

## State aid – Impact on Nuclear New Build in the EU

If you wish to receive more information on the topics covered in this publication, you may contact your regular Shearman & Sterling contact person or any of the following:

### Contacts

Nicholas Buckworth  
Partner  
London  
+44 207 655 5085  
[NBuckworth@Shearman.com](mailto:NBuckworth@Shearman.com)

George Borovas  
Partner  
Tokyo  
+81 3 5251 0214  
[george.borovas@shearman.com](mailto:george.borovas@shearman.com)

James Webber  
Partner  
London  
+44 207 655 5691  
[James.Webber@Shearman.com](mailto:James.Webber@Shearman.com)

[SHEARMAN.COM](http://SHEARMAN.COM)

**The European Commission has a vital role in formulating EU energy policy – but it is not a Government. It has far less executive power than many assume. One of the few executive powers it has relates to supervision (and prior approval) of support by Member States to companies or sectors of the economy. The EU refers to such support as 'State aid'.**

**The State aid regime gives the Commission the power to intervene where Member States wish to use public money to support major new investments – including nuclear new build. We are currently seeing such intervention with respect to the Hinkley Point C project in the UK. Potential investors in UK nuclear new build will need to understand and interact with the State aid regime if they are to be successful. This memorandum looks at the background of State aid and considers the possible options open to potential investors in the UK nuclear industry to maximize the likelihood of a positive outcome for their project.**

### The EU State Aid Regime - Background

EU State aid rules essentially prohibit EU Member States from using public money to benefit individual businesses or sectors, unless this is approved in advance by the Commission.

The EU's State aid rules do not apply in respect of public money from non-EU states (such as export credit agencies in Japan or the United States etc.). Neither do they prohibit companies from receiving State aid. That said, the consequence of a finding of illegal State

aid against a Member State is that the Commission may force that Member State to 'recover' the aid from the company to which it was granted. This risk of 'aid recovery' is the single biggest reason why companies and financiers need to pay attention to the State aid rules in their projects.

But there are two further reasons why companies and financiers need to understand the State aid aspects to their deals. The first is the risk of delay – State aid investigations have no timetable and investment agreements (such as that for Hinkley Point C) would typically have State aid approval as a condition precedent to closing. The second is the risk the Commission requires alteration to the agreed terms of State support as a condition for approval – impacting project economics and possibly requiring investors to re-evaluate their investment decision.

### Key Points about State Aid Review

EU Member States must obtain prior approval for any aid measure from the Commission *before* starting to fund a project. When this prior approval is not obtained or support is provided in breach of the terms of an approval, State aid becomes illegal.

It is important to understand that the approval process is bilateral between the Member State and the Commission. All other project participants are considered to be "third parties" with very limited procedural rights – notwithstanding that their interests are heavily affected by the Commission's review and approval.

The effect of the bilateral nature of the approval process is that all parties to the relevant project are heavily dependent on the Member State; both to keep them informed of progress, but more importantly to properly defend the project's position. The reality is that the ability of Member States to do this effectively is highly variable. Some Member States have effective and experienced civil servants who are able to build a strong and coherent defence of their projects. Others are much less proficient at steering State aid approval through the Commission.

### The Importance of *Hinkley Point C*

The Hinkley Point C case is the most important State aid decision to be considered by the Commission in the nuclear sector for a number of years. We currently expect the Commission's decision in September or October this year – before the current Commissioner leaves office. This is a few months earlier than was previously announced.

Senior Commission officials confirm that the Commission's Hinkley Point C decision will be highly influential and will set an important precedent for UK and all other EU nuclear projects (such as Kozloduy in Bulgaria). This is in part because, following a political compromise, the Commission's new guidelines for State aid in energy (applicable from 1 July 2014) do not extend to cover aid for nuclear energy. The Hinkley Point C decision therefore has the potential to fill a 'gap' in the Commission's energy policy framework.

The Commission's latest public view is that the UK Government's measures for Hinkley Point C do involve State aid. They also have "serious doubts" that the State aid measures meet the criteria for approval. In particular, the Commission appears not convinced the Hinkley Point C project needs public support at all. Even if it does, the Commission considers that the strike price in the Contract for Differences agreed the project and Government (in essence the guaranteed purchase price for power) is overly generous. Further, the Commission doubts that the Hinkley Point C project company NNB Generation Company Limited (NNB GenCo) was selected in a sufficiently fair way and considers that the UK should provide a more rigorous assessment of the NNB GenCo's costs and future profitability against which the level of guaranteed revenue is set.

Some in the Commission – including the outgoing energy Commissioner Günther Oettinger - are also concerned that national energy policies (including but not only the UK's) distort investment incentives and make it harder for the EU to achieve a coherent, secure and competitive energy policy.

*"We don't need national investment decisions driven by government interference in the market."*

As State aid approval is one of the few executive instruments available to the Commission to help it pursue its energy policy goals it is possible for such political views to become influential in the approval process. To illustrate the importance of politics in these decisions, the Czech energy Minister recently coordinated a letter to Commissioner Oettinger in support of nuclear new build. The letter was sent on behalf of the Czech Republic but also Bulgaria, France, Hungary, Lithuania, Poland, Romania, Slovakia, Slovenia and the United Kingdom.<sup>2</sup> This means that Member States, companies and financiers also therefore need a political strategy to build support for their project as well as competent legal and economic advisers.

### What is the likely outcome?

Ultimately, projects such as Hinkley Point C are unlikely to be prohibited on State aid grounds. Nevertheless, the eventual outcome may well mean less advantageous terms for the project. This could be with regard to a number of features of the support package, including: the duration of the Contract for Differences, the level of the guaranteed revenue under the Contract for Difference (its "strike price"), sharing any benefits with the UK in the post-Contract for Differences period, or the level of fee for the credit guarantee. While the Commission's decision can be appealed to the Court of Justice of the European Union, such an appeal is unlikely due to the political nature of State aid decisions and, in any event, would take a long time.

While each project is considered by the Commission on a case-by-case basis, the outcome of the Hinkley Point C decision will likely have a flow-on effect to the support package available for potential investors in future UK nuclear new build. Indeed, all EU nuclear power projects will likely be impacted by the framework set in the decision. This increases the importance of paying early and close attention to State aid in the context of structuring new nuclear power projects in Member States.

### What does this mean for Successor Projects in the UK such as Horizon and NuGen?

It seems likely that the UK Government may have (initially) underestimated the strength of the concerns relating to aid in the nuclear sector – especially in light of the fact that no established EU policy exists for nuclear new build. So what lessons can we learn from the Hinkley Point C experience and what can those interested in promoting projects like Horizon and NuGen do to help ensure the success of these projects in the light of the State aid challenge? There are a number of things that could now be done to improve their position and help obtain faster, more advantageous and more efficient State aid approval, regardless of the Hinkley Point C decision.

- Identify, anticipate and seek to mitigate the State aid "weaknesses" in your own project now.

<sup>1</sup> Commissioner Günther Oettinger: *Is delivery of the Internal Market on time*; speech to Conference of Council of European Energy Regulators; Brussels 18 June 2014

<sup>2</sup> See World Nuclear News "Ten nations petition Brussels for nuclear": 4 July 2014

- Identify the "market failure" that requires Government support in order for the investment to proceed. Consider collecting the evidence needed to illustrate the existence and extent of this now. We can help you understand what this evidence is and how to build it.
- Appoint legal and economic advisers who can help you make an early and realistic assessment of capacity of the Member State to effectively pursue a State aid notification. It is crucial to identify and help to fill competence gaps.
- Don't leave State aid compliance to the Member State concerned – as appears to have happened in respect of Hinkley Point C. Be involved early on and help the Member State with the development of its strategy and arguments as well as the preparation of submissions to the Commission.
- Develop a public affairs plan to advocate the need for public financial support for nuclear new build – especially aimed at the incoming European Commissioners for Energy and Competition.

## Conclusion

The State aid process is a major challenge for all participants in the UK's nuclear new build industry. However, there is a high degree of self-help available to participants who can work closely with the UK Government to anticipate and provide solutions to concerns. Helping influence the real-time development of EU policy in the nuclear space will be the best way for participants to achieve better visibility on what is a very obscure process and ultimately to improve the likelihood of achieving the right outcome for their projects.

---

ABU DHABI | BEIJING | BRUSSELS | FRANKFURT | HONG KONG | LONDON | MILAN | NEW YORK | PALO ALTO  
PARIS | ROME | SAN FRANCISCO | SÃO PAULO | SHANGHAI | SINGAPORE | TOKYO | TORONTO | WASHINGTON, DC

This memorandum is intended only as a general discussion of these issues. It should not be regarded as legal advice. We would be pleased to provide additional details or advice about specific situations if desired.

599 LEXINGTON AVENUE | NEW YORK | NY | 10022-6069

Copyright © 2014 Shearman & Sterling LLP. Shearman & Sterling LLP is a limited liability partnership organized under the laws of the State of Delaware, with an affiliated limited liability partnership organized for the practice of law in the United Kingdom and Italy and an affiliated partnership organized for the practice of law in Hong Kong.