

# State aid and competitive neutrality: allies or opponents? 1/3/25



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State aid and competitive neutrality are the two important principles for public entities that must be respected to ensure the fairness and efficiency of their activities in the market. These principles are essential to prevent market distortions and promote fair competition between public and private companies. While these concepts have recently gained more attention, their interactions have not yet been sufficiently explored. This article discusses how they influence and complement each other.

## Are the competitive neutrality and state aid the same thing?

State aid and competitive neutrality are closely linked but different concepts. State aid is any such aid granted by a public entity out of public funds which distorts or may distort competition by favouring certain enterprises or the production of certain goods in so far as it affects trade between Member States<sup>1</sup>.

Competitive neutrality is a broader principle that derives from the laws and regulations governing the activities of a public entity and is enshrined in Section 1 of the Competition Law. The said section obliges public entities to ensure free and fair competition under the same conditions as private enterprises. The principle of competitive neutrality is based on the idea that the market is most efficient when all players operate under the same conditions. Neutrality ensures that market participants compete based on their capabilities and effectiveness rather than the conferred political or financial advantages.

## Can a breach of competitive neutrality be established even if the rules on state aid are complied with?

At first glance, it appears that state aid is not compatible with competitive neutrality, as certain companies are conferred an advantage. However, a simultaneous analysis of the two principles leads to the conclusion that the rules on state aid control actually contribute to ensuring competitive neutrality.

Under The Competition Law the principle of competitive neutrality does not apply if the activity in question arises from requirements laid down in other laws. Thus, if a public entity grants or receives state aid that complies with the requirements of the Law on the Control of Aid for Commercial Activity, the aspect of competitive neutrality is not assessed and it could be assumed that competitive neutrality has been complied with because the rules prevent undue distortion of competition. (e.g., in the case of a contract for the provision of a service of general economic interest).

In order to ensure competitive neutrality, it is important that state aid is granted in a transparent and limited manner. Before granting aid, a thorough assessment is required to ensure that the public intervention is necessary and that the aid is granted in the most effective way.

In practice, however, there may be situations where the aid granted does not fall within the definition of state aid, for example if it has only local effects or if the state aid control framework is not applied accurately. In addition, there are cases where an advantage has been granted by a public entity without

having been assessed under the state aid rules, resulting in an undue advantage to public undertakings. Such an advantage may, for example, take the form of access to information that is not available to private enterprises. In such cases, the principle of competitive neutrality must be strictly observed. Failure to do so may result in a breach of both the principle of state aid and the principle of competitive neutrality.

The Competition Council also examines the aspects of competitive neutrality for public funding projects that do not fall under the definition of state aid. For example, the Competition Council has determined that the restriction of applications to legal entities for projects supported by the State Culture Capital Foundation (SCCF) constitutes unlawful discrimination against self-employed individuals and is contrary to the principle of competitive neutrality. After discussions with the SCCF, this restriction was removed.

Public entities can influence the conditions of competition not only through legal framework, but also through the activities they carry out on the market as part of their economic activity through corporations.

## How do we ensure the competitive neutrality?

In order to ensure the competitive neutrality, public entities must comply with a number of principles, including:

1. Cost-based pricing: prices must be set on a similar basis to those of private enterprises, including all related costs.
2. Segregating accounting: structural and functional segregation of economic activities and public functions must be ensured in order to avoid cross-subsidisation.
3. Equal conditions: equal access to the market, resources and infrastructure must be ensured so as not to expose private enterprises to stricter regulation and to ensure that there are no undue advantages for public entities.

## Conclusions

State aid and competitive neutrality are aimed at contributing to the fair and efficient functioning of the internal market in the European Union by preventing market distortions. Properly granted state aid can contribute to maintaining competitive neutrality. In cases where state aid rules do not apply, it is important that the public sector acts in accordance with the principle of competitive neutrality. When the public sector enters the market, it must be ensured, through independent and effective supervision, that competition is not distorted and that the competitiveness of the private sector is not jeopardised. If you need in-depth consultation or assistance on competition law issues, please contact PwC's subject-matter experts.

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<sup>1</sup> For more on the state aid concept see this PwC MindLink.lv publication.