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**NORDIC AVIATION GROUP AS – ITS RELATION TO AS
ESTONIAN AIR AND APPLICABILITY OF THE
DEGGENDORF PRINCIPLE IN THE CONTEXT OF
RECEIVING STATE AID**

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ABSTRACT

The thesis aims to examine if there is a legal basis to apply the *Deggendorf principle* to Nordic Aviation Group AS and can the undertaking be seen as a successor of the state-owned airline AS Estonian Air which filed bankruptcy after receiving a negative recovery decision from the European Commission. The research is conducted by using theoretical qualitative methods. The research question is: Is Nordic Aviation Group AS a successor of AS Estonian air and does *Deggendorf principle* apply in the situation? The hypothesis of the research is that Nordic Aviation Group AS cannot receive state aid because of the *Deggendorf principle*.

AS Estonian Air received state aid incompatible with the internal market from the Estonian government and Nordic Aviation Group AS might not receive new aid until the old aid is recovered in accordance with the *Deggendorf principle* if these undertakings are seen as successors. The results of the research illustrate together with the *Deggendorf* case law and the principle of economic continuity that Nordica and Estonian Air have a legal and financial relation.

Keywords: competition law, state aid, *Deggendorf principle*, successor, economic unit, economic continuity

INTRODUCTION

Member states of the European Union (EU) can receive state aid in accordance with criteria laid down in Article 107 of the Treaty on the Functioning of the European Union (TFEU). The state aid must be compatible with the internal market. The State aid Control aims to ensure that the intervention of the government does not distort the competition.¹

The core principles of the State aid rules have not changed significantly during the past decades, however, these core principles have been specified by the European Commission's (the Commission) guidelines and recommendations and the Court of Justice of the EU case-law.²

In accordance with the *Deggendorf principle*, an undertaking cannot receive new compatible state aid if its successor has not paid the incompatible state aid back if certain criteria are fulfilled. The Commission evaluates each individual situation. To determine whether the *Deggendorf principle* applies or not it must be understood what a legal and financial successor is as it also applies to successors of an undertaking.

The state aid policy in the EU leaves gaps when determining how to act in the situation when the receiver of incompatible and unlawful aid cease to exist. Establishing a relation between two companies is challenging if there is no proof of them having an economic or legal connection and if the companies argue that they have no relation.

This thesis will focus on two companies and their relation, AS Estonian Air (Estonian Air) and Nordic Aviation Group AS. In 2015 AS Estonian Air, an Estonian state-owned airline, filed bankruptcy after the Commission giving its negative recovery decision according to which the

¹ Kurcz, B., & Vallindas, D. (2008). Can general measures be... selective? Some thoughts on the interpretation of a state aid definition. *Common Market Law Review*, 45(1). p. 159

² Veebel, V., Ploom, I., & Kulu, L. (2015). Shortcomings of the EU state aid model from peripheral perspective: the case of Estonian Air. *Baltic Journal of Economics*, 15(1), 50-64. p. 50

state aid received from Estonian Government is incompatible with Article 108(3) TFEU and therefore the company was obligated to recover the incompatible and unlawful aid.³

Nordic Aviation Group AS doing business as Nordica, also an airline owned by the Estonian government, was established in 2015 right after Estonian Air filed its bankruptcy. The establishment of one state-owned company right before the other one declared bankruptcy raises legal concerns from the Competition law perspective. How should Nordica be seen in state aid matters especially when Estonian Air has had competition law infringements? Should Nordica be seen a legally and financially independent company or as a successor of Estonian Air which would lead to the “successor’s liability” of having legal and financial obligations towards Estonian Air.

The Harju County Court decided in September 2020 that Nordica is responsible for Estonian Air’s unpaid salaries to its employees.⁴ The decision was appealed and in March 2021 the Tallinn Circuit Court held to the County Court’s decision, meaning that Nordica shall compensate EUR 1.5 million to the Estonian Air’s former employees for their unpaid salaries.⁵ At the time of conducting the thesis the access to the decisions is restricted and therefore the author of the thesis has not referred directly to the decisions.

The thesis was conducted during the ongoing COVID-19 pandemic, therefore, these aspects will be analyzed in a sub-paragraph. The Commission actually granted Nordica a measure of EUR 30 million due to the COVID-19 pandemic in accordance with the Temporary Framework.⁶ The undertaking is at the same time receiving support due to the pandemic and claimed to be responsible for Estonian Air’s salaries which also raises questions. The situation is challenging when it comes to the context of Nordica being eligible of receiving state aid before Estonian Air’s incompatible state aid is paid back.

³ Commission Decision (EU) 2016/1031 of 6 November 2015 on the measures SA.35956 (13/C) (ex 13/NN) (ex 12/N) implemented by Estonia for AS Estonian Air and on the measures SA.36868 (14/C) (ex 13/N) which Estonia is planning to implement for AS Estonian Air, OJ L174/1.

⁴ Vaino, R. (2020) *Court orders Nordica to pay unpaid salaries to former employees*. Accessible: <https://news.err.ee/1129798/court-orders-nordica-to-pay-unpaid-salaries-to-former-employees>, 2.11.2020

⁵ Wright, H. (2021). *Court rejects Nordica’s back pay appeal for Estonian Air employees*. Accessible: <https://news.err.ee/1608157453/court-rejects-nordica-s-back-pay-appeal-for-estonian-air-employees>, 28.3.2021

⁶ European Commission (2020) “State aid: Commission approves €30 million Estonian measure to support Nordica in the context of the coronavirus outbreak” Press release. Accessible: https://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_SA_57586, 28.3.2021

The thesis aims to underline the legal basis to apply *Deggendorf principle* to Nordica. The relation between the two undertakings Nordica and Estonian Air will be analyzed, i.e., is Nordica Estonian Air's legal and financial successor and can *Deggendorf principle* be applied or not. The hypothesis is that Nordica cannot receive "new" state aid because of the Deggendorf principle.

The author of the thesis introduces both companies and the state aid regime in the EU in the first section. Also, the COVID-19 situation in the light of state aid matters is discussed in the first section. In the second section *Deggendorf principle* and related case law is discussed. The third part analyzes the concept of an economic unit and the economic continuity.

1. BACKGROUND

The EU State aid regime is introduced and more specifically the rules and process of receiving state aid. Also, the two airlines Estonian air and Nordica are introduced in this section. The legal relation between them is discussed and how the COVID-19 pandemic has affected the granting of state aid and more specifically in the scope of Nordica.

1.1 European Union on state aid regime

The primary EU law concerning state aid rules can be found in the TFEU. State aid can be defined as any economic advantage granted by the national public authorities to an undertaking. It is important to define what an undertaking to understand the applicability of EU competition law.⁷ An undertaking is an entity engaged in economic activity.

Both the Commission and the national courts have an important role when considering the enforcement of state aid rules. However, their role can be easily distinguished. The Commission has a “competence to rule on the substantive issue of the compatibility of State aid with EU law” and the national courts ensures that State aid measures will not be implemented without the Commission’s approval.⁸

In general, the Article 107(1) TFEU prohibits granting state aid to undertakings by Member States, since it gives an advantage to the undertaking compared with its competitors (general prohibition), i.e. distorts competition. There are four conditions set out by the Article 107(1) TFEU and if those all are cumulatively met the aid granted to an undertaking can be seen as state aid.

⁷ Kloosterhuis, E. (2017). Defining non-economic activities in competition law. *European Competition Journal*, 13(1), 117-149. p. 117

⁸ Goyder, J., & Dons, M. (2017). Damages Claims Based on State Aid Law Infringements. *European State Aid Law Quarterly*, 16(3), 416-428. p. 416

Firstly, the measure shall be granted by or through State resources.⁹ Secondly, it must give the undertaking(s) an advantage.¹⁰ Thirdly, the measure shall be selective and lastly, it shall distort or threaten to distort the competition.¹¹

The condition of a measure being granted by or through State resources do not constitute any aid received from private resources even though the funds went via the State.¹² The advantage condition is fulfilled if it can clearly be seen that the undertaking receiving the aid has improved due to receiving it.¹³ Selectivity is widely interpreted and includes *inter alia* general tax exemptions.¹⁴ To simplify the selectivity condition refers to that State aid shall not be granted to all undertakings in the Member States, only to selected ones.¹⁵ The measure threatening to distort or distorting the competition and affecting the trade in the single market refers to the main importance of the European Union state aid policy.

1.1.1 Exceptions

Even though Article 107(1) declares any state aid as incompatible, the prohibition is yet not absolute and exceptions are laid down mainly in the Article 107(2) TFEU. If one of the conditions set out in the Article the state is seen as compatible with the internal market. These conditions are aid with social character for consumers, aid compensating damage by a natural disaster or other exceptional occurrence and aid granted for the Federal Republic of Germany due to historical reasons.¹⁶

Moreover, Article 107(3) TFEU also lays down exceptions when the aid can be seen as compatible with the internal market. Namely, aid promoting economic development, projects of common European interest, certain economic activities of certain areas, culture and heritage conservation and other categories of aid which might be specified by the Council.¹⁷

⁹ Bacon, K. (2017). *European Union law of state aid*. Oxford University Press. p. 12

¹⁰ *Ibid.*

¹¹ *Ibid.*

¹² Koenig, C., & Kühling, J. (2002). EC control of aid granted through State resources. *European state aid law quarterly*, 1(1), 7-18. p.7

¹³ Craig, P., De Búrca, G. (2015). *EU Law: Text, Cases, and Materials*. 6th Ed. Oxford: Oxford University Press. p. 1138

¹⁴ Schmauch, M. (2012). *EU Law on State Aid to Airlines: Law, Economics and Policy*. Lexxion Verlagsgesellschaft. p.116

¹⁵ López, J. J. P. (2015). The Concept of State Aid Under EU Law: From internal market to competition and beyond. *Oxford Studies in European Law*. pp. 144-150

¹⁶ Craig, P., De Búrca, G. (2015), *supra nota 13*, pp. 1139-1140

¹⁷ *Ibid.*, pp. 1140-1144

In addition to the exceptions introduced above in 2008 the Commission introduced the General Block Exemption Regulation (GBER).¹⁸ The GBER states that regional aid granted to SMEs can be exempt if favoring R&D, environmental protection etc.¹⁹ The GBER does not apply to undertakings which are subject to the *Deggendorf* recovery order.²⁰

1.1.2 Recovery decision

Any state aid not compatible with the common market is automatically incompatible and thus illegal. The only consequence of an illegal state aid is recovery whereas in general the undertaking who received illegal state aid has to pay it back with interest even if it will lead to the financial difficulties or create insolvency.

Only due to an absolute impossibility the undertaking must not recover the incompatible state aid since “no one is obligated to do the impossible” in accordance with the EU’s principles.²¹ A financial difficulty does not constitute the meaning of an absolute impossibility unless the undertaking has been liquidated, however, the responsibility does not cease to exist if the undertaking has an economic or legal successor.²²

Since the responsibility does not cease to exist even though the undertaking files bankruptcy if there is an existing successor it means that Nordica might be demanded to compensate the incompatible aid which might prevent it from receiving new compatible aid.

There is a slight difference between the State aid and antitrust infringements. In antitrust matters the Commission shall identify who is responsible but in State aid matters the responsibility of

¹⁸ Commission Regulation (EC) No 800/2008 of 6 August 2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty (General block exemption Regulation), OJ L 214, 9.8.2008, p.1

¹⁹ *Ibid.*

²⁰ Deiberova, K., & Nyssens, H. (2009). The new General Block Exemption Regulation (GBER). *European State Aid Law Quarterly*, 8(1), 27-38. p. 29

²¹ Commission Notice (EU) on the recovery of unlawful and incompatible State aid, OJ C 247, 23.7.2019, See 2.4.1.4

²² *Ibid.*

identifying the beneficiary is on the Member State, more specifically, on the Member State organ which is executing the recovery.²³

The purpose of recovery of incompatible state aid is not trying to return to the *status quo ante*, rather to maintain a level-playing field in the internal market.²⁴ The failure to recover the state aid is to be taken seriously and so has the Commission acted by not leaving any discretion to the national authorities.²⁵ The Commission can refer its concerns straight to the Court of Justice of the EU in accordance with Article 108(2) TFEU if an undertaking do not recover the incompatible aid in accordance with the Commission's decision.²⁶

If the Commission gives the Member state a negative recovery decision and the Member State does not implement it the Commission might rely on the *Deggendorf principle* in the future (if the undertaking or its beneficiary applies for new state aid).

1.2. AS Estonian Air

Estonian Air, a flag carrier owned by the Estonian government was established in 1991 after the collapse of the Soviet Union. The company had its head quarter at Lennart Meri Airport located in Tallinn. Estonian air participated in a joint venture with Aviokütuse Teenuste AS which is engaged in refueling the aircrafts at the Lennart Meri Airport in Tallinn. In 2004 when Estonia joined the EU, it opened up wider possibilities for Estonian Air also meaning that the company had to comply with the EU's state aid policy, i.e., the competence was transferred to the Commission. Estonian air participated in a joint venture with Aviokütuse Teenuste AS which is engaged in refueling the aircrafts at the Lennart Meri Airport in Tallinn.²⁷ The undertaking faced financial losses since 2006, and from 2010 until 2011 the undertaking lost more than one quarter of its capital.²⁸ Despite capital injections and increases received the net loss continued to increase

²³ Monti, G. (2011). Recovery Orders in State Aid Proceedings. *European State Aid Law Quarterly*, 10(3), 415-424. p. 415

²⁴ Commission Notice (EU) towards an effective implementation of Commission decision ordering Member States to recover unlawful and incompatible State aid, OJ 272, 15.11.2007, See 2.2.1

²⁵ Goyder, J., & Dons, M. (2017), *supra nota* 8, p. 423

²⁶ D'Sa, R. M., & Drake, S. (2010). Financial penalties for failure to recover state aid and their relevance to state liability for breach of Union law. *European State Aid Law Quarterly*, 9(1), 33-46. p. 33

²⁷ Commission Decision (2015), *supra nota* 3, 23

²⁸ *Ibid.*, 23-24

and in 2014 the undertaking had a net loss of EUR 10.4 million.²⁹ Thus, it can be understood that the undertaking had financial difficulties.

According to the Commission's decision Estonian Air had received state aid which was incompatible with the internal market from the Estonian government.³⁰ The decision states that the capital injection implemented in 2009 breaches Article 107(1) TFEU and state aid received in 2010 (EUR 17.9 million), 2011 (EUR 30 million), 2012-2014 (EUR 37 million) is incompatible with the internal market and breaching Article 108(3) TFEU.³¹

As the state aid received was considered incompatible with the internal market and therefore unlawful by the Commission, the Estonian government received a negative recovery decision meaning that the incompatible state aid must be recovered in accordance with the decision.

However, the state-owned undertaking decided instead to file for bankruptcy meaning that the incompatible state aid has not been recovered. The question arises whether Estonian Air tried to escape the recovery of the incompatible state aid by filing bankruptcy after the Commission's decision or not.

1.3 Nordic Aviation Group AS

Nordica, also a state-owned airline was founded in 2015 right after Estonian Air filed bankruptcy. The undertaking has two subsidiaries Xfly (previously Regional Jet OÜ) and Nordic Aviation Advisory OÜ and also cooperates with the Polish state-owned LOT Polish Airlines. The former CEO of Estonian Air Jan Palmer is now Xfly's CEO, meaning that the head of Estonian Air is also engaged in Nordica.

Nordica has only received state aid under the COVID-19 due to an exceptional disturbance in the economic activity which will be discussed further on in the thesis, but no other state aid. However,

²⁹ Commission Decision (2015), *supra nota* 3, 23-24

³⁰ *Ibid.*, Article 1-3

³¹ *Ibid.*

the Estonian government has given a green light and showed its willingness to grant cash injections to the undertaking. In June 2020, the former finance minister Martin Helme pointed out that funds will not be allocated to the company before knowing if it is considered as state aid to avoid what happened to Estonian Air. Thus, one can assume that the Estonian government was also unsure how the relation of Estonian Air and Nordica would be seen in the state aid context.

As mentioned, the author of the thesis cannot refer directly to the Harju County Court's and the Tallinn Circuit Court's cases as they cannot be accessed by the general public at the time of writing the thesis. Tallinn Circuit Court gave its decision of Nordica being responsible for Estonian Air's unpaid salaries³², there must be a weighty reasoning for it. It seems that the undertaking is ready to pay for the salaries but not willing to recover Estonian Air's unlawful and incompatible state aid and was perhaps not prepared of being a successor of Estonian Air.

However, in June 2021 the former employees of Estonian Air signed an agreement with the Nordic Crew Management (NCM) annulling the previous decisions.³³ NCM is engaged in staffing flight crew for the undertakings which has been used by Nordica's subsidiarity Xfly.³⁴ As the details of the agreement are classified it cannot be analyzed why the counterparties reached an agreement, however, it has been pointed out that now it can be ensured that there will be enough of crew while opening up new flight routes.³⁵

The situation is tense and no situation of exactly this kind can be found to rely in the EU state aid scope. Nordica's and Estonian Air's relation is complex as it is not evident if the same economic activity continued or not and even though some similarities can be found in previous *Deggendorf* cases none has been the same as the situation with Estonian Air and Nordica. If Estonian Air had not declared bankruptcy the relation between these two oughts to be easier to determine.

³² Wright, H. (2021), *supra nota* 5.

³³Wright, H. (2021). *Court rejects Nordica's back pay appeal for Estonian Air employees*. Accessible: <https://news.err.ee/1608261723/former-estonian-air-employees-abandon-nordica-lawsuit>, 2.7.2021

³⁴ *Ibid.*

³⁵ *Ibid.*

1.3.1 Successor liability

The concept of “successor liability” in the state aid context refers to the successor being liable for company’s competition law infringements. Even though the legal entity changes its name, nature of business or structure, the successor can be held liable for the earlier made competition law infringements.³⁶ The situation is challenging when the companies do not have a clear link, i.e. they are not beneficiaries and the company infringing the Competition law has ceased to exist.

Reflecting the successor liability on Estonian Air and Nordica, it is understood that Estonian Air has performed a competition law infringement meaning that Nordica can be held liable due to the successor’s liability if we hypothetically assume that Nordica is Estonian Air’s successor.

1.3.2 COVID-19 and state aid

COVID-19, the still ongoing pandemic has affected the whole world significantly. It is not surprising that it has also affected the measures of granting state aid. Due to the financial crisis in 2008, the Commission adopted a Temporary Framework allowing Member states to adopt additional state aid measures.³⁷ In 2020 the Temporary Framework was introduced by the Commission to enable additional support for undertakings due to the COVID-19 pandemic.

It is clear that the pandemic has especially hit the aviation industry due to travel restrictions. Therefore, it is obvious that the Temporary Framework includes especially the aviation sector when it comes to ensuring additional support for undertakings.

In accordance with Article 107(2)(b) TFEU aid making good damage due to a natural disaster or exceptional occurrence is incompatible with the internal market. Also, according to Article 107(3)(b) TFEU an aid to remedy a serious disturbance in the economy of a member state is compatible with the internal market. When evaluating if COVID-19 falls in the scope of an

³⁶ Chandler, A. (2006). Successor Liability for Competition Law Infringements and How to Avoid It. *Competition LJ*, 5, 63., p. 65

³⁷ Communication of the Commission — Temporary Union framework for State aid measures to support access to finance in the current financial and economic crisis Text with EEA relevance, OJ C 6, 11.1.2011, See 1.1

exceptional disaster the Commission uses a case-by-case approach also taking into account the previous practices in the field.³⁸

In August 2020 the Commission approved Nordica a share capital increase of €22 million and a subsidized interest loan of €8 million in line with the Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak and Article 107(3)(b) TFEU.³⁹ According to the Article 107(3)(b) TFEU an aid to remedy a serious disturbance in the economy of a Member state is compatible with the internal market. The ongoing COVID-19 pandemic falls in the scope of Article 107(3)(b) TFEU due to being “a serious disturbance” in Member states’ economies.

It is understandable that Nordica is not the only airline receiving state aid due to the pandemic and actually as of April 2021 all together thirty-four schemes of state aid to airlines were granted under the Article 107(2)(b) TFEU and 107(3)(b) TFEU.⁴⁰ Few airlines were already in a difficult situation before receiving the state aid due to the pandemic meaning that some undertakings might have benefitted from the COVID-19 pandemic more than others as no state aid would have been granted if there had not been an exceptional occurrence or serious disturbance in the economy of a Member State. However, the undertaking must proof that it was not in a significantly difficult situation before the COVID-19 as it would not be fair.⁴¹

The fact that Nordica received state aid due to the ongoing pandemic and the decision according to which Nordica is responsible for Estonian air’s salaries contradicts at a first sight. However, one has to remember that the capital increase and subsidized interest loan are granted in accordance with Article 107(3)(b) TFEU. The question arises that shall the *Deggendorf principle* also apply in case of an exceptional occurrence or serious disturbance in the economy of a Member state? In addition, how flexible can state aid rules be during an exceptional occurrence or a serious disturbance. One could not predict the COVID-19 outbreak and perhaps it is not reasonable to apply the *Deggendorf principle* in the situation in question.

³⁸ European Union Guidelines for State aid in the agricultural and forestry sectors and in rural areas 2014 to 2020. OJ C 204, 1.7.2014, p. 1–97, para. 330

³⁹ European Commission (2020) “State aid: Commission approves €30 million Estonian measure to support Nordica in the context of the coronavirus outbreak” Press release. Accessible: https://ec.europa.eu/commission/presscorner/detail/en/ip_20_1538, 15.4.2021

⁴⁰ Pantazi, T. (2021). State Aid to Airlines in the Context of Covid-19: Damages, Disturbances, and Equal Treatment. *Journal of European Competition Law & Practice*.

⁴¹ Motta, M., & Peitz, M. (2020). State Aid Policies in Response to the COVID-19 Shock: Observations and Guiding Principles. *Intereconomics*, 55(4), 219-222. p. 220

In addition to this the Commissioner for competition, Vestager, has stated that the Commission is not entitled to demand the Member States to fulfil specific conditions, for instance to achieve green economy, in the context of receiving state aid during the ongoing pandemic.⁴² The state aid control seems to be more flexible during the pandemic. However, the Commission should ensure that the state aid rules will not be misused and therefore follow that the state aid measures notified by Member States during the pandemic actually complies with the TFEU and principles of the EU law.⁴³

The two companies' (Nordica and Estonian Air's) legal and economic relation will be discussed in the light of relevant case law in the next sections of the thesis to understand if the *Deggendorf principle* itself is applicable.

⁴² Maczkovics, C. (2020). How Flexible Should State Aid Control Be in Times of Crisis?. *European State Aid Law Quarterly*, 271. p. 281

⁴³ *Ibid.*, pp. 282-283

2. Deggendorf principle

The *Deggendorf* case law has shaped the interpretation of the *Deggendorf principle*. Based on the *Deggendorf* case law the Commission might ask an undertaking to recover earlier received incompatible state aid before “new” aid can be granted to the undertaking even though the “new” aid would be compatible with the internal market. Thus, it might enable to quicken the execution of recovery decisions.⁴⁴

In accordance with the case *TWD Textilwerke Deggendorf GmbH v Federal Republic of Germany*, state aid compatible with the internal market shall be suspended until earlier received unlawful and incompatible state aid to Deggendorf as laid down in the Case 86/509/EEC⁴⁵ is repaid to prevent distorting effects.⁴⁶ In the case *TWD Textilwerke Deggendorf GmbH (TWD)* received state aid from the German government, compatible with the internal market but it was suspended until the old aid was recovered from the previous Case 86/509/EEC.⁴⁷

The General Court has stated that the Commission has not misused its power when giving its Decision stating that the incompatible aid must be recovered before receiving new aid.⁴⁸ After the Decision of *TWD v Federal Republic of Germany*, the Commission has started to use the *Deggendorf* case law “in a more systematic manner”.⁴⁹

Based on the *Deggendorf* case law both beneficiaries and legal entities belonging to the same economic unit receiving compatible state aid are entitled to repay the earlier received incompatible and unlawful aid. I.e. if the recovery decision has not been implemented and the member state has

⁴⁴ Bruc, J. B., & Louis, E. (2018). Passing-on and recoverable unlawful state aid under European Union law. *Eur. St. Aid LQ*, 54. p. 62

⁴⁵ Commission Decision (EU) of 21 May 1986 on aid granted by the Federal Republic of Germany and the Land of Bavaria to a producer of polyamide and polyester yarn situated in Deggendorf, OJ L 300, 24.10.1986, See Article 1

⁴⁶ Judgement of the Court, 9.3.1994, *TWD Textilwerke Deggendorf GmbH v Federal Republic of Germany*, C-188/92, EU:C:1994:90

⁴⁷ *Ibid.*

⁴⁸ Judgement of the Court, 15.5.1997, *Textilwerke Deggendorf GmbH (TWD) v Commission of the European Communities and Federal Republic of Germany*, C-355/95 P, ECLI:EU:C:1997:241, para. 24

⁴⁹ Commission (EU) Document C:2007:272:TOC, OJ C 272, 15.11.2007, p.12

submitted a new notification, the Commission might suspend the new aid until the previously received incompatible state aid has been paid back in accordance with the *Deggendorf* case law.⁵⁰ Furthermore, in accordance with the *Deggendorf* case law the Commission's decision can be challenged within two months.⁵¹ If the undertaking fails to declare its complain on the Commission's decision within the given (two months) time period it cannot question the validity of that decision before national courts by stating that it is unlawful.⁵² This was also seen in the ruling of the TWD case. In the light of the requirements of the principle of the legal certainty and the fact that the time frame of two months had past, the Court ruled in the TWD case the TWD cannot challenge the decision of the Commission before the national court meaning that the national judge is also bound to the decision in the state aid context.⁵³

In addition, according to the Guidelines provision 76 if the Commission has given a negative recovery order which has not been implemented and has violated Article 14 of Council Regulation No 659/1999 the Commission shall take into account the "cumulative effect of the old aid and of the new aid" on competition and also the fact itself that the incompatible old aid has not been recovered before assessing if any new aid can be granted in accordance with the guidelines.⁵⁴ This provision is based on the *Deggendorf principle*.⁵⁵

However, it can be seen from the Commission's decision-making practice that the Commission prefers to demand the undertaking to recover the incompatible state aid before receiving the new state aid rather than evaluating the new and old aids' cumulative effect on competition.

The General Court has clarified in its judgements that the *Deggendorf* case law is also applicable when the "aid measure is subject to two Commission decisions", also when one decision was

⁵⁰ Lessenich, C., Koska, M., & Mariñas, N. (2008). The new Commission Notice on the recovery of unlawful and incompatible State aid. *Competition policy newsletter*, (1), 8-12. p.9

⁵¹ Arhold, C. (2003). Suspension orders in state aid cases-Is the court closing Pandora's box again. *Eur. State Aid Law Quarterly*, 39. p. 49

⁵² Podsiadło, P. (2019). The Issue of Liability for Expenditure of Public Funds From the Perspective of State Aid Regulation. p. 130

⁵³ Turner, S. (1995). Challenging EC Law before a National Court: A Further Restriction of the Rights of Natural and Legal Persons. *Irish Journal of European Law*, 4, 68. p. 74

⁵⁴ Communication from the Commission (EU) Community Guidelines on state aid for rescuing and restructuring firms in difficulty, OJ C:2004:244:TOC, 1.10.2004, para. 23

⁵⁵ Commission Decision (EU) of 25 July 2012 on state aid that France plans to grant to FagorBrandt (SA.23839 (C/2007)), OJ L 166, 18.6.2013, p. 1–23, See 63.

appealed, or when the first decision could have caused serious economic disturbances to the beneficiary of the aid.⁵⁶

As the state aid to Estonian Air was incompatible and unlawful according to the Commission's decision and was not repaid, state aid to Nordica can be suspended if these two undertakings can be considered as successors. Also, it must be seen if the new and old aid has had a cumulative effect and are Estonian Air and Nordica belonging to the same economic unit, i.e. a single undertaking or are they independent undertakings.

2.1. ACEA SpA

In the Commission's Decision 2003/193/EC the Commission evaluated two Italian state aid schemes: an income tax exemption and "subsidised loans to public utilities with a majority public capital holding".⁵⁷ These schemes were considered incompatible with the internal market under Article 87(3)(a-d) and Article 87(2) of the EC Treaty.⁵⁸ ACEA SpA, a multi-utility company (51% owned by the municipality of Rome)⁵⁹, challenged the Decision of the Commission as it had benefitted from the three-year tax income exemption, it was however dismissed by the Court of First Instance.⁶⁰

The Commission opened a formal investigation under Article 108(2)(1) and based on the *Deggendorf* case law concerning two energy saving projects supported by the Italian government which were already declared compatible.⁶¹ ACEA SpA is the undertaking that would have benefitted from this aid. The Commission evaluated that ACEA SpA is one of the former public utilities owned by local public administrative bodies still after several reorganizations involving

⁵⁶ Buendía, J. L., Buts, C., & Cyndecka, M. (2020). Review of EU Case Law on State Aid-2019. *European State Aid Law Quarterly*, 468.p. 509

⁵⁷ Joris, T. (2012). The Concept of an "Economic Unit" in State Aid Matters and the Deggendorf Principle. *European State Aid Law Quarterly*, 11(1), 149-162. p. 149

⁵⁸ Commission Decision (EU) of 5 June 2002 on State aid granted by Italy in the form of tax exemptions and subsidized loans to public utilities with a majority public capital holding, OJ L 077, 24.3.2003, para. 95-97

⁵⁹ Judgement of the Court of First Instance, 11.6.2009, ACEA SpA v Commission of the European Communities, T-297/02, ECLI:EU:T:2009:189, para. 1

⁶⁰ *Ibid.*

⁶¹ Commission Decision of 16 March 2005 concerning State aid that Italy (Regione Lazio) intends to grant for the reduction of greenhouse gas emissions, OJ L 244, 7.9.2006, para. 5

several undertakings: AceaElectrabel Produzione (AEP) which is 50% controlled by Electrabel Italia and 50% by AceaElectrabel (at the time of the investigation).⁶²

This meant that ACEA SpA was benefitting from the state aid which was previously considered incompatible by the Commission in the Decision 2003/193/EC.⁶³ However, the cumulative effect of the old and new aid (in accordance with the guidelines)⁶⁴ should be assessed but as the Decision 2003/193/EC concerned an aid scheme and not an individual state aid the exact amount should be discussed with the Italian government and the situation is also challenging as ACEA SpA was still in the progress of recovering the incompatible aid.⁶⁵

To determine the applicability of the *Deggendorf principle* the Commission assessed if ACEA SpA which is a part of the ACEA Group should be regarded as an economic unit of rather as a legally and financially independent undertaking when it comes to applying State aid rules.⁶⁶ It is said that ACEA SpA has recognized its joint control over AEP with Electrabel in the financial reporting of ACEA SpA and moreover the agreement between the undertakings was concluded after the Commission had given in its decision concerning the state aid after which ACEA SpA challenged it meaning that the undertaking was well aware of its situation.⁶⁷

This shows that ACEA SpA is a part of the Group and can be considered as an economic unit meaning also that incompatible aid shall be recovered before the new compatible state aid for the energy saving projects can be granted.

⁶² Commission Decision (2005), *supra nota 61*, para. 8-10

⁶³ *Ibid.*, para.10

⁶⁴ Communication from the Commission (2004), *supra nota 43*.

⁶⁵ Commission Decision (2005), *supra nota 49*, para.14

⁶⁶ *Ibid.*, para. 53-55

⁶⁷ Commission Decision (2005), *supra nota 49*, para 59

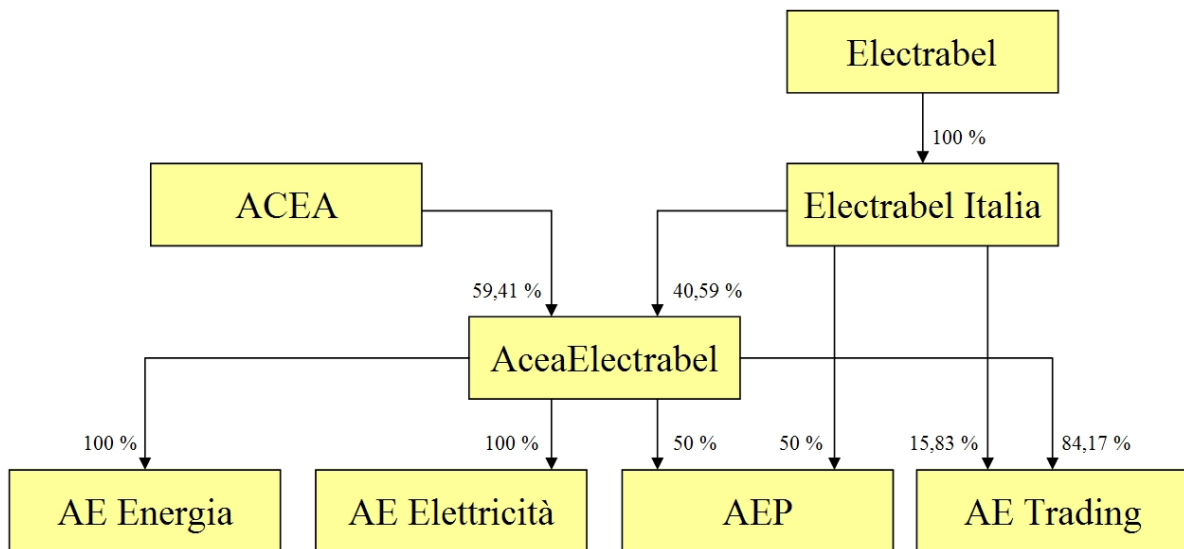


Figure 1: The structure of the undertakings

Source: Judgment of the Court, 16 December 2010, *AceaElectrabel Produzione SpA v European Commission*, C-480/90 P, ECLI:EU:C:2010:787

However, AEP was not satisfied with the Decision and stated that the that the Commission had failed in its assessment of the “new” aid and that there had been an error of interpreting the *Deggendorf* case law. The General Court held to the Commission’s Decision as AEP and ACEA SpA belonged to the same economic unit, between the new and old aid there could be seen a cumulative effect and *Deggendorf* case law shall also apply both to aid schemes as well as to individual schemes.⁶⁸ Furthermore, the General Court saw that under these specific circumstances it is not up to the Commission to state an exact amount of aid that shall be recovered.⁶⁹ The undertaking appealed and the question of the beneficiaries financial and legal decision together with the question of the scope of the *Deggendorf* case law was brought to the Court of Justice. It was also held that there is an economic continuity between ACEA SpA and AEP since AEP inherited *inter alia* a part of the incompatible aid and also would have had benefitted from the new aid.⁷⁰ The pleas were rejected based on previous arguments. Figure 1 demonstrates the structure of the undertakings when the decision was appealed to the Court of Justice.

It must also be kept in mind that it does not automatically mean that the newly established undertaking is enjoying cumulative effects in the situation when the old undertaking has not

⁶⁸ Joris, T. (2012), *supra nota 47*, p. 151-152

⁶⁹ *Ibid.*, 152

⁷⁰ *Ibid.* p. 157

recovered the incompatible aid.⁷¹ The burden of proof when it comes to the existence of the cumulative effect is on the Commission.⁷²

The Decisions are linked to the third section of the thesis as in order to know if *Deggendorf* case law is applicable it must be evaluated if the undertakings form an economic unity and has there been economic continuity between the undertakings.

2.2 FagorBrandt

The Commission has in its Decision 2004/485/EC stated that the French undertaking FagorBrandt can receive compatible aid.⁷³ However, the matter was appealed, and the General Court stated that the Commission failed to assess the incompatible state aid received by the subsidiarity of FagorBrandt, i.e. the *Deggendorf principle* was not taken into account meaning that the Commission also breached point 23 of the Guidelines^{74, 75}

In addition to the issue with the subsidiarity of Fagor Brandt, FagorBrandt had previously received incompatible state aid in form of a tax exemption called the *Septies aid* (laid down in Article 44 of the French General Tax Code) which was not recovered at the time of Commission's decision.⁷⁶

As the General Court stated that the Commission has committed "a manifest error" and failed to assess the previously received incompatible aid by the subsidiarity it can be understood from the FagorBrandt case that the General Court has taken a strict approach when it comes to the application of the Guidelines (point 23)^{77, 78}

⁷¹ Nettesheim, M. (2011). Obligation Imposed on a Newly Founded Company to Repay a Previous Unlawful Subsidy. *Journal of European Competition Law & Practice*, 2(6), 557-559.p.559

⁷² *Ibid.*, p. 558

⁷³ Commission Decision (EU), *supra nota 47*.

⁷⁴ Communication from the Commission (EU), *supra nota 46*, para 23

⁷⁵ Callol, P., & Manzarbeitia, J. (2013). Judgment of the General Court in the FagorBrandt Case. *European State Aid Law Quarterly*, 12(2), 373-381. p. 373

⁷⁶ Callol, P., & Manzarbeitia, J. (2013), *supra nota 64*.p. 376

⁷⁷ Communication from the Commission (EU), *supra nota 46*, para 23

⁷⁸ Callol, P., & Manzarbeitia, J. (2013), *supra nota 64*. p. 381

The judgement is important as it strengthens the *Deggendorf principle's* importance as it can be seen that the General Court takes actions if the Commission fails to consider the principle in its decisions. The Commission will most likely not “forget” to assess the principle if at certain point state aid should be granted to Nordica and if it was not assessed the decision would most likely be challenged by another party.

2.3 Alitalia

The Commission opened two formal investigation procedures (April 2018 and February 2020) concerning the Italian state-owned airline Alitalia’s received state aid.⁷⁹ The undertaking is still under investigations but received state aid since the undertaking suffered damage due to the COVID-19 outbreak which can be seen as an exceptional occurrence in accordance with Article 107(2)(b) TFEU. If the Commission sees a direct link between the damage suffered and the exceptional occurrence, in this case the COVID-19 pandemic, the Italian state is allowed to compensate this financial loss in accordance with the EU state aid rules.⁸⁰

When evaluating if the measures are considered as state aid accordance with the EU State aid rules the Commission took indirectly into account the *Deggendorf principle*. The Commission stated that if the criteria laid down in Article 107 TFEU are met the Commission is bound to declare the state aid compatible with the internal market and the ongoing formal investigations are not therefore preventing the undertaking from receiving state aid.⁸¹ From the decision it can be analyzed that while the investigations are still ongoing *Deggendorf principle* does not apply in the scope of granting new state aid.

Comparing the Alitalia’s situation with Estonian Air and Nordica, Alitalia had ongoing proceedings while the state aid was granted and Estonian Air was deemed to have received incompatible state aid when Nordica received state aid during the COVID-19 pandemic.

⁷⁹ European Commission (2020) “State aid: Commission approves €199.45 million Italian support to compensate Alitalia for damages suffered due to coronavirus outbreak” Press release. https://ec.europa.eu/commission/presscorner/detail/en/ip_20_1538, 15.4.2020

⁸⁰ European Commission (2020), *supra nota 63*

⁸¹ Commission Decision (EU) SA.59188 (2020/NN) Alitalia COVID-19 Damage II, 29.12.2020, JOCE C/134/2021, para. 98

Therefore, in the next section the concept of an economic unit and the relation between Nordica and Estonian Air will be discussed.

3 Economic unit in EU state aid context

The concept of an economic unit plays an important role in the context of applying state aid rules.⁸² The Court of First Instance has stated that the Commission has a broad discretion when it comes to determining if two legal entities form an economic unit or not.⁸³ As seen in the decisions concerning ACEA SpA, the *Deggendorf principle* ought to apply not only to the undertaking itself but also for instance to the beneficiaries belonging to the same economic unit.⁸⁴ Several

⁸² Nicolaidis, P., Kleis, M., & Kekelekis, M. (2008). Cumulation of de minimis Aid to Enterprises that form a Single Economic Unit. *European State Aid Law Quarterly*, 48.p. 53

⁸³ *Ibid.* p. 53

⁸⁴ Coutrelis, N. (2010). *AceaElectrabel v Commission (T-303/05)*. *Eur. St. Aid LQ*, 683.

undertakings ought to be considered as an economic unit in the scope of applying state aid rules.⁸⁵ The Court has set up three criteria when it comes to assessing the existence of an economic unit.⁸⁶ There is an economic unit, if the companies have parallel or identical activities, a profit-sharing system exercised indirectly or directly, or they have a holding company controlling a group of companies, even though, new companies have been created.⁸⁷

On the one hand, Nordica and Estonian air operated on the same relevant market, even though the determination of the relevant market can be challenging in the aviation sector. One example is that Nordica relaunched several of Estonian air's routes, meaning that it is engaged in same sector in the same area.

On the other hand, the Commission has used its broad discretion when determining whether a company can be seen as a successor or rather as a financially and legally independent company.⁸⁸ In the Case T-371/94, the Court stated that even though two companies have same management board, or they are using the same routes (which is common in the aviation sector) it does not directly mean that they are successors.⁸⁹

3.1 Economic continuity

The principle of economic continuity is slightly ambiguous. The judgements of the Court of Justice of the European Union have extended the principle to apply not only for competition law infringements but also to private enforcement of competition law rules.⁹⁰ In the Commission's decision-making the principle has been referred as same activity, assets or company is used by a new owner and seller and buyer having same shareholders. In general, the responsibility of paying

⁸⁵ Commission Notice (EU) on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, OJ C 262, 19.7.2016, see 2.1

⁸⁶ Coutrelis, N. (2010). Assessment of the Risks in State Aid and Antitrust Cases. *European State Aid Law Quarterly*, 9(3), 685-688. p. 686

⁸⁷ Coutrelis, N. (2010), supra nota 84

⁸⁸ Joris, T. (2012), Supra nota 45, p. 151

⁸⁹ Judgement of the Court, 25.6.1998, *British Airways and Others et British Midland Airways v Commission*, T-371/94, ECLI:EU:T:1998:140, § 314-315

⁹⁰ Fasoula, V. (2019). Extending the Principle of Economic Continuity to Private Enforcement of Competition Law. What Lies Ahead for Corporate Restructuring and Civil Damages Proceedings after Skanska: Case Comment to the Judgement of the Court of Justice of 14 March 2019 *Skanska Industrial Solutions and Others* (Case C-724/17). *YARS*, 20, 259. p. 261

the incompatible state aid follows if an undertaking which is filing bankruptcy transfers its assets to another undertaking, because of the economic continuity.⁹¹

According to the Commission's decision the recovery of the new aid can also be the "new" company's responsibility and not only restricted to the original company if the activity of the original company continues and there is economic continuity between the two.⁹² The commission examines the purpose of the transfer, for instance, continuity of the workforce and the identity of the shareholders and what is the economic logic of the transaction performed.⁹³ The beforementioned is further supported by the General Court's judgement.⁹⁴ The examination is performed to ensure that undertaking cannot escape their burden. Competition law infringements occur, and it might be tempting to escape the sanctions by filing bankruptcy and escaping the liability.

Nordica and Estonian air were both engaged in same activities. One can argue that even though that Nordica aimed to wipe the slate clean it might have purchased, *inter alia*, Estonian air's aircrafts and other equipment, meaning that there has in a sense been economic continuity. In addition, as it was mentioned, the CEO of Xfly and Estonian Air is the same person which does not mean that they directly are successors but together with the supportive findings it can be seen as a strengthening factor when evaluating the undertakings relation.

⁹¹ Hartikainen, S. (2020). Economic Continuity in a State Aid Recovery Case. Eur. St. Aid LQ, 359. p. 362

⁹² Commission Decision (EC) of 2 June 1999 concerning State aid granted by Italy to Seleco SpA, OJ L 227, 7.9.200, §116

⁹³ *Ibid.*, §117

⁹⁴ Judgement of the General court 28.3.2012, Ryanair Ltd v European Commission, T-123/09, ECLI:EU:T:2012:164, §155

CONCLUSION

Assessing the research question of the thesis, which was is Nordica and Estonian Air successors, firstly, taken into account the *Deggendorf* case law and the principle of the economic continuity it seems that there has been economic continuity between Nordica and Estonian Air showing that the *Deggendorf principle* ought to be applicable. Secondly, it seems that Nordica is Estonian Air's financial and legal successor only operating with a different name meaning that Nordica has a successor liability. Thus, Nordica should recover the incompatible state aid if applying for a new aid after the COVID-19 crisis if the certain criteria laid down in the *Deggendorf* case law are met. In this case, the Commission could also evaluate the cumulative effect of the new and old aid on the competition in accordance with the Guidelines or state that the incompatible aid shall be recovered before the new aid will be granted.⁹⁵

In the light of the findings, the hypothesis of the thesis is affirmed since Nordica has significant strains to Estonian air. The Tallinn Circuit Court's decision must also be kept in mind. The decision itself strengthens the implication of Nordica being Estonian Air's successor. In addition, there can be seen an economic continuity (same person as a CEO, shared equipment etc.) between Nordica and Estonian Air strengthening the affirmation of the hypothesis.

Considering the future, the lawsuit filed by the Estonian Air's former employees annulled but Estonian Air's incompatible state aid remains unrecovered. It can be understood that the state aid received due to the pandemic is an exception. After the COVID-19 pandemic if there will be a situation of Nordica requesting state aid it shall, in the light of the findings gathered in this thesis, recover Estonian Air's incompatible state aid before it can receive "new" state aid due to being Estonian Air's successor and the *Deggendorf principle* being applicable.

⁹⁵ Communication from the Commission (2003), *supra nota* 45, para. 23

The granting of state aid under the COVID-19 pandemic due to an serious disturbance or exceptional occurrence shows that the state aid rules have some flexibility in these situations. There has only been situations when this has been needed, in 2008 (financial crisis) and 2020 (COVID-19).

It has become evident that it is difficult to interpret the applicability of the *Deggendorf principle* in certain situations even though it can be understood from previous decisions that the *Deggendorf principle* shall not be forgotten by the Commission. When one undertaking is involved or a direct successor it is relatively easy to understand the applicability of the principle and its importance but in cases such as the one examined in this thesis the difficulties arise as it must be reflected from many angles.

Even though the interpretation of the *Deggendorf principle* can be difficult in certain situations the judgments of the General Court as seen in the case FagorBrandt has strengthened the *Deggendorf principles* importance. It is clear that the Commission shall take into account the principle when assessing wheater or not an undertaking can receive state aid.

To sum it up, it is important to understand that in state aid matters it plays a significant role to identify if the undertakings form an economic unit in order to assess to whom the possible infringements can be imposed. The assessment faces difficulties if the undertakings do not admit that they have a relation as it was the case with Nordica and Estonian air. The assessment becomes even more difficult when the undertaking surprisingly receives state aid under the COVID-19 pandemic even though the incompatible state aid of Estonian air has not been recovered. Exceptions have occurred before as in the case of Alitalia where the *Deggendorf principle* did not hinder the undertaking to receive compatible aid even though it still was under formal investigation by the Commission. Thus, it can be stated that the *Deggendorf principle* has not been considered in all situations, for instance when granting the state aid due to the COVID-19 pandemic. As the research on the topic is not broad further research in this area is suggested to understand more precisely the applicability of the *Deggendorf principle* in different situations and how the Commission takes into account the principle.

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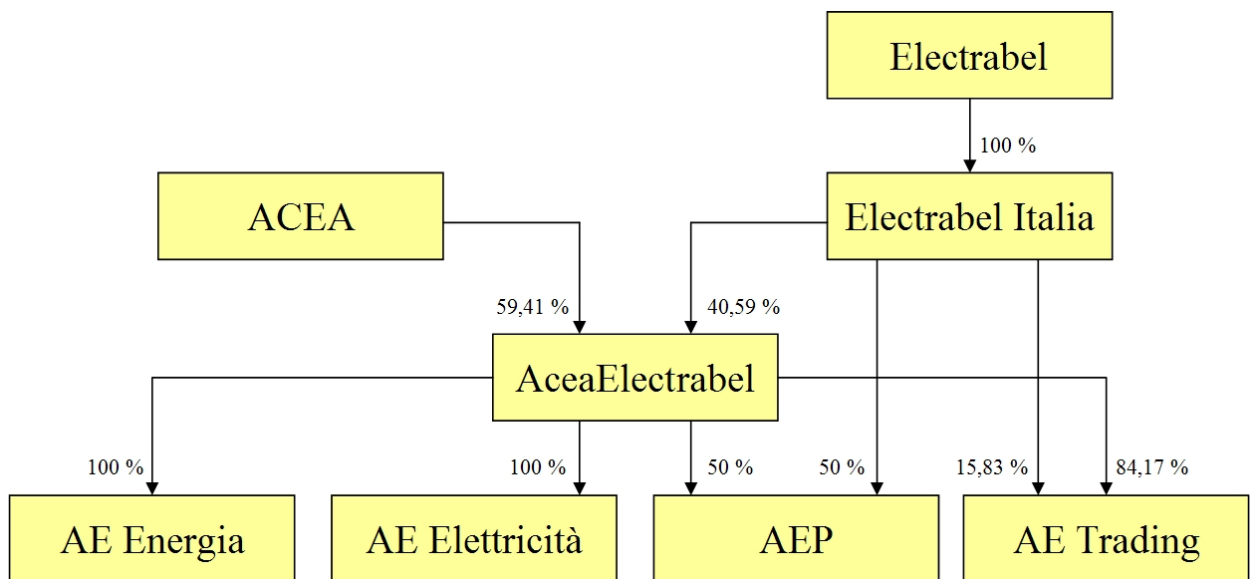
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APPENDICES

Appendix 1. The structure of the undertakings



Source: Judgment of the Court, 16 December 2010, *AceaElectrabel Produzione SpA v European Commission*, C-480/90 P, ECLI:EU:C:2010:787

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