EUROPEAN COMMISSION

Brussels, 21.05.2014
C(2014) 3158 final

PUBLIC VERSION

This document is made available for information purposes only.

Subject: State aid no SA.37554 (2014/N) - United Kingdom

Amendment of the funding and remit of the Green Investment Bank

Sir,

1. Procedure

1) By decision of 17 October 2012 ("GIB Decision"), the Commission approved the establishment and funding of the Green Investment Bank, UK ("GIB"). In that decision the Commission declared the aid measure to the GIB compatible with the internal market on the basis of Article 107(3)(c) TFEU.

2) The approval only covered the funding amount notified. As a consequence, any further fund injection exceeding that limit requires formal notification and approval. Moreover, the GIB Decision defined a clear remit covering specific sectors in which the GIB could intervene. The addition of any sectors to the ones covered by the approved remit also requires formal notification to and approval by the Commission.

3) The UK plans to extend the GIB's funding volume by GBP 800 million and to enlarge its sectorial remit to include small-scale onshore wind and small-scale onshore hydro energy. In that context, the UK also wants to slightly modify the detailed mechanisms by which the GIB intervenes.

4) On 15 April 2014, the UK notified those amendments.

---

2 GIB Decision, recital 159.
3 GIB Decision, recital 159.

The Rt Hon William HAGUE
Secretary of State for Foreign Affairs
Foreign and Commonwealth Office
King Charles Street
London SW1A 2AH
United Kingdom
2. Facts

The GIB Decision

5) On 17 October 2012, the Commission approved the creation of the GIB which was established as a response to market failures resulting in a financing gap for green energy projects. By creating and funding the GIB, the UK intended to close at least partially that financing gap.

6) The GIB Decision, limited to a four-year period from the date of the adoption of the decision, approved the funding of the GIB (level 1) but did not extend to any potential aid to projects and/or co-investors (level 2) resulting from the interventions of the GIB.

7) The approval was based on the assessment of a number factors such as:
   i) the limitation of the public support to the minimum necessary to address the market failures;
   ii) the existence of a "double bottom line" for interventions by the GIB (namely, implementing an objective having a positive environmental impact but sticking whenever possible to market pricing and conditions in each of its interventions);
   iii) the guiding role for the GIB of the principle of "additionality" (meaning that it will only complement or top up private investors to the extent necessary, and each intervention should be the "last resort").

8) The approval was limited to a capital injection of GBP 3,082 million and to GIB's remit of intervention sectors. The approved remit included three priority sectors - (i) offshore wind power generation; (ii) waste infrastructure and (iii) non-domestic energy efficiency – and five non-priority sectors: (iv) biofuels for transport; (v) biomass; (vi) carbon capture and storage; (vii) marine energy; and (viii) renewable heat generation.

9) The GIB Decision states that any further fund injection exceeding that limit and any extension of the remit beyond the sectors approved in that decision would require formal notification and approval by the Commission.

Amendments to the scope of the permissible interventions by the GIB

10) The GIB became operational in October 2012. According to the UK, it currently backs with a committed sum of GBP 842 million 25 projects stimulating a total investment of GBP 3.2 billion.

11) After its analysis of public reports and of the market, the UK government has concluded that market failures also exist in relation to small-scale onshore wind and small-scale hydro projects. According to the UK, those market failures, if left unaddressed, would adversely affect the UK's ability to meet its international and domestic environmental obligations, in particular its 2020
targets on renewable energy. Thus, the UK would like to add small-scale onshore wind and small-scale hydro as sectors in which the GIB may intervene, thereby extending its remit.

12) Secondly, the UK wishes to extend the funding of the GIB by GBP 800 million. According to the notification, the government had originally budgeted to provide the GIB with funds during each financial year for the period up to 31 March 2015 (i.e. until the end of the financial year 2014/15 when the current Spending Review period of the UK government ends). The GIB Decision approved the initial funding of GBP 3 082 million for a four-year period until 17 October 2016. Therefore, the UK submits that in order to continue its activities during the period from 31 March 2015 until the expiry of the current State aid approval, the GIB will require further funding to deal with both its general functioning after March 2015 and the inclusion of the two new sectors in its remit.

Amendments to the GIB’s mode of intervention

13) Finally, the UK wishes to modify how the GIB mobilises private sector investment. Currently, the GIB executes transactions on pari passu terms with private co-investors on a per project basis, adding to the financing provided by private sector participants per project. However, that method has not always been the most efficient in mobilising investment. As a consequence, the UK envisages creating a more efficient co-investment structure such as a fund to mobilise upfront private capital. The GIB's investments into the co-investment structure would be made alongside investors on the same pari passu basis as is contemplated in the GIB Decision. As a result, according to the UK, such investments by the GIB will fully respect the Market Economy Investor Principle. Finally, the UK submits that investments by private investors, alongside whom the GIB invests pari passu, will be of real economic significance. Since those plans would involve financial market activities that are subject to regulation, they would be conducted through a new subsidiary wholly-owned by the GIB that will receive capital from the GIB. According to the notification, private co-investors would be selected through an open, transparent, non-discriminatory and objective selection process. To the extent that the GIB (or a GIB subsidiary) would act as a financial intermediary and/or manager, its management fee would be capped and its overall remuneration would reflect normal market conditions and be linked to performance. Should the GIB provide any services to the new subsidiary, such services would be provided strictly on commercial terms and conditions.

---

7 According to the UK, the exact form of that additional funding is yet to be determined and may also comprise, besides equity, a part in the form of debt provided by the UK Government’s National Loans Fund. Although in the notification it is noted that the UK government does not consider debt provided by the National Loans Fund to constitute aid (as, according to the UK, the NLF lends on commercial terms) it is also said in part 4, footnote 104, of the notification "that, for the purposes of this Notification the Commission should consider the entire measure of £800m of funding to be aid for the purposes of Article 107(1) TFEU:(even if the actual amount of aid ultimately is less than £800m)."

8 Notification, part 2, paragraphs 2.25 to 2.27.

9 Notification, part 2, paragraphs 2.11 and 2.18.
3. Position of the UK

14) Regarding the extension of the remit, the UK submits that market failures with respect to the small-scale onshore wind and small-scale hydro sectors primarily relate to the provision of finance which has resulted in under-investment in smaller projects. The UK contends that the funding gap for both sectors is caused by a limited participation of external funders. According to a study which the UK submitted with the notification, that limited participation is largely the result of the small size of individual investments. Those investments are typically below the threshold\(^10\) at which many financial institutions consider their involvement efficient and worthwhile. The study submitted by the UK also identifies as a reason for such limited participation of external funders the withdrawal of one of the key third party funders (the Co-op Bank) from the small-scale renewable sector.

15) Under those circumstances, for the period through to 2020, the UK estimates that there is a financing gap in the small scale onshore hydro and small scale onshore wind markets of up to GBP 1.5 billion\(^11\). In order to address the market failure regarding those technologies, the UK proposes to extend the GIB’s State aid remit to include both sectors as additional priority sectors, applying the same principles of intervention that currently exist in the GIB Decision. The GIB will utilise the same investment products as described in the original notification and the GIB Decision, namely debt underwriting and syndication, senior debt, mezzanine or junior debt, guarantees and equity.

16) According to the UK, the assessment of the GIB’s initial funding of GBP 3.082 billion under State aid rules applies equally to the extension of the GIB’s remit. According to the UK, the inclusion of small-scale onshore wind and small-scale hydro as two additional priority sectors in the remit should be considered compatible with the internal market on the basis of Article 107(3) TFEU\(^12\).

17) As to the additional funding of GBP 800 million for the period from 1 April 2015 to 31 March 2016, the UK submits that the overall funding gap across its current sectors for the period 2013 to 2020 is - with an estimated GBP 54.7 billion - larger than the UK’s initial assessment at the time of the original notification (which was GBP 47 billion for the period 2012 to 2020).\(^13\) That increase has been caused, inter alia, by structural changes affecting the respective sectors and has occurred primarily in relation to the offshore wind sector and the waste sector. With the addition of the two new sectors the overall funding gap is now estimated to be GBP 56.2 billion.

---

\(^{10}\) According to the UK, market feedback confirms that the minimum threshold is typically in the GBP 20 million range which, in turn, translates into projects of up to 18MW in size for onshore wind and projects of up to 8MW in size for hydro.

\(^{11}\) When all factors including the withdrawal of a key third party funder are taken into account, the financing gap is estimated to be GBP 1.3 billion in the sector of small-scale onshore wind and up to GBP 200 million in small-scale hydro; see Notification, part 3, paragraphs 7.5. – 7.16.


\(^{13}\) Based on an assessment by the GIB; see Notification, part 4, paragraph 3.8.
18) The UK submits that this further GIB funding partly involves State aid\(^{14}\) and that, to the extent it does, such aid is compatible with the internal market on the basis of Article 107 (3) TFEU. Accordingly, the assessment of the initial funding of GBP 3.082 billion under State aid rules still applies, as the increased funding provided to the GIB does not change the assessment of the underlying market failures as described in the GIB Decision. The UK states that the fulfilment of its obligations during the period up to the end of the financial year 2015/2016 cannot be achieved with less aid or a less severe distortion of competition and refers to the relative size of the funding (GBP 3.882 billion combined) compared with the overall funding gap of GBP 56.2 billion by 2020.\(^{15}\)

19) Regarding the mobilisation of private investment, the UK submits that third party investors’ lack of appetite and capability to engage in complex and specialised processes of investing directly in individual projects has slowed the GIB's efforts. By combining instead the GIB's investment capital within a co-investment structure such as a fund, capital could be deployed into large-scale investments in a more efficient manner. As a consequence, the UK considers a more efficient co-investment method within structures in which third party investors would co-invest ex-ante with the GIB on a pari passu basis. The investments will be restricted to interventions within the scope of the GIB remit.

4. Assessment

20) The Commission in its GIB Decision took the view that the public funding of the GIB involved State aid within the meaning of Article 107(1) TFEU since the funding by the State granted an economic advantage to the GIB which would not have been provided by private investors under the same conditions. That reasoning also applies to the additional funding provided by the State to the GIB (level 1)\(^{16}\).

21) Furthermore, the Commission in its GIB Decision examined GIB's original funding volume on the basis of a strict remit of intervention sectors and the principles described in recitals 6 to 9 and found the State aid compatible with the internal market by virtue of Article 107(3)(c) TFEU.

22) In that context the Commission considered that the measure could be deemed well-designed to address the defined objective since (i) it effectively remedied the market failures it targets to achieve a well-defined objective of common interest (i.e. its interventions could not have been performed by market forces), (ii) it was an appropriate instrument, (iii) it possessed an incentive effect, (iv) it remains proportional and (v) its adverse effects on trade and competition remained commensurate with its objective.

\(^{14}\) The UK states that, if and to the extent that the GIB were to take any portion of its approved funding in compliance with the Market Economy Investor Principle (e.g. as a loan obtained on market terms), the provision of such funding would not involve any transfer of State aid to the GIB; see Notification, part 4, paragraph 5.4.

\(^{15}\) Including small-scale onshore wind and small-scale hydro, see Notification, part 4, paragraph 4.10.

\(^{16}\) For the purpose of that assessment the Commission considers that the whole amount of GBP 800 million is provided on terms an advantage to the GIB itself (see also footnote 7 above for the supporting position of the UK). The Commission agrees however that to the extent part of that funding is procured on commercial terms, the relevant part will not constitute aid, and therefore the aid amount granted to the GIB may in reality be reduced accordingly.
23) Since the now notified amendments of the level 1 support of the GIB follow the same principles, the assessment performed by the Commission in the GIB Decision can be applied to those extensions of remit and additional funding.

24) First, as to the addition of the two new sectors to the remit, the UK has demonstrated that market failures also exist in relation to small-scale onshore wind and small-scale onshore hydro projects. Those market failures can be summarised as a lack of long-term finance, be it in the form of bank debt or equity investment by traditional investors such as utilities and project developers or by institutional investors. The market failures are caused by factors such as a tightening of credit and liquidity in the banking markets, imperfect information on the part of both lenders and project developers, relatively high costs compared to the scale of projects, perceived risks and the withdrawal of a key third party funder. The UK has furthermore provided information - based on a study submitted with the notification - on the resulting funding gap and also explained why an intervention by the GIB is the most effective and least distorting remedy to tackle the financial market failures and to enable the UK to meet its international and domestic environmental obligations.

25) The Commission acknowledges the market failures in relation to small-scale onshore wind and small-scale onshore hydro projects and agrees that those market failures and resulting funding gaps are not likely to be closed without the GIB's intervention. The Commission considers that the inclusion of the two new sectors in the remit of the GIB pursues an objective of common interest, namely the aim to lower carbon emissions to meet environmental obligations, and is an effective tool to overcome the described market failures. The Commission notes that the two new sectors would only include projects smaller than 18MW for onshore wind and 8MW for hydro, since such projects fall below the GBP 20 million threshold above which financial institutions are usually willing to provide financing. Since the GIB's investment principles for the new sectors will be the same as the ones underlying the GIB Decision – for instance, the double bottom-line and additionality (topping up as last resort lender) approach as described in recital 7 – the criteria of appropriateness, proportionality and a given incentive effect are likewise fulfilled. The Commission therefore takes the view that the extension of the GIB's remit to small-scale onshore wind and small-scale onshore hydro projects ensures that the aid provided to the GIB will target well-defined market failures.

26) Secondly, regarding the provision of GBP 800 million of additional funding to the GIB, the Commission acknowledges that the additional funding is a necessary measure to achieve the environmental objectives of the UK. As the UK has demonstrated, private investment in the intervention sectors within the GIB’s current remit continues to be constrained by a combination of financial market failures with the same applying to the two additional sectors. As a result the overall funding gap has widened and amount to an estimated GBP 56.2 billion now, as Table 1 shows:

---

17 As defined in the notification submitted by the UK, namely projects smaller than 18MW for onshore wind and 8MW for hydro
Table 1: Funding gap by 2020\textsuperscript{18}

<table>
<thead>
<tr>
<th>GIB Sector</th>
<th>Financing need by 2020 (£bn)</th>
<th>Funding gap by 2020 (£bn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Offshore wind</td>
<td>26.9</td>
<td>18.5</td>
</tr>
<tr>
<td>Waste</td>
<td>6.0</td>
<td>4.3</td>
</tr>
<tr>
<td>NDEE</td>
<td>23.0</td>
<td>18.4</td>
</tr>
<tr>
<td>Biofuels for transport</td>
<td>2.5</td>
<td>2.5</td>
</tr>
<tr>
<td>Biomass power (including biomass conversions)</td>
<td>4.0</td>
<td>3.2</td>
</tr>
<tr>
<td>CCS</td>
<td>4.2</td>
<td>1.6</td>
</tr>
<tr>
<td>Marine energy</td>
<td>1.5</td>
<td>0.6</td>
</tr>
<tr>
<td>Renewable heat generation</td>
<td>8.3</td>
<td>5.6</td>
</tr>
<tr>
<td><strong>Sub-total (current remit)</strong></td>
<td><strong>76.4</strong></td>
<td><strong>54.7</strong></td>
</tr>
<tr>
<td>Small-scale onshore wind</td>
<td>3.0</td>
<td>1.3</td>
</tr>
<tr>
<td>Small-scale hydro</td>
<td>0.4</td>
<td>0.2</td>
</tr>
<tr>
<td><strong>Sub-total (new sectors)</strong></td>
<td><strong>3.4</strong></td>
<td><strong>1.5</strong></td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>79.8</strong></td>
<td><strong>56.2</strong></td>
</tr>
</tbody>
</table>

27) The Commission acknowledges that without further intervention by the GIB, there is a significant risk that investment in the sectors within the GIB's remit will not be at the level required for the UK to meet its environmental policy objectives.

28) Furthermore, the Commission notes that the additional financial support addresses the market failures affecting the funding of green projects within the GIB's original remit as described in the GIB Decision and of projects within the two new sectors as described in recital 24. The precisely defined intervention scope of the GIB and its principle of additionality continues to clearly focus the GIB's interventions on the aim of closing the funding gap while not crowding out competition.

29) In the view of the Commission the potential distortion induced by the additional funding provided to the GIB in the existing market for financing environmental projects in the UK will be limited, since the provided amount of up to GBP 800 million is not substantial when compared with the overall funding gap. The additional funding does not change the GIB's investment principles and obligations, allowing it to maximise the impact of public funding entrusted to the GIB, while at the same time keeping the public intervention limited to the minimum necessary.

\textsuperscript{18} GIB analysis; see Notification, part 4, paragraph 3.11.
30) For the reasons set out above, the Commission takes the view that the provision of additional funding to the GIB is in line with the principles set out in the GIB Decision and, therefore, can be found compatible on the basis of Article 107(3)(c) TFEU.

31) Finally, the modification of the GIB's co-investment activities, i.e. mobilising upfront private sector investment via a co-investment structure such as a fund and creation of the GIB subsidiary to manage it does not alter any of the underlying principles of the GIB Decision.

32) In conclusion, the notified extension of the GIB's remit by including two new sectors (small scale onshore wind and small scale hydro), additional funding (of GBP 800 million) as well as the modification of its co-investment activities, are in line with the original GIB Decision and can be approved by the Commission as aid compatible with the internal market based on Article 107(3)(c)TFEU.

5. Conclusion

The Commission accordingly considers the amended aid to the GIB to be compatible with the internal market and raises no objections to the notified amendments.

If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site:

http://ec.europa.eu/competition/elojade/isef/index.cfm

Your request should be sent by registered letter, fax or e-mail to:

European Commission
Directorate-General for Competition
State Aid Greffe
B-1049 Brussels
Belgium

Fax No: +32-2-296 12 42
Stateaidgreffe@ec.europa.eu

Yours faithfully,

For the Commission

Joaquín ALMUNIA
Vice-President