

No.3196

EUROPEAN COMMISSION
DG Competition

Government Support II
The Director

Brussels, 14.7.2005* 0/55413
COMP HIFSP/NT/lc (2005)
A/30854 D/1001

Permanent Representation of
the Netherlands at the European
Union
Hermann-Debrouxlaan 48
BE - 1160 Brussels

Dear Sir or Madam,

Re: Supporting measure no. E 2/2005 (Ex.-NN 93/02) - Funding of housing associations - The Netherlands

Letter in respect of article 17 of the Procedural regulation concerning social housing in the Netherlands

- (1) In 2002, the Dutch authorities announced the funding measures for social housing to ensure legal certainty. For the reasons explained under III, the Commission directorate suggested to the Dutch authorities that they treat the funding measures as existing support. The Dutch authorities consequently withdrew the announcement. In addition, they repealed a number of measures.¹
- (2) The Commission's directorate consulted with the Dutch authorities as to how the regulation should be amended to comply with the rules for State support. The Dutch authority suggested that the laws be adjusted by reducing the scope of the government measures to public service activities in the social housing field and by restricting the government's operative scope in this connection to housing valued at less than EUR 200,000.

¹ Exemption from transfer tax, three subsidy measures.

I. Background

- (3) The Dutch housing sector is highly regulated and includes a subsidised rental sector in which 600 housing associations are active. These housing associations own 75% of rental dwellings, private persons owning 12% and institutional investors, project developers and building contractors controlling the other 13% of the market.
- (4) Housing corporations are independent non-profit-making institutions with the legal position of an association or foundation. Most associations are financially healthy. The total balance sheet value of all housing associations has been estimated at EUR 78 billion.
- (5) The public task of housing associations includes the construction, purchase and letting of homes to ensure the availability of quality housing at reasonable rents, *chiefly* to persons on low incomes, the elderly and the handicapped. However, social housing activities are not limited to persons on low incomes and homes may also be leased to higher income groups.
- (6) Their public task apart, housing associations may also undertake commercial activities. They have formed commercial subsidiaries, often in conjunction with market operators².
- (7) The following measures apply to housing associations:
 - Central Social Housing Fund (CFV): This fund may provide subsidies to promote the rescue of housing associations in financial difficulties. In addition, home construction projects may be subsidised on an ad-hoc basis. The subsidies may cover only the net cost of the projects. The fund is financed from levies imposed on housing associations. The government must approve the amount of such levies.
 - Social Housing Guarantee Fund (WSW): The WSW acts as guarantor for the financial obligations of housing associations towards their backers. The guarantee fund obtains its resources from contributions by housing associations, government hand-outs and third parties. The government is obliged to provide the fund with interest-free loans where necessary.
 - Exemption from corporation tax: According to the corporation tax act, housing corporations are exempt from this tax.
 - Entitlement to lend money to the Netherlands Municipal Bank (BNG): The BNG is a specialist bank with triple A status and the legal form of a public limited company. The bank lends only to local authorities, state-owned

² For example, the "Friesland Housing Association" is a conglomerate of undertakings within a holding company structure, consisting of (i) six housing associations letting dwellings, (ii) contracting companies, (iii) a project developer and (iv) undertakings providing property services.

institutions and private institutions with a public function³. Housing associations are similarly entitled to borrow from the bank. The BNG funds approx. 25% of the capital borrowed by housing associations.

II. Assessment of support in the light of article 87 (1) of the Treaty

- (8) A supporting measure may entail State support within the meaning of article 87 (1) only if each of the following conditions is met:
- a) resources must be provided by a member state or from State fund irrespective of their form;
 - b) the measure must favour particular undertakings or particular production (selective advantage) where competition is distorted or under threat of distortion;
 - c) it must unfavourably influence commercial dealings between member states.
- (9) State resources are concerned in the **Central Social Housing Fund** because the levies that housing association pay to the fund can be compared with a tax-type levy. In addition, State resources are also concerned in the **Guarantee Fund**, since the government acts as guarantor here. Furthermore, State resources are concerned in the **exemption from corporate tax**, because a loss of tax income comes down to the same thing as the consumption of State resources in the form of tax expenditure⁴. In addition, **BNG loans** are State resources since this specialist government bank with AAA status grants low-interest loans to housing associations.
- (10) Since only housing associations benefit from this transfer of State funds, unlike all other commercial competitors that are active in the home lettings sector, the above State support measures appear to offer these housing associations a financial advantage that they would not have obtained under normal market conditions. Housing associations can, after all, access substantial financial resources that do not flow from the sale of goods and services produced by the housing associations themselves. Since competition is distorted whenever support strengthens the competitive position of the beneficiary undertaking as against its competitors, this advantage can distort competition between housing associations and other undertakings⁵.

³ Undertakings in the field of housing, public utilities (water, energy, telecom, cable), education and health care

⁴ Commission Notice concerning the application of rules for supporting measures of states for steps in the area of direct taxes on undertakings (item 10), PB C 384, of 10.12.1998, pages 3-9.

⁵ See case 730/79, Philip Morris, Jurispr. 1980, page 2671, item 11 and the conclusion of the advocate-general, page 2698; see also case 259/85, Jurispr. 1987, page 4393, item 24. See also the conclusions of the advocate-general in case C-280/00, Altmark, not yet published, item 103. In the latter conclusions, the advocate-general comments that this condition is easily met because it may be assumed that all State support distorts competition or threatens to do so.

- (11) Housing associations are active on a limited scale outside the Netherlands⁶. According to the European Court of Justice, supporting measures influence commercial dealings, even if there is no question of direct consequences on commercial dealings between member states. It is sufficient if the measures place the recipient of the support in a favourable position compared with other undertakings competing with each other in internal community trade. "If financial support from a State strengthens the position of an undertaking compared with other competing undertakings in intra-community commercial dealings, such dealings must be considered influenced by the support"⁷, even if the beneficiary undertaking does not itself participate in their implementation⁸. In the present case, the competitors of housing associations are active in the community market (such as builders and institutional investors). In addition, government funding may prevent foreign investors from investing in the Dutch market.
- (12) In view of the above, the Commission comes to the conclusion that the measure concerned may unfavourably influence commercial dealings between member states within the meaning of article 87 (1).
- (13) On the basis of the above, the Commission concludes that the measures must be regarded as State support.

III. Qualification of measures as new or existing support

- (14) The Housing Act 1901 already gave housing associations the task of ensuring "improvement in social housing". At the time, local authorities gave direct subsidies to housing associations to build dwellings. The housing associations' task was further detailed in the course of the 20th century.
- (15) However, the public task as described in the Housing Act has not changed in time. Nonetheless, discharge of the task has been differently and ever more explicitly detailed in the various general statutory orders, not least because the social activities are no longer subsidised. In doing so, reference has always been made to the associations' public duties.
- (16) In the 1950-1974 period the system of direct subsidies to housing associations was converted into one of government loans. In addition, housing associations were exempted from corporation tax. Furthermore, they could still receive subsidies for specific activities, such as restructuring, renovation of pre-war homes and developing building sites.

⁶ Dutch law permits housing associations to support projects outside the Netherlands on a limited scale, e.g. in the form of flexible contributions or investment payments.

⁷ See Case 730/79, Philip Morris, Jurispr. 1980, page 2671, item 11 and case 259/85, Jurispr. 1987, page 4393, item 11.

⁸ See Case C-75/97, Maribel bis/ter ruling, Jurispr. 1999, page I-3671.

- (17) In 1984, direct government loans were replaced by a guarantee system managed by the Guarantee Fund backed up by local authorities and central government. Following the formation of the Guarantee Fund, the associations had to borrow on the capital market at a higher rate (approx. 0.5% higher) than before; the government certainly guaranteed these loans, unlike before 1984 when the loans were provided by government itself. In fact, government support consequently receded and it became more expensive for housing associations to obtain loans.
- (18) The object of any change in the measures concerned was gradually to reduce distortion of competition as against the previous situation (the original direct subsidies were converted into loans and subsequently replaced by guarantees).

The principal legislation concerning the funding of social housing in the Netherlands.

- (19) In the present case, that the Housing Act 1901 is the fundamental law concerning the funding of social housing in the Netherlands is not disputed. Nor is it disputed that this act has been repeatedly changed. As stated above, the Housing Act 1901 provides for the funding of social housing in the Netherlands.
- (20) Advocate-General Trabucchi explained in his conclusions in case C51/74 HULST of 23 January 1975 that, if a new supporting measure is to be introduced, the change in the arrangement must be substantial, i.e. the main elements of the arrangement must be changed, "*such as for example the objectives, the levy yardsticks, the levy payors or sources of financing*".
- (21) It is clear from this conclusion and from the case law⁹ that not all changes in the provisions on which support is based change existing support to new support. *Adjustments that do not substantially change support* have no consequences on the classification of the measure.
- (22) What is now concerned, therefore, is whether the rules providing for funding of social housing in the Netherlands have or have not undergone substantial changes so that the classification of the measures may have to be adapted.
- (23) Although the nature of the measures has changed in the course of time, every successive change was intended to reduce the distortion of competition compared with the previous situation (the original direct subsidies were converted into loans, to be subsequently replaced by guarantees). Furthermore, the changes did not affect the laws providing for support, either as far as the aim in view or the persons and bodies affected were concerned nor, generally, with regard to the sources of finance (State funds) or the substance of the activities with which the advantage was associated.

⁹ See case C-44/93, *Namur-Les Assurances*, Jurispr. 1994, page I-3829.

- (24) So, although it is not disputed that the funding of Dutch social housing has changed, the only substantial changes introduced since the effective date of the Treaty concerned the nature of the advantage that has gradually become less competition-distorting.
- (25) For the time being, it seems that support must be classified as existing support. After all, the funding measure already existed before the Treaty took effect in the Netherlands and the nature of the existing support from the provision was not subsequently substantially changed.
- (26) Summarising, the Commission feels, firstly, that the Dutch funding rules comprise an existing support measure for social housing.

IV. Compatibility with the common market under article 86 (2)

- (27) State support to finance social housing in the Netherlands must be examined by the Commission to ascertain whether it falls under the ban on State support under article 87 (1) and whether it can be deemed compatible with the common market.
- (28) According to the Court's established precedents, article 86 may provide an exception to the ban on State support for undertakings entrusted with services of general economic importance (DAEB). The recent judgement in *Altmark* implicitly confirmed that State support to offset an undertaking's expenses in providing such services may be deemed compatible with the common market if the conditions of article 86 are met¹⁰. The Court stressed that, to be eligible for such an exception, a supporting measure must comply with the criteria regarding definition, allocation and proportionality.

Definition of a public service and allocation

- (29) As far as the definition of public service is concerned, the Commission doubts whether it can accept the existing definition in law because it is insufficiently clear and may contain obvious errors.
- (30) When letting homes, housing associations are obliged to give preference to persons who have difficulty in finding suitable living space (through low income or other circumstances). However, their housing activities are not limited to the socially deprived. On over-capacity cover, the housing associations let the dwellings to persons with relatively high incomes, so that commercial competitors, who do not receive state support, are disadvantaged. The possibility of letting homes to higher income groups or undertakings should be regarded as an obvious error on the part of the public services. The solution proposed by the Dutch authorities to limit the maximum value of housings that can be regarded as "social homes" does not solve this problem.

¹⁰ *Altmark*, already cited, items 101 to 109 inclusive.

- (31) According to the Commission's recent established practice, certain limits are imposed on what may be regarded as a service of general economic interest within the framework of social housing. This is illustrated in Order N 209/2001 concerning state support for the Housing Finance Agency ("HFA") in Ireland¹¹.
- (32) the HFA order states that the state guarantee offered within the HFA loans framework can be applied to persons that meet certain criteria. They must need a loan, their income must be below a certain limit level and they may not be eligible for a loan from a commercial source¹².
- (33) The "social" justification for DAEB status under the Irish scheme is therefore based on stricter criteria than is at present the case.
- (34) The public services have a social character; the definition of activities of housing association must therefore maintain a direct link with socially disadvantaged households and not only with a maximum value of homes.
- (35) As far as the allocation is concerned, the Commission feels that Dutch law makes it sufficiently clear that the tasks of providing social housing lies with the housing associations.

Proportionality of funding and cross-subsidies

- (36) In its proportionality test, the Commission proceeds on the assumption that an undertaking will normally require State support to discharge its public duty. To meet this test, the State support may not exceed the net cost of the public tasks, whereupon account will also be taken of other direct or indirect income resulting from this task. In the present case, the Commission must first consider whether the costs and income connected with the public services and with non-public service activities can be properly ascertained and, secondly, whether the funding is proportionate to the net cost.
- (37) As far as determining the cost and income of the public services is concerned, it should be noted that the transparency directive¹³, contains a definition of undertakings that must keep separate accounts for various activities¹⁴, all costs and income regarding which are correctly allocated on the basis of consistently

¹¹ Published in PB C67 of 16.3.2002, page 33.

¹² The Irish Department of the Environment issues an advisory brochure stating the conditions that have applied since January 2001 and including the maximum incomes and loans. The Commission has learned that these maximum limits have since been increased in line with inflation in the area of incomes and house prices. See http://www.environ.ie/DOEI/DOEIPub.nsf/wvNavView/PublicationsList?OpenDocument&Lang=en#3_03ABDF363C09AEE80256B76005DF319.

¹³ Directive 80/723/EEC of the Commission of 25 June 1980, as amended by Commission Directives 85/413/EEC, 93/84/EEC and 2000/52/BG.

¹⁴ "Various activities" means on the one hand, products or services concerning which an undertaking has been granted special or exclusive rights, or all services of general economic interest with which an undertaking is entrusted and, on the other hand, every separate product with regard to which or every other separate service with regard to which the support is effective (article 2 (1) e. of the "Transparency Directive").

applied and objectively justified principles concerning cost price administration (article 3a (b)). The Dutch authorities have advised the Commission that non-public service activities must be carried out within the framework of separate "connections" and that the housing associations provide these connections with capital under market conditions. However, the Dutch authorities have not made it clear what criteria are adopted to determine such market conformity. Moreover, it is unclear to what extent the above measures can directly or indirectly benefit commercial connections.

- (38) The following may be stated regarding the proportionality of funding. Since the Dutch authorities could not provide sufficient information on the additional cost that housing associations incurred on public service activities, nor on the exact value of supporting measures, it is impossible to say whether or not there is over-offsetting of the net cost of the public service. Over-offsetting of this kind could arise if the housing associations were to obtain an excessive profit from their public service activities. At the present time, the Commission has no information in this connection.
- (39) Moreover, the Dutch housing associations are sometimes faced with a housing surplus. In that case, they let these homes to other parties (in other words not to the socially deprived). As commented above, the Commission feels that letting homes to households that are not socially deprived cannot be regarded as a public service. The Commission acknowledges that it would be arbitrary to keep separate accounts for homes that are temporarily exploited commercially. The Commission further acknowledges that the housing associations need flexibility for themselves and that they cannot be required to allow homes to stand empty.
- (40) Structural over-capacity is not in fact necessary for providing the public service and distorts competition on the property market. Excessive and structural over-capacity of social homes should therefore be avoided by selling these homes and the over-capacity should be restricted to a small percentage of the total stock.
- (41) Moreover, housing associations that were to let surplus social dwellings that were funded with State support commercially would distort competition on the property market if they were to offer these homes at market prices and invest the ensuing profit in other business activities.
- (42) Housing associations that let social dwellings to parties that cannot be regarded as socially disadvantaged must therefore invest the profit resulting from this back into social housing; this profit must be taken into account when ascertaining whether Support is necessary.
- (43) Following consultation with the Commission's staff, the Dutch authorities announced that they would improve transparency between the commercial activities and the public service activities. The Commission takes note of the Dutch authorities' intention to introduce laws whereby all business activities must be accommodated in distinct legal persons and the benefits of supporting measures remain restricted to public service activities.

(44) However, State support must be prevented from spilling over to commercial entities. A spill-over of this kind could be achieved if housing associations equip their own commercial subsidiaries with resources under conditions that other investors operating on the basis of market conditions would find unacceptable.

(45) In the light of these considerations and of its disposal practice¹⁵, the Commission considers that, to guarantee compatibility of the funding mechanism for social housing with the common market, the Netherlands must take the necessary steps to ensure that:

- *the public service has a social character; the definition must therefore make a direct connection with socially disadvantaged households and not only with a maximum value of such homes;*

- *any commercial exploitation of public service activities must take place under market conditions, housing associations re-investing the profit that they make from the commercial exploitation of assets destined for public service in social housing and taking the net profit from such commercial exploitation into account when calculating the net cost of the public service and the associated offsets. In particular, all financial transactions between the housing associations and commercial subsidiaries must proceed according to market practice: commercial subsidiaries must pay market prices for input (such as the letting of over capacity) that they receive from the public service entity. An authorised independent authority should check regularly whether these rules are observed;*

- *in addition, excessive and structural over-capacity of social dwellings must be avoided by selling these homes and the over-capacity must be limited to a small percentage of the total housing stock*

(46) The Commission feels for the present that the funding rule for social housing can be regarded as compatible with the common market only if the Dutch authorities take the necessary steps to ensure that these conditions are met.

(47) As stated in article 17 (2) of Council Regulation no. 659/1999, this letter contains a first opinion from the Commission on the Dutch social housing funding rules and their compatibility with the common market. In the framework of cooperation between the Commission and national authorities as laid down in article 88 (1) of the Treaty and article 17 of the Council Regulation no. 659/1999, I would therefore request that you to ask the Dutch authorities to make their comments on the Commission's initial opinion known within one month following the date of receipt of this letter.

¹⁵ See footnote 11.

(48) I also take the liberty of reminding you of article 18 of Council Regulation no. 659/1999, which reads as follows:

“If in the light of the information provided by a member state in accordance with article 17, the Commission comes to the conclusion that the existing support rules are not or are no longer compatible with the common market, it will make a recommendation that the member state concerned proposes suitable measures. This recommendation may in particular include proposals to:

- (a) change the content of the supporting measure concerned,
- (b) introduce procedural requirements, or
- (c) discontinue the supporting measure”

Yours faithfully,

signature

Loretta DORMAL MARINO