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Competition *policy brief*

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Guidelines on Regional state aid for 2014-2020

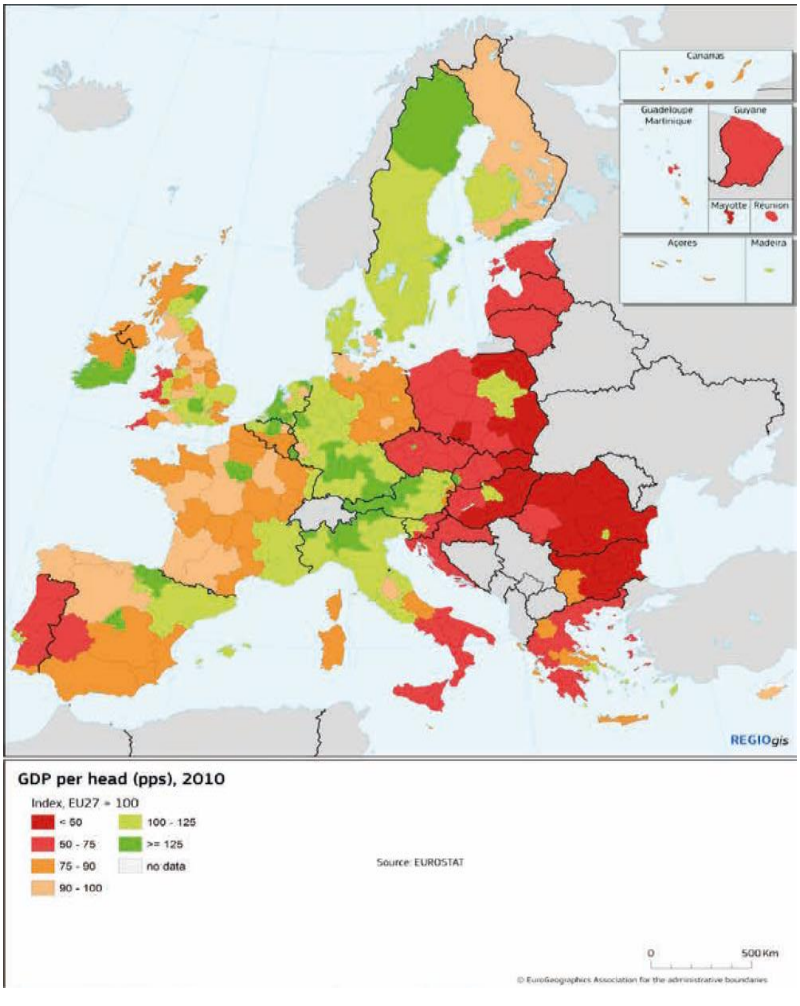
1. State aid control 2.0

The Commission has completely refurbished its State aid rules. Following the principle of "trust and verify", the new rules massively cut red tape for innocuous aid measures. Measures that threaten to seriously harm competition or fragment the internal market will be assessed, monitored, and evaluated even more carefully. This allows Member States and Commission to promote good aid and to focus attention on the cases that matter. The Commission's new Regional Aid Guidelines (RAG) are part of this comprehensive overhaul.

2. Regional aid and State aid control

Europe has always been characterised by very significant regional disparities in economic well-being, in levels of income and unemployment. Recent enlargements have accentuated these disparities. According to the most recent figures, GDP per capita in the five richest regions of the EU is five times higher than in the five poorest regions.

Disparities in unemployment are even more pronounced, unemployment ranges from 2.5% in some regions to over 35% in others.



In a nutshell

The objective of regional aid is to support economic development and employment in disadvantaged regions of Europe. In order to avoid or minimise any distortion of competition caused by this aid, the regional aid guidelines set out the rules under which Member States can provide financial incentives to companies to invest in these areas.

Regional State aid is an important instrument to promote regional development in many Member States. This has always been recognized by the EU. This is one of the reasons why State aid for the development of less favoured regions is explicitly mentioned in Article 107(3) as one of the categories of aid that can be exempted from the Treaty ban on State aid.

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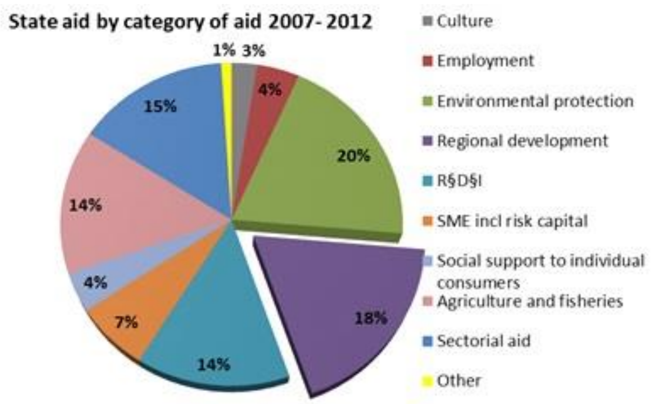
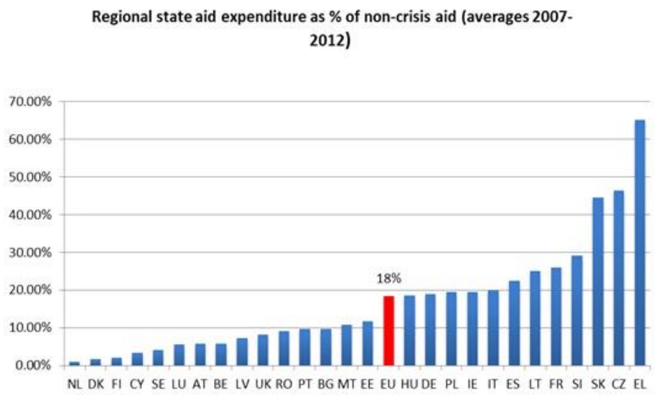
State aid policy is an important component of the EU Cohesion policy. As the Member States are responsible for allocating EU funds, these co-financed projects are subject to State aid control. In the last programming period, around 40% of structural funds involved State aid. For example, during the 2007-2013 period, numerous schemes for infrastructure investments were approved under the Regional Aid Guidelines, and included co-financing from the ESI funds.

Regional aid is a very important component of the total amount of aid granted by Member States. Between 2007 and 2012, Member States spent some EUR 75 billion on State aid for regional development. This represented 0.11% of EU GDP and 18.3% of total non-crisis related State aid.



The share of regional aid as a proportion of horizontal aid varies considerably between Member States. The below chart illustrates the extensive differences between Member States when it comes to using regional aid as an economic policy tool.



In the context of tight public budgets and continuing strain on public finances, it makes sense to cap the aid to what is strictly necessary. Engaging in subsidy races to attract investments that would in any event have taken place is nothing but a waste of public money.

The inequalities in spending capacity between Member States are another reason to limit aid. Relaxing regional aid discipline would be detrimental to economic and social cohesion. Richer Member States and regions normally have deeper pockets than their less developed counterparts. They can set up more generous support schemes and grant higher amounts of aid to attract mobile investment. Slackening discipline would lead to further divergence: the richer parts of the EU would grow richer and the poorer regions poorer.

3. The basic principles

Over the years, the Commission has put a framework into place for governing aid. This allows Member States to provide State aid to promote economic and social cohesion, while limiting the distortion of competition and trade within the common market. The basic principles underlying this framework can be summarised as follows:

- To be effective, aid must be focussed on the regions that need it most. Regional aid maps are used to show the areas in which companies may receive regional State aid, and at what intensity.

- Aid should promote activities that provide a basis for long-term regional growth. This puts the focus on aid for initial investment, and only in exceptional circumstances allows for the granting of operating aid.

The rules are set out in:

- *Regional aid guidelines for 2014-2020* (adopted in June 2013), which set the basic framework for the granting of regional aid between 1/7/2014 and 31/12/2020. They contain:

    - Criteria for designation of areas eligible for regional aid between 2014 and 2020. As of 16/09/2014, all regional aid maps have been adopted.

    - Conditions under which regional aid can be granted (eligible types of projects, maximum levels of aid and other conditions to be respected).

- *The General Block Exemption Regulation* (GBER), which defines the criteria necessary to gain exemption from advance Commission approval for regional aid. The new GBER entered into force on 1 July 2014.

4. Where can regional aid be granted?

The Treaty provides for the possibility to grant aid for two types of regions:

- **Article 107(3)(a) regions, where the economic situation is extremely unfavourable compared to the Community as a whole. These regions are defined on the basis of strict EU-wide criteria. They include NUTS 2 regions that have a GDP per capita lower than 75% of the EU average, and outermost regions as defined in Article 349 of the Treaty.**

- **Article 107(3)(c) regions, which are disadvantaged in relation to the national average. These regions are defined on the basis of a wider range of criteria, including criteria that reflect socioeconomic, geographical and structural problems at national level. These include sparsely populated regions, former Article 107(3)(a) regions and other problem regions as proposed by member States.**

Compared to the previous period, the *number* of assisted areas remains stable. Under the 2014-20 guidelines, approximately 47.7% of the EU-28 population will live in “assisted” regions.

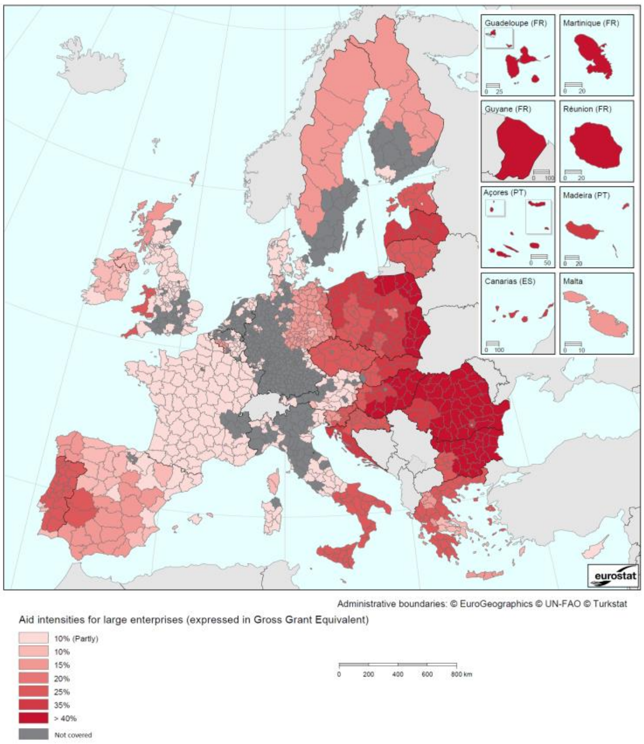
The important achievement is, however, that the poorest regions have shown significant economic development. As a result, there has been a shift between ‘a’ and ‘c’ regions. While in the previous period ‘a’ areas represented 33% of Europe, this has decreased to about 26%. At the same time, the coverage of less disadvantaged “c” areas has increased from 13.6% to about 21.8%

The aid intensity varies, based on the development level of the given region and on the size of company.

Regional aid map 2014-2017

Regional aid intensities for large enterprises

Period 1/7/2014 - 31/12/2017



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5. What can regional aid be used for?

Regional aid consists mainly of investment aid aimed at large companies and small and medium-sized enterprises (SMEs). In certain limited circumstances it can also be used for operating aid. As a general rule, aid should be granted under multi-sectoral aid schemes that are an integral part of a regional development strategy.

- Investment aid: aid awarded for investment in tangible and intangible assets relating to the setting up of a new establishment, the extension of an existing establishment, diversification of the output of an establishment into new, additional products, or a fundamental change in the overall production process of an existing establishment or, under certain conditions, the acquisition of assets directly linked to an establishment provided the establishment has closed or would have closed if it had not been purchased ('initial investment');

A recent example for setting up a new establishment is an investment project by Apollo Tyres in Hungary, in a region with high unemployment and a GDP well below EU average. This investment project will create almost 1000 direct jobs in a disadvantaged area and will contribute to the long term increase of local GDP. The project is carried out in a region with a maximum aid intensity of 50%. The guidelines have further safeguards to ensure that aid remains within reason. For this particular project, the aid was capped at 21 per cent.

- Operating aid: regional aid intended to reduce a firm's current expenses, for example in the form of tax exemptions or reductions in social security contributions not linked to eligible investment costs. Covering such expenses very rarely brings benefits to society, which is why the Commission assesses such aid on very strict terms. Any aid of this type has to be justified by the contribution it makes to regional development. Nature and level of the aid must be proportionate to the problems it seeks to alleviate.

6. The modernisation of the regional aid regime in 2013-2014

Why reform regional aid?

- Regional disparities decreased after 2000 (although new regional problems arose as a result of the financial crisis, for instance in Greece, Spain, Portugal).

- The financial crisis had an impact on national budgets, especially in programme countries. This increased the need to strengthen the effectiveness of aid, and to ensure the proper targeting of regional aid towards the weakest regions.

- Studies demonstrate that State aid in favour of large enterprises often carries significant deadweight. Many case studies show that, when deciding to invest in an area, companies do not consider aid to be the most important factor, other factors can be more important in driving investment.

Main changes brought by the reform.

- Geographical concentration:
  - The overall total population coverage of the assisted areas in the 28 Member States remains stable at around 47%
  - Even so, the catching up that took place in many of the poorest regions in the 2000's has resulted in a shift from 'a' regions to 'c' regions.

- Strengthening effectiveness of regional aid
  - Lowering maximum regional aid intensities in all assisted regions, except in the poorest regions: this is consistent with the Commission's preference for less and more efficient aid, especially at times of tight budgetary constraints. There is another rationale behind the reduction of aid intensities: as the economic development of regions in Europe progresses, the level of aid necessary to compensate for regional problems should also be reduced. The closer integration of national economies within the internal market also justifies the progressive reduction of the differences in aid intensities towards a more level playing field for everybody. A possible exception are the very poorest regions, which can still claim higher levels of support. By maintaining high aid intensity ceilings in the poorest regions, governments can offer more attractive incentives to investors in regions that are most in need.
  - An important element in the new guidelines is the more restrictive approach towards aid to large enterprises and/or large investment projects in the more developed assisted areas (i.e. in the 'c' areas). Both the academic literature[1] and the Commission's case practice in the field of State aid control shed doubts about the effectiveness of aid in these regions, especially with respect to "follow-on investments" (as opposed to "greenfield" investments). Large enterprises are less affected by regional handicaps. Evidence shows that, in most cases, subsidies are not the main reason for companies to invest in a region. For example, the pre-existence of a local production site is often an important driver to invest in an area. The presence of a company in a region reduces the costs of follow-up investments because of synergies and economies of scale, which means that it is often not the aid that attracts activity to the region. Granting aid in such cases could result in handing out "free money" to firms, which can lead to competition distortions in the internal market, with damaging effects on growth. However, these synergies and economies of scale play a less important role when companies decide to embark upon a truly new activity. In such cases, aid might be the pivotal factor for deciding on location. For these reasons, - under certain conditions - aid is only allowed to new investments by large enterprises in 'c' regions.

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[1] See: http://ec.europa.eu/regional_policy/sources/docgener/focus/2012_02_counterfactual.pdf. - published by DG REGIO

http://ec.europa.eu/competition/consultations/2013_regional_aid_guidelines/literature_review_study_en.pdf

Ex-post evaluation of the RAG 2007-2013 (case study report by Ramboll Management / Matrix) - commissioned by DG Competition http://www.nber.org/papers/w17842.pdf

This restriction does not apply to aid for large companies in "a" areas where the balance between the contribution to development and the distortion of competition is more favourable.

- Another major new element of the reform is a focus on the added value of aid. This is done through a more rigorous assessment, in particular of the incentive effect and proportionality aid. When granting aid to large enterprises, the authorities will have to make sure that the aid makes a real difference. It must give the company concerned a real incentive to invest or set up operations in an assisted area. The level of aid must not be higher than needed to convince the company to invest in that region.

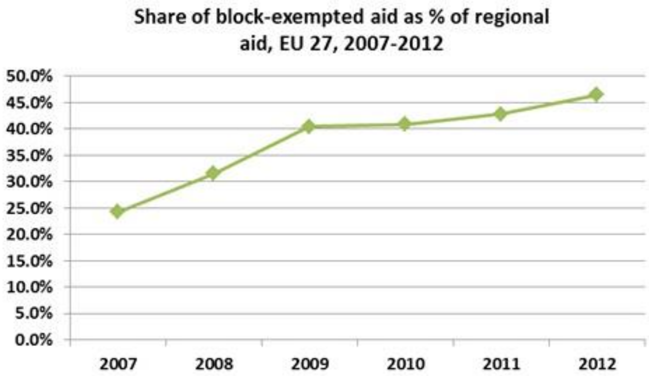
- The strengthening of anti-relocation provisions. This will allow the Commission to prohibit regional aid linked to relocation of activity within the EEA. The Commission intends to encourage more new investments, and would like to avoid shifting existing investments from one place to the next.

- To improve effectiveness of regional aid, Member States will be required to subject their main regional aid schemes to ex post evaluation by independent experts. The Commission working document of May 2014 describes the methodology for state aid evaluation[2].

- To increase transparency and accountability, Member States are required to publish the main data regarding the aid online. This will allow greater scrutiny by citizens. Information about the aid measures, the granting authorities and the beneficiaries will be publicly available.[3]

7. The other side of the coin, the block exemption

Between 2007 and 2012 almost 40% (EUR 30 billion) of all regional aid was spent under the general block exemption regulation. The use of the block exemption has increased over the period, with almost 47% of all regional aid in 2012 being granted under this instrument. Some Member States chose to provide regional aid only under block exempted measures (e.g. UK).



While the new regional aid guidelines establish rules to assess the bigger cases of regional aid, the new general block exemption regulation has been extended. Both the categories of measures and the aid amounts have increased. This allows the Commission to focus on cases involving large amounts of aid with a significant potential impact on the internal market.

The list of aid types which the Member States may grant without a notification obligation has been extended, e.g. ad hoc aid below the notification threshold, operating aid schemes for outermost regions, transport aid schemes for outermost regions and sparsely populated areas.

Adopted regional aid maps – press releases

Member state	IP Number
Austria	IP/14/579
Belgium	IP/14/1011
Bulgaria	IP/14/731
Croatia	IP/14/662
Cyprus	IP/14/868
Czech Republic	IP/14/105
Denmark	IP/14/525
Estonia	IP/14/578
Finland	IP/14/407
France	IP/14/526
Germany	IP/14/242
Greece	IP/14/527
Hungary	IP/14/243
Ireland	IP/14/583
Italy	IP/14/1009
Latvia	IP/14/408
Lithuania	IP/14/581
Luxembourg	IP/14/661
Malta	IP/14/528
The Netherlands	IP/14/1010
Poland	IP/14/180
Portugal	IP/14/666
Romania	IP/14/409
Slovakia	IP/14/63
Slovenia	IP/14/244
Spain	IP/14/580
Sweden	IP/14/326
United Kingdom	IP/14/582

[2] See policy brief on evaluation
http://ec.europa.eu/competition/publications/cpb/2014/007_en.pdf

[3] See policy brief on transparency
http://ec.europa.eu/competition/publications/cpb/2014/004_en.pdf