

Capital increase: How to ensure compliance with EU regulations? 1/21/25



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State support for companies is often associated with direct subsidies, grants, or tax reliefs. However, a state or municipal investment in a company's share capital, which may take the form of acquiring shares or stocks, in-kind contributions (such as the transfer of real estate or equipment), or recapitalisation, also constitutes a form of state aid. It is important to remember that any public investment in a company's share capital, if it meets the criteria set out in Article 107 of the Treaty on the Functioning of the European Union (TFEU), is considered state aid and is subject to EU regulation. This is a grave error that Member States occasionally make, as they fail to recognise that any such investment must be assessed against these criteria, which may otherwise result in the granting of unlawful state aid.

The purpose of the investment is the decisive factor

When assessing whether an investment constitutes state aid, its purpose is a key factor. For example, if the state contributes real estate to the share capital of a state-owned company, it must be determined whether the property will be used for economic activity (e.g., leasing) or for public administration purposes. If the property is used for economic activity, the investment must be assessed in line with EU state aid rules for commercial activity, evaluating whether all four criteria of state aid are met. For more information on the nature of state aid, read this article.

Market conditions and the Market economy investor principle

To avoid granting an economic advantage and to ensure that the investment does not qualify as state aid, it is especially important that the state or municipal investment is made under market conditions. This means that the amount and terms of the investment must not be more favorable than those a private investor would accept under similar circumstances. For example, if the state contributes real estate to a company's share capital at a price below market value, or offers other preferential terms, such a transaction may be considered state aid. Therefore, it is essential to carry out an independent asset valuation and prepare a detailed justification of the economic rationale behind the transaction. For more information on the Market economy investor principle, read this article.

Investments in companies facing financial difficulties

State investment in share capital is particularly important for companies in financial difficulties. Well-known examples in Latvia include the state investments in AS "Air Baltic Corporation" ("airBaltic") and VAS "Riga International Airport," which were authorised by the European Commission to ensure compliance with EU state aid control rules. These cases illustrate that state investments can serve both as one-off measures and as long-term stabilisation instruments. It is important to remember that phased investments and any changes to the conditions of support must also be reassessed and authorised in accordance with EU rules.

Aspects of capital reduction

A reduction in share capital — that is, the withdrawal of public funds — can also be considered state aid if it does not comply with the Market economy investor principle. Therefore, such actions must also adhere to EU state aid control regulations. Just like making an investment, the withdrawal of an investment must be assessed in light of market conditions.

Conclusions

A state or municipal investment in a company's share capital is a significant form of state aid that can create competitive advantages and must therefore be carefully assessed in line with EU regulations. Examples from Latvia clearly demonstrate how this type of support can be critical for the survival of strategically important companies. This highlights the need to respect market conditions, apply the Market Economy Investor Principle, and ensure a well-justified decision-making process. PwC subject matter experts provide advice and support on state aid matters, helping clients navigate the complex regulation and make strategically sound decisions. Contact us if you need additional information.