provisions in particular

The AAT is divided into eight Chapters covering various matters, including: the regulations on the objective of the agreement in the first Chapter (Article 1 and Article 2); general provisions in the second Chapter (Articles 3 to 14); and the mechanisms for applying the provisions in the fourth Chapter (Articles 17 to 20).

Under Article 1 paragraph 2 section 2, the AAT provisions, insofar as they are essentially in conformity with the corresponding regulations of the Treaty

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3 Agreements between the European Community and the Swiss Confederation: on trade in agricultural products, OJ 2002 L 114/132; on Scientific and Technological Cooperation, OJ 2002 L 114/468; on certain aspects of government procurement, OJ 2002 L 114/430 ; on mutual recognition in relation to conformity assessment, OJ 2002 L 114/369; on the Carriage of Goods and Passengers by Rail and Road, OJ 2002 L 114/91, and on Air Transport, OJ 2002 L 114/73; agreement between the European Community and its Member States on the one part and the Swiss Confederation on the other on the free movement of persons, OJ 2002 L 114/6.

4 See Dispatch (a Dispatch is the report of the Swiss Federal Council on proposed legislation that is submitted to the Swiss Parliament) of 23 June 1999 on the approval of the AAT (hereinafter "AAT Dispatch"), Chapter 148.2. There are, however, exceptions in the field of competition law, see Zurkinden, "Ausführung internationaler Abkommen", in: von Bueren/David (ed.), Schweizerisches Immaterialgüter- und Wettbewerbsrecht, vol. V/2, 2000, Basle/Geneva/Munich, pages 533 et seq.

5 Subsidies Act, SuA, of 5 October 1990, Systematic Compilation of Federal Law, SR 616.1.

establishing the EU and the EU legal regulations based on them, are to be interpreted in conformity with the judgments and decisions of the European Commission and the European Court of Justice in relation to the EU provisions concerned.

In accordance with Article 17 of the AAT, the parties subject to the Agreement must take all appropriate measures of a general or specific nature in order to guarantee the fulfilment of the obligations arising from the Agreement.

Lastly, under Article 18 paragraph 1 of the AAT, each contracting party is responsible in its own area for the proper application of the Agreement, particularly of the ordinances and guidelines specified in the Annex. The Annex constitutes an integral element of the Agreement and includes the provisions of subsidiary EU legislation that are to be applied or implemented in Switzerland. The provisions covering State aids in the AAT may be found in Articles 13 and 14 of the AAT.

Article 13 of the AAT

1. Save as otherwise provided in this Agreement, any aid granted by Switzerland or by an EC 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, insofar as it affects trade between Contracting Parties, be incompatible with this Agreement.
2. The following shall be compatible with this Agreement:
   a. aid having a social character, granted to individual consumers, provided that such aid is granted without discrimination related to the origin of the products concerned;
   b. aid to make good the damage caused by natural disasters or exceptional occurrences.
3. The following may be considered to be compatible with this Agreement:
   a. aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious under-employment;
   b. aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Contracting Party;
   c. 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.

Article 14 of the AAT

The Commission and the Swiss authorities shall keep under constant review matters to which reference is made in Article 12 and all systems of aid existing respectively in the EC Member States and in Switzerland. Each Contracting Party shall ensure that the other Contracting Party is informed of any procedure initiated to guarantee respect of the rules of Articles 12 and 13 and, if necessary, may submit observations before any final decision is taken. Upon request by one Contracting Party, the Joint Committee shall discuss any appropriate measures required by the purpose and functioning of this Agreement.

Article 13 of the AAT basically corresponds to Article 87 EC Treaty. Fundamentally, it prohibits State aids that can lead to distortions of competition. Paragraphs 2 and 3, however, provide for the possibility of granting certain restricted and discretionary exemptions. Under Article 14 section 1 of the Agreement, the European Commission and the responsible Swiss authorities are required to keep under permanent review any State aid schemes in the Member States and in Switzerland. There is also a requirement, in accordance with Article 14 section 2 of the AAT, to provide information and the possibility for requesting the Joint Committee to discuss any appropriate measures[6].

Subsidiary regulations under EU law in relation to State aids are not contained in the Annex.

II. Importance and need for action in Switzerland

As already mentioned, Switzerland has no national law on State aids. Accordingly, at the time when the AAT was concluded no authority existed which was either responsible for this matter or familiar with it. There was therefore a need for action, both in relation to the setting up of a supervisory authority and also for preparing precise implementing regulations, in formal and material terms, of the principles set out in Articles 13 and 14 of the AAT.

1. Setting up the supervisory authority

Switzerland took its time over setting up the supervisory authority. At the time the AAT came into effect no authority had been set up. Nor does such an authority exist today from a formal point of view.

6 The "Joint Committees" are joint bodies representing both contracting parties. Each bilateral agreement should have its own joint committee, which has the task of monitoring the proper implementaton of the bilateral agreement. The Joint Committees have the following areas of responsibility: exchanges of opinion and information, drawing up recommendations, decision-making powers in cases expressly provided for in the agreement (e.g. amendment of annexes). The Joint Committees may decide by mutual agreement. Amendments to the bilateral agreements that include new obligations for the contracting parties remain the responsibility of the contracting parties.

However, the draft for modifying the Swiss Federal Aviation Act[7] (hereinafter "FAA") provides in its Article 103 for the Competition Commission to assume this duty.

Article 103 of the FAA as very recently approved by the Swiss Parliament:

1. The Competition Commission will examine whether the following are compatible with Article 13 of the Agreement of 21 June 1999 between the Swiss Confederation and the European Community on Air Transport:
   a. the drafts of decrees of the Federal Council that favour certain companies or manufacturing branches in the scope of the application of the Agreement, in particular services and shareholdings according to Articles 101, 101 a and 102;
   b. similar support measures taken by cantons and communes or other Swiss bodies or institutions subject to public law or of mixed economic structure;
   c. similar support measures taken by the European Union or its Member States.
2. In its deliberations the Competition Commission is independent of the Federal Council and the administration.
3. The authorities responsible for the decision will take into account the result of the Competition Commission's inquiry.

In the dispatches on both the bilateral AAT and the revised FAA[8], it is specified in accordance with the so-called "twin pillar system" laid down in Article 14 of the AAT that each contracting party is responsible for checking the compatibility of its aids with the regulations of the Agreement. This statement must be understood to mean that the European Commission will be responsible for the supervision of measures taken by the European Union or its Member States within the European Union, and the Swiss Competition Commission is responsible for measures taken by the Swiss authorities in Switzerland. In Article 103 of the FAA, however, the Swiss Competition Commission is also granted the authority to inquire into support measures taken by the European Union or its Member States. Practice will reveal the extent to which this authority can be implemented and whether in fact the AAT even affords an adequate legal basis for such a power. Furthermore, it is noticeable that paragraph 3 of Article 103 foresees that the authorities responsible for the decisions on aids only shall have to take into account the result of the Competition Commission, whereas the European Commission is empowered to take formal decisions.

2. Implementing regulations in terms of material law

The principle in Article 13 of the AAT constitutes the central basis in terms of material law for the control of aids in Switzerland in accordance with the AAT. As already mentioned, and in contrast to other legal areas, the Annex contains no subsidiary EU legislation in relation to State aids which Switzerland is obliged to accept.

The principle in Article 1 paragraph 2 of the AAT, which has also been mentioned above, requires that any legal clauses corresponding to EU legislation that are contained in the AAT must conform in their implementation and application to the respective interpretations of the EU organisations. Article 13 of the AAT corresponds to Article 87 EC Treaty. The extent of validity of the rules of interpretation created in the EU on this Article is open to question, particularly rules such as the "Community guidelines on State aid for rescuing and restructuring of firms in difficulty"[9] as well as the guidelines for State aid in civil aviation ("Application of Articles 92 and 93 of the EC Treaty and Article 61 of the EEA Agreement to State aids in the aviation sector")[10] which are both central to the interpretation of Article 87(3) EC Treaty.

Since the guidelines concern, in concrete form, Article 87 EC Treaty, and since Article 13 of the AAT essentially corresponds to this Article, Switzerland is required at least to pay attention to these guidelines in the implementation and application of the AAT. In the dispatch detailing the modification of the FAA, explicit reference is also made to these guidelines[11]. The precise definition in material legal terms required for the practical implementation of Article 13 of the AAT must therefore be guided by the guidelines relating to Article 87 EC Treaty.

3. Implementing regulations in terms of procedural Law

Article 14 of the AAT makes a distinction between the power to investigate in respect of State aid schemes and the requirement to inform the other contracting party about all procedures designed to ensure compliance with AAT Article 13.

7 See Federal Act on Civil Aviation, FAA, of 21 December 1948, SR 748.0; see Dispatch on the amendment to the Civil Aviation Act of 10 September 2003, hereinafter "Dispatch FAA", Chapter 1.2.

8 See Dispatch on AAT, Chapter 253.2; Dispatch FAA, Chapter 1.1.

9 See OJ 1999 C 288/2, hereinafter "Rescue and restructuring aid guidelines".

10 See OJ 1994 C 350/2, hereinafter "Air transport guidelines".

11 See Dispatch FAA, Chapter 1.2., see above II.1.

The Ordinance No. 3976/87 contained in the Annex of the AAT regarding the details on the application of the rules on competition to airlines does not include the procedure in respect of State aid.

For the European Commission the procedure for taking decisions on the compatibility of State aids is codified in the Regulation (EC) 659/1999. However, this Ordinance is not contained in the Annex of the AAT.

The question thus arises as to how Switzerland will organise its procedure[12]. A regulation in relation to the investigation proceedings based on Articles 13 and 14 of the AAT has not yet been specified. According to the opinion put forward here, it cannot be concluded that the principle of AAT provisions corresponding to EU legislation being applied in conformity with EU practice must mean that the procedure itself must likewise correspond to that found in EC law.

Swiss law has a review procedure in respect of State payments in the Subsidies Act. It seems, however, inappropriate to apply this to the investigation of State aids on account of its different orientation[13]. Neither has the proposed modification in Article 103 of the FAA[14] anything to say on the procedure to be applied. The dispatch[15] treats this matter merely by stating that, as a result of the twin-pillar principle, Switzerland undertakes to set up the necessary structures and procedures within which the compatibility of State aids with the AAT may be reviewed in a consistent and proper manner.

In view of the present situation, despite the lack of legal obligations some move must be made towards creating a regulation procedure corresponding to Regulation (EC) 659/1999. This procedure has proved its worth within the EU and, in addition, its structure possesses similarities with the EU merger control procedure (both proceedings are divided into two phases). In 1995, structurally and systematically speaking a very similar merger control procedure regulation was incorporated into the Swiss Cartels Act[16] with the result that it became familiar to the Swiss Competition Commission that the Federal Council has indicated it would like to assume the future supervision of State aids as well.

4. Need for action

In view of the fact that the AAT has been in force since 1 June 2002, there is an urgent need for action in Switzerland. While Switzerland is bound to EU subsidiary guidelines for the precise definition in terms of material law, from the procedural point of view Switzerland is probably free. There are, however, also with this respect good reasons for taking the EU legal solution as the standard to follow.

The need for action has also become urgent in practical terms. For a long time the case of the "Swiss" airline company (hereinafter "Swiss") has been posing important questions relating to the law on State aid. Below we attempt to analyse this case from the viewpoint of the State aid regulations that have been in force in Switzerland since 1 June 2002.

III. Specific repercussions of the AAT in the "Swiss" case

In the following section, the intention is to examine and clarify the restructuring measures carried out by the Swiss Confederation for the benefit of the "Swiss" airline in terms of the restructuring plan for national civil aviation in Switzerland in the year 2001[17] and also following State aids from the viewpoint of the State aid regulations contained in the AAT.

1. The evolution of the "Swiss" airline and the relevant State measures

In 1931 "Swissair", the "Schweizerische Luftverkehr Aktiengesellschaft", came into being as a result of the merger of "Balair", the "Basler Luftverkehrsgesellschaft, Basel", and the "Ad Astra-Aero Schweizerische Luftverkehrsgesellschaft, Zurich". After Swissair had grown to become one of the largest companies in the country, its parent company, the SAir-Group Holding, collapsed into a hopeless financial situation. This was due in part to the constant deregulation of the civil aviation markets and the partial privatisation of the airlines at the beginning of the 1980s. The global crisis in civil aviation also played a role and, ultimately, so did the negative consequences of the tragic events of 11 September 2001.

At the start of October 2001, Swissair successfully filed for a moratorium on the enforcement of its debts. In order to ensure that Switzerland, as a prime business location, would retain a national airline with intercontinental routes, some of the Swissair fleet and air routes were taken over by Crossair, another subsidiary of SAir-Holding, under the terms of a Federal

12 The same question probably arises in connection with Articles 13 and 14 of the AAT as part of the Vaduz Convention of 21 June 2001 which corresponds to Articles 6 and 7 of Annex Q on Air transport in the Convention establishing the European Free Trade Association (EFTA).

13 See above I. 2.

14 See above II. 1.

15 See Dispatch FAA, Chapter 1.3.

16 Federal Act of 6 October 1995 on Cartels and other Restraints on Competition, ACart, SR 251.

17 See Federal Council Dispatch on the Financing of the Restructuring Plan for National Civil Aviation of 7 November 2001, hereinafter "Dispatch on Restructuring".

Decree issued in November 2001 and as part of restructuring plan that had been agreed earlier.
In an unprecedented move[18], both the state and the private sector backed Swissair and Crossair with a view to their merger, using funds amounting to CHF 2.561 million. The new equity was injected into the company in the form of CHF 2.286 million as share capital and CHF 275 million as a paid–up surplus.

To finance the restructuring plan, the Swiss Confederation took a stake amounting to a CHF 600 million increase in the share capital of Crossair, and granted Swissair a loan of CHF 1.450 million. The Swiss Confederation loan of CHF 1.450 million in favour of Swissair was based on two loan agreements. Under the public loan agreement of 5 October 2001, the government first of all granted Swissair financial aid in the form of an interest-free loan amounting to CHF 450 million. In the supplementary agreement, dated 25 October 2001, the loan amount was increased by CHF 1.000 million.

Under Article 1 paragraph 1 of the loan agreement, the purpose of granting the loan was to guarantee flight operations by Swissair until 28 October 2001. Furthermore, the loan was intended in terms of Article 1 paragraph 2 to allow flight operations to continue thereafter and to permit such operations to be handed over in the proper manner to a new national airline (i.e. Crossair). Regarding repayment, the parties agreed that if following the sale of the assets repayment in full was not possible, the Swiss Government would waive the unsecured portion of its claim. Crossair took over the important activities of Swissair, and in 2002 was renamed "Swiss"[19].

2. Validity of the AAT provisions on support measures prior to the AAT's coming into force

At the time that Swissair was being restructured, neither the AAT nor the relevant State aid provisions were yet in force. In principle, therefore, the regulations in the AAT had no direct binding effect at this moment. Nevertheless, with an eye on the AAT, Switzerland informed the EU Commission about the measures it had taken, and also pursued a continuing exchange of information[20]. This was done in particular as a result of the controversial issue of whether the AAT had already given rise to certain prior effects even before it had come into force[21]. Those who supported this view cited in particular Article 18 of the Vienna Convention on the Law of Treaties[22] as well as the international law and the principle of good faith resulting from it. They deduced that even before the AAT came into force, Switzerland would be obliged to refrain from taking any measures that would nullify the basic aims of the AAT or which would harm Switzerland's ability to apply the AAT once it had come into force.

As a result of this as yet unanswered question, in its dispatch on the restructuring plan for the sake of good form the Federal Council had also addressed the issue of a possible conflict between the support measures and the AAT which was due to come into effect a short time later[23]. The Council came to the conclusion that the loan and the minority shareholding were not capable of nullifying the basic objectives of the AAT or of harming Switzerland's ability to apply the AAT once it had come into force[24]. In the Federal Council's opinion, the loan given to Swissair was to be classified as rescue aid, and as such it was basically unobjectionable as far as the EU was concerned[25]. The minority shareholding, according to the Federal Council, was to be regarded as a normal state of affairs for the market. The majority shareholding being in the hands of the private sector indicated that the Confederation had made a sensible investment which a private investor motivated by concerns about profitability would also have made. Accordingly, it could not be regarded as State aid[26].

Although the Swiss Government has addressed the problem of compatibility of its measures in favour of "Swiss" with the AAT rules, it has always made clear that it was of the opinion that the AAT had no effect prior to 1 June 2002. In the section below, however, the support measures taken at that time as part of the restructuring plan will again be critically appraised from the viewpoint of Article 13 of the AAT.

3. Appraisal of the State measures taken in terms of a restructuring plan for national civil aviation

a. Principles for the appraisal of State measures in terms of Article 13 AAT and Article 87(1) EC Treaty

Under Article 87(1) EC Treaty and Article 13 paragraph 1 of the AAT, State aids or aids granted using State resources, whatever their form, which distort or

18 See Dispatch on Restructuring.

19 According to a Press release of the Swiss Federal Chancellery of 21 May 2003, the loan, amounting to around CHF 300 million, has not so far been claimed.

20 See Dispatch on Restructuring, Chapter 5.

21 See on the applicability of the Vienna Convention to the Air Transport Agreement: Christa Tobler, "Vorwirkung des Luftverkehrsabkommens", in: Neue Zürcher Zeitung, 31 October 2001.

22 Vienna Convention on the Law of Treaties, concluded in Vienna on 23 May 1969, in force in Switzerland since 6 June 1990.

23 See Dispatch on Restructuring, Chapter 5.

24 See Dispatch on Restructuring, Chapter 5.

25 See Dispatch on Restructuring, Chapter 5.

26 See Dispatch on Restructuring, Chapter 5.

threaten to distort competition through the preferential treatment of certain firms or manufacturing branches is irreconcilable with the Treaty or with the Agreement if it harms trade between EU Member States and between contracting parties to the AAT respectively. In the guidelines on air transport[27] it is stated that the appraisal of State measures by the European Commission comprises two stages. In order to establish whether State aid has been granted, in the first stage the Commission examines the circumstances of the financial transaction, judging them according to the criteria of an investor acting according to the principle of a free market. If the Commission comes to the conclusion that the measures taken include elements of State aid (which is regularly the case when the transaction demonstrates features which lead to the supposition that a private investor in similar circumstances would not have been prepared to accept the risk), it is then determined at a second stage whether or not the State aid falls under the exemption regulations in Article 87 paragraph 3 of the Agreement and therefore is compatible with the common market.

b. Determining the presence of State aid in relation to the minority shareholding of the Swiss Confederation in Crossair

According to the guidelines on air transport[28] we are not dealing with State aid in the case of capital inputs as part of a stake held by the State in a company, insofar as the provision of capital corresponds to the number of shares held by the State and takes place at the same time that capital is provided by shareholders acting according to the principles of a free market. The principle of acting as a free-market investor is normally deemed to be satisfied when the structure and the future prospects of the company suggest that, within a reasonable period of time, normal returns are to be expected similar to those that would be expected from a similar company operating in the private sector.

In its appraisal of this aspect the Commission will normally not limit itself to short-term profit expectations. The conduct of a private investor, with whom the intervention of the public investor must be compared, does not necessarily correspond to the conduct of a normal investor who is using his or her capital in the expectation of profits more or less in the short term. This means that economic interventions may take place that are justified not just by probable profits but also, for example, as a means of enhancing the image of the company[29]. Nevertheless, just like every other investor acting in the free market, the State too must be able to count on receiving normal returns within a reasonable period of time. If no such returns are realised in either the short term or the long term, or if a similarly unhappy outcome is to be expected, then it can be assumed that the company is receiving State aid and that the State is prepared to forego the profit that an investor acting in a free market would have expected to receive from a comparable investment.

In accordance with the guidelines on Air transport[30] redevelopment and restructuring measures play a crucial role for the Commission in judging measures that affect a loss-making company in terms of the principle of acting as a free-market investor. In order to satisfy the condition of a free-market character, such measures must constitute a coherent restructuring programme. The Commission welcomes restructuring plans that have been drawn up after a study carried out by independent financial consultants. In keeping with the recommendations of the Committee of Wise Men[31] the Commission can also call on an independent expert, if necessary, in order to examine a plan's feasibility.

The restructuring plan of the Swiss Confederation in favour of Swissair must be classified as restructuring. The Federal Government used the Deutsche Bank as its financial advisor when reaching a judgment on the restructuring plan[32]. The Bank did consider that the operating assumptions for the new Crossair company were by and large reasonably predicted operating and financial results. However, the Deutsche Bank also drew attention to a whole range of major operational and financial risks. In conclusion, the Bank judged the financial participation in the new Crossair company as an investment carrying a high degree of risk[33]. As counter argument, however, it can be stated that although the expectation of profits in the short term was not considered to be positive, in the longer term growth in civil aviation could in principle certainly be expected. Since the Deutsche Bank did not judge that the minority shareholding in the context of the restructuring plan was unreasonable, it cannot be assumed that the Federal Government at that time was willing to waive its right to appropriate returns.

c. Judging the presence of aid in relation to the granting of the loan

According to the guidelines on air transport, the principle of acting as a free-market investor is also applied

27 See Air transport guidelines, Chapter IV.

28 See on the following: Air transport guidelines, Chapter IV.1.

29 ECJ, Judgment of 21 March 1991 in Case 303/88 - Italy v. Commission.

30 See Air transport guidelines, Chapter IV.1.

31 Final Report of the "Committee of Wise Men" of 1 February 1994. A committee of air transport experts was appointed as the "Wise Men" and in summer 1993 was instructed by the Commission to analyse the civil aviation industry in the EU and to submit recommendations for future political initiatives.

32 See Dispatch on Restructuring, Chapter 2.1.3.

33 See Dispatch on Restructuring, Chapter 2.1.3.

in judging whether a loan is granted in conformity with normal banking conditions and whether a commercial bank would have approved such a loan. In relation to this, both the rate of interest and the security provided have particularly to be taken into consideration[34]. The security provided must be sufficient to provide for the repayment of the loan in its entirety in the case of default. Accordingly, in the case of an unsecured loan being granted to a company which under normal circumstances would not have been afforded such facilities, the whole loan must be regarded as State aid[35]. In relation to the agreed rate of interest it is also to be assumed that an element of aid is present if the rate is below that which the airline would have had to pay under normal market conditions.

The loans from the Confederation made to Swissair are, from the point of view of EU law, to be regarded as State aid. According to Article 1 paragraph 1 of both the supplementary agreement and the basic loan agreement, the loans are interest-free and are covered by no form of security.

From the viewpoint of the AAT-derived principles therefore, under the circumstances prevailing at the time, the loan would have to be considered as State aid even though the loan agreement foresaw that the loan would have to be paid back after the liquidation of Swissair.

d. Compatibility of the aid with Article 13 paragraphs 2 and 3 of the AAT and Article 87(2) and (3) EC Treaty

When elements of State aid are present, it must be established whether the measure is still to be exempted, according to the criteria set out in Article 13 paragraphs 2 and 3 of the AAT and Article 87(3) EC Treaty respectively from the prohibition clause in Article 13 paragraph 1 of the AAT and Article 87(1) EC Treaty respectively. According to these regulations, aid measures may be compatible if they serve to further certain economic sectors or economic areas and insofar as they do not change commercial conditions in such a way as to affect the common interest adversely. According to the wording of Article 87(3) EC Treaty and Article 13 paragraph 3 of the AAT, aid must be restricted to either certain economic branches (i.e. sectors) or to certain economic areas in a regional geographic sense. The Commission, however, also includes under the heading "certain economic sectors" the aid that a Member State grants to individual companies that are experiencing economic difficulties. The requirements for State rescue and restructuring aid for firms in difficulty are spelled out by the Commission in the above-mentioned "Community guidelines on State aid for rescuing and restructuring firms in difficulty"[36]. These guidelines are valid for all aid, regardless of the economic sector concerned[37].

The requirements for determining a "firm in difficulty" are set out in Chapter 2.1. of the Rescue and restructuring guidelines[38]. A firm is considered to be in difficulty when it is not able to stem losses – by using either its own resources or any funds it has been able to obtain from its owners, shareholders or creditors – which without State intervention would almost certainly lead to the company's going out of business in the short to medium term.

By its nature rescue aid[39] has, in accordance with Chapter 2.2. of the rescue and restructuring guidelines, a temporary character. It is designed to make possible the continued operations of a company in difficulty, for as long as is necessary either to draw up a restructuring plan or receivership, or the time needed by the Commission to judge the plan. Such rescue aid may be approved by the Commission when it satisfies the requirements contained in Chapter 3.1. Thereafter, in the case of loans, a rate of interest must be demanded that is at least comparable to the interest rates that may be observed in loans granted to "healthy" companies, whereby the loans must be granted for a maximum period of twelve months. In addition, the rescue aid must be justified on acute social grounds and must not have any serious so-called "spillover" effects in other Member States. The Member State concerned is required to present to the Commission a restructuring or receivership plan within the six months following the approval of the rescue aid; otherwise within this same period it must provide proof that the loan has been repaid in full or that the guarantee has lapsed.

In contrast, restructuring is, according to Chapter 2.2., based on a realistic, coherent and extensive plan aimed at restoring the long-term profitability of a company. It extends over a longer period and includes at least one of the following elements: reorganisation and rationalisation of the company's activities, restructuring of some areas of activity and, in some cases, diversification through assuming new profitable activities. Normally the operating restructuring has to be accompanied by a financial restructuring.

34 See on the Commission criteria: Air transport guidelines, Chapter IV.2.

35 Air transport guidelines, Chapter IV.2.

36 See the remarks on the other requirements made by Valle/van de Casteele, "Revision of Rescue and Restructuring Guidelines: A Crackdown?", in: EStAL 2004, 9, and of Anestis/Mavroghenis/Drakakakis, "Rescue and Restructuring Aid – A Brief Assessment of the Principal Provisions of the Guidelines", in: EStAL 2004, 27.

37 Sector specific regulations for firms in difficulty, such as here, in particular, the guidelines for State aid in Civil Aviation, remain unaffected according to Chapter 2.3 of the rescue and restructuring guidelines. The Rescue and restructuring guidelines and the Air transport guidelines can be applied side by side.

38 The draft Community guidelines for rescue and restructuring, proposed by DG Competition on 9 January 2004, are published on the website of the European Commission http://www.europa.eu.int/comm./competition/state aid/others.

39 See in relation to this the new concept of "immediate aid" in the draft guidelines.

The requirements for the approval of a restructuring aid are spelled out in Chapter 3.2.2. For the purposes of restoring the long-term profitability of the company it will be necessary, according to Chapter 3.2.2 clause b) to submit a restructuring plan to the Commission together with the application for the approval of the restructuring. The measures set out in this plan must guarantee that after completing the restructuring the company will be capable of covering all its costs. The principle of "one time, last time", set out in Chapter 3.2.3., makes it clear that restructuring aid should be granted only on one occasion, i.e. no further applications for granting aid will be approved if they are presented within a period of ten years following the completion of a restructuring phase or the abandonment of a restructuring plan.

In the present case, firstly "Swiss" is to be regarded as a successor firm in accordance with the State aid regulations as it took over the assets and liabilities of its sister company.

The loan made by the Swiss Confederation to Swissair had, according to Article 1 paragraph 1 of the basic agreement and Article 2 paragraph 1 of the supplementary agreement, on the one hand the aim to allow Swissair to continue airline operations until the takeover of operations by Crossair. On the other hand, it enabled the orderly transfer of operations to Crossair, which was later renamed "Swiss". It is difficult to classify this clearly as a form of either rescue aid or restructuring aid, since the loan was intended to guarantee both the continuation of Swissair operations and the long-term reorganisation of the company. The difficulty in deciding on the correct classification results from the fact that even the first instalment of the loan under the basic agreement of 5 October 2001 cannot be regarded as simply rescue aid[40], as it was not intended to be of a temporary nature, as the rescue and restructuring guidelines provide[41], nor was it simply intended to bridge the gap until a decision was made on the restructuring plan. The plan, named the "Phoenix Rescue and Restructuring Plan"[42], in which the loans were also foreseen, was approved by the parties involved on 1 October 2001; on the same day the Federal Council decided to support the plan. By October a reduced flight schedule was already in operation.

Under the existing guidelines, however, it is not permitted to carry out restructuring activities in the rescue aid phase. Drawing a line between rescue and restructuring aid is not without its difficulties, since very often firms that find themselves in financial difficulties are already in the rescue phase left with no alternative but to adopt structural measures as a matter of urgency in order to prevent, or at least to limit, the deterioration of their financial situation. The draft of the new guidelines on the assessment of rescue and restructuring aid provides for the introduction of the new term, "immediate aid"[43]. Immediate aid has the same objective as rescue aid, but also enables the beneficiary to take immediate measures that are structural in their nature, such as the immediate closure of a branch office or withdrawal from loss-making areas of activity in some other way.

The loan made by the Confederation to Swissair would therefore have had to have been assessed under the currently valid rescue and restructuring guidlines as a hybrid; if assessed under the proposed future guidelines, it would have been classified as immediate aid.

Irrespective of its classification as rescue or restructuring aid, there are grounds for arguing that the loan could not be regarded as being compatible with either the AAT or the EC Treaty. From this point of view, it constitutes an infringement of the rescue and restructuring aid guidelines if loans are granted on an interest-free basis and fail to comply with the maximum term of twelve months.

4. "One time, last time" principle and existing aid

As already mentioned, a draft of the revised guidelines on rescue and restructuring aid has been tabled. This draft provides for the reinforcement of the principle of "one time, last time"[44]. While in the currently valid guidelines it seems that this principle applies only to restructuring aid and not to rescue aid, the draft guidelines expressly indicate that it applies to rescue aid as well[45].

As there are grounds for arguing that the loan from the Confederation to Swissair is to be regarded under the currently valid guidelines as restructuring aid (or under the draft guidelines as immediate aid) and insofar as subject to the "one time last time" principle, the specific question definitely arises of whether or not the support measures described above must now be examined retrospectively by the Competition Commission for compliance with the AAT.

Under Article 1 b) i) of the Regulation (EC) 659/1999[46], irrespective of the provisions of the Vienna Convention[47], all aid that existed before the Treaty

40 But see Dispatch on Restructuring, Chapter 5.

41 See Rescue and restructuring aid guidelines, Chapters 10 et seq.

42 Later "Phoenix +".

43 See the introduction to the draft guidelines, Chapter 1.6.

44 See Commissioner Monti's speech "New developments in State aid Policy", British Chamber of Commerce, Brussels, Belgium, 1 December 2003.

45 See draft guidelines, Chapter 3.1.

46 See above II. 2.

47 Article 18 Vienna Convention on the Law of Treaties, see above III. 2.

came into force (i.e. State aid schemes and individual instances of State aid, that were introduced before the accession of the relevant Member State to the EU and remain applicable after its accession) is to be regarded as existing aid[48]. In relation to Switzerland and the AAT, it could therefore be argued on behalf of the EU that in particular the loan granted as part of the restructuring plan before the AAT came into force represents an existing aid and accordingly would have to be examined by the Competition Commission. If this were the case, "Swiss" would already have made full use of its "one time, last time" privilege and any future aid would be unlawful. As already mentioned above, the Swiss Government is of the opinion that the AAT could not have any retroactive effects in this respect and therefore "Swiss" had not made any use of the "one time, last time" privilege. It is also of the opinion that there is no existing aid, even though an amount of about CHF 300 million of the loan has not yet been claimed and is still available for "Swiss" to take up[49].

Even if, however, the loans should be regarded as contrary to the AAT, it must be taken into consideration that they were approved by the Swiss Parliament and it is doubtful whether the proposed Article 103 of the FAA mentioned above would cover loans approved by the Swiss Parliament.

In the following remarks, a brief analysis is provided of the new support measures that do not form part of the restructuring plan.

5. Support measures for "Swiss" falling outside the restructuring plan

Despite constant efforts towards rationalisation, and several reductions of overheads and capacities, in its first financial year "Swiss" recorded a loss of CHF 1 billion; this was due to the state of the market and also to internal problems of its own. Following further drastic cutbacks in staff and airline operations, the government exempted "Swiss" in June 2003 from the payment of the mineral oil tax on domestic flights (which meant an annual saving of around CHF 6 million)[50] and agreed to pay the cost of special flights for the repatriation of foreign nationals[51] (CHF 0.9 million per annum).

In addition, the Federal Council looked into issuing a "Letter of Comfort"[52], in which the Swiss Government would express its confidence in the company and on the basis of which "Swiss" hoped, inter alia, to be able to purchase aircraft on more favourable conditions.

Following the melting away of the equity of "Swiss" from an original amount of over CHF 2.6 billion at the launch of the new airline to CHF 1.084 billion at the end of September 2003, predicted to fall well under a billion by the end of 2003, and after the share capital had been reduced to CHF 1.681 billion, a further reduction in capital in 2004 is probably inevitable[53]. For some time "Swiss" has already been negotiating with banks for an operating loan. Four banks – the Swiss major banks UBS and Credit Suisse and the British banks Halifax Bank of Scotland (HBOS) and Barclays Bank – were working towards getting this loan for "Swiss", amounting to around CHF 400 million, off the ground[54]. The banks have made it clear from the outset that any overall package must also include commitments from other shareholders. A loan from these shareholders amounting to CHF 70 million is under discussion, secured by the same guarantees as those given for the loans from the banks. The principal shareholders in "Swiss" are the Swiss Confederation with 20,4% of the shares, the canton of Zurich, UBS and Credit Suisse, each with around 10% of the shares, the private individual Walter Haefner with 6,8%, followed by Nestlé, Novartis, Roche, Swisscom, Swiss Re and Zurich Insurance, which have each obtained a shareholding of 3,4% through the injection of CHF 100 million each. To date, Swisscom has shown its willingness to back "Swiss" for a second time with a small loan in the order of CHF 10 million. Likewise, it is understood that Walter Haefner is prepared to make additional funds available to "Swiss".

6. Appraisal of the measures outside the restructuring plan[55]

a. Exemption from mineral oil tax and assumption of repatriation costs

Under the guidelines on air transport[56], tax breaks such as the reduction of or a moratorium on tax debts or social security contributions do amount to State aid in terms of Article 87(1) of the EC Treaty if the firm involved obtains a competitive advantage as a result and is relieved of costs that would normally have to be met from its own financial resources, with the result

48 See ECJ, OJ 2003 L 209/1.

49 See footnote 19 above.

50 See press release from the Federal Chancellery of 25 June 2003, "Begleitmassnahmen des Bundes für „Swiss"-Restrukturierung"; "Der Bundesrat stärkt der Swiss die Flügel", in: Neue Zürcher Zeitung, 26 June 2003.

51 See press release from the Federal Chancellery of 25 June 2003, footnote 50 above.

52 See press release from the Federal Chancellery of 25 June 2003, footnote 50 above.

53 See Beat Bumbacher, "Swiss konnte 2003 ihre Auslastung verbessern – Ermutigende Entwicklung im 4. Quartal", in: NZZ Online, 15 January 2004.

54 S. Birgit Voigt, "Bettelbrief an die Swiss-Aktionäre, Swisscom-Chef Jens Alder bittet persönlich um Kredit für Swiss bei ausgewählten Wirtschaftsführern", in: NZZ am Sonntag, 18 January 2004.

55 Cantonal measures are not considered in this article. According to the proposed Article 103 FAA, they are also covered and follow the same assessment criteria.

56 Air transport guidelines, Chapter II.4.

that market forces cannot exert their normal effect[57]. Although a measure through a State authority granting to a certain firm a tax exemption that is not tied to a handout of State resources, but which leaves the beneficiaries in a better position than other tax payers does amount to State aid in terms of Article 87(1) EC Treaty[58], it must also be taken into consideration if there is no mineral oil tax on domestic flights for competitors either. If "Swiss" does not find itself in a privileged position, this exemption from the mineral oil tax does not amount to a State aid.

Assumption of the repatriation costs of persons who are not entitled to enter Switzerland takes effect only in those repatriation cases for which "Swiss" cannot be held responsible. Accordingly, in the opinion of the writer, this cannot be regarded as aid in terms of Article 13 of AAT or of Article 87 EC Treaty.

b. Operating loan

By their nature, operating loans from banks cannot be regarded as State aid. In the present case, the loan being sought is to be regarded as an overall package, as the other principal shareholders would also have to commit themselves to it, including the Swiss government. In the event that the Swiss government were to decide to offer its backing as one of several principal shareholders, the measure would not, based on the concept of the investor acting in a free market, be regarded as a State aid.

So far, however, only Swisscom and Walter Haefner are known to have expressed their willingness to participate in a further loan. Equally, it cannot be excluded that the remaining private shareholders will refuse to make any further commitment; it is even possible that the consortium of banks will not wish to take the risk of offering a further loan. In such an extreme situation, the Swiss Confederation would ultimately come into view as virtually the only possible lender. At first sight, such a commitment by the Confederation would appear unobjectionable in that there are additional cash-providers in the shape of Swisscom and Walter Haefner. Here though, the following must be taken into account: the Swiss Confederation still holds 62,73% of the shares in Swisscom and thus controls that company. There are good arguments to consider that it would therefore be the Swiss Confederation and not an investor acting in the free market that would be paying. As a result, such a loan would have to classified as State aid if the federal government were to approve through Swisscom a loan that a private company would not have granted.

It would also be decisive to consider how the granting of a loan by a wealthy Swiss private individual[59]would be assessed. In this connection, it must be examined whether the private investor is also truly acting in the free market. This would be answered in the negative if he was not acting for recognised economic reasons. Thus it is at least open to question whether or not, if one of Switzerland's richest men whose personal wealth is estimated at up to 11 billion Swiss francs ($6.70 billion)[60] is ready to support "Swiss" again because his car import empire has always followed the fate of Swissair Group and its employees with great sympathy, and given that the majority of the other private investors have voted against a further loan, this private handout would be enough to legitimise the State measure.

c. Letter of comfort

Under the broad definition of State aid, it cannot be excluded at least that a "letter of comfort" has to be examined against the requirements of Article 13 of the AAT and Article 87 EC Treaty. A "letter of comfort" would certainly not be legally binding, but would nonetheless have the aim of improving the financial position of "Swiss". It might in certain circumstances have to be measured against the criteria for assessing credit guarantees.

In a circular dated 5 April 1989[61], the Commission stated that all credit guarantees that are issued either directly by a State or through an authorised credit institution are considered to fall under the terms of Article 87(1) EC Treaty. The element of aid in the case of a credit guarantee corresponds to the difference between the interest rate paid by the borrower in the free market and the rate actually paid as a result of the credit guarantee, after deduction of the premiums paid in respect of the credit guarantees. If, in view of the parlous financial situation of an airline, no financial institution were prepared to grant a loan without a State credit guarantee, the full amount of the loan could be regarded as aid[62].

A "letter of comfort" would therefore probably be regarded as aid under Article 13 of the AAT and Article 87 EC Treaty if it were crucial for obtaining financial support. To date, however, no specific application has yet been made to the Federal Council.

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57 ECJ, Judgment of 14 February 1990 in Case C-301/87 - France v. Commission, [1990] ECR I-1990, page 307, No 41, page 362.

58 ECJ, Judgment of 15 March 1994 in Case C-387/92, [1994] ECR I-877.

59 See Werner Enz, "Wenig Zuspruch für die Swiss-Finanzhilfe – Nach der Swisscom will auch Amag-Gründer Haefner Hilfe anbieten", in: Neue Zürcher Zeitung, 20 January 2004.

60 See Michael Shields, "Swiss billionaire to help airline", in CNN.com, 13 October 2001.

61 See Air transport guidelines, Chapter IV.3., letter of 5 April 1989, supplemented by a letter of 12 October 1989.

62 Commission Ruling of 7 October 1994 in Case C-14/94 - Olympic Airways, OJ 1994 L 273/22.

7. Conclusions

Although the Air Transport Agreement between Switzerland and the European Union has been in force since 1 June 2002, the substantive and procedural law requirements for implementing in Switzerland the provisions on State aid still have to be defined in precise terms. In addition, no Supervisory Authority has yet been properly set up. There is therefore an immediate need for action in order to be able to comply with the AAT in this area. This is all the more urgently required as the State support measures in connection with "Swiss" give rise to serious questions. Whatever the case, future measures to be taken by the Swiss Confederation may only be approved after they have been very carefully examined to ensure compliance with Article 13 of the AAT. In particular, the issue of the assessment of the 2001 restructuring plan must be clarified once and for all.