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## **Primer on European Union State Aid Rules and Procedure**

In the European Union, the regulation of state aid (what Americans would call subsidies) is part of competition policy. In the United States, competition policy consists simply of anti-trust policy; that is, it focuses on deterrence of monopolies via mergers and takeovers, especially as they may adversely affect consumers.

The EU's competition policy encompasses not just anti-trust but also government subsidies to business. (The EU's Directorate-General<sup>1</sup>, or DG, for Competition has units to investigate both anti-trust issues (including merger control) and state aid.) It does so on the grounds that subsidizing some firms but not others distorts and diminishes competition in the market. If a less efficient company gains market share because of a subsidy, that harms its country's long-term economic growth. This is an argument similar to one libertarians make against the use of economic development incentives in the U.S.

"State aid" is very widely defined to include all sorts of subsidies to business, including grants, loans, loan guarantees, tax breaks, free or reduced-price land or other inputs, government assumption of debt, government purchase of part/full ownership of a company, and more.

State aid policy applies to ad hoc subsidies to an individual company or project, to subsidies given to a particular industry (such as railroads, mining, or textiles), and to subsidies given for "horizontal" goals across industries (such as pollution control, research and development, or regional policy).

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<sup>1</sup> An EU Directorate-General is approximately equal to a U.S. Cabinet Department or a large agency.

State aid is not banned under the EU's rules, but it is regulated in a number of ways and used sparingly. The EU's founding treaty, the Treaty of Rome, and its descendants as consolidated in the Treaty on the Functioning of the European Union (TFEU) specify instances of when state aid is generally permitted (for example, natural disasters). The TFEU also specifies conditions when the European Commission may allow the use of state aid (improving the economic situation of the poorest regions of the EU, for example). The Commission, guided by DG Competition, has broad discretion to make decisions and propose new policies regarding state aid.

A cornerstone of EU state aid policy is advance notice and transparency: the 27 Member States of the European Union must notify planned project subsidies or new subsidy programs in advance to the European Commission, to the extent they are not block exempted, and may not implement such plans until the Commission approves them (Article 108(3) TFEU). This notification requirement makes possible a degree of *transparency* in subsidy use that is not generally present in the U.S. Block-exempted aid must be notified to the Commission within 20 working days, and its legal provisions and aid beneficiaries above €500,000 must be published on a fully searchable website within six months.

To be sure, there have been times when governments have ignored the notification requirement, but such violations are often revealed anyway (by complaints from competing companies or other Member States, or simply from press coverage). Based on policy and case law evolution on the issue, when failures to notify come to light, the recipient company is usually required to repay the subsidy, with interest, to the government.

Once notified, proposed state aid is evaluated by the Commission to decide if it meets one of the exceptions that would allow it, that it does not unduly distort competition, and that it is the smallest amount necessary to achieve an objective that is of EU-wide significance, rather than simply national significance. The Commission can approve the original aid proposal or open a full investigation into it, which allows it to reject, to modify or to finally approve the aid proposal.

The Commission occasionally announces "frameworks" that codify the way some types of state aid will be treated in the future. Several, for example, concern limiting state aid to industries in decline, such as automobiles, textiles, and shipbuilding. The steel industry is now completely banned from receiving restructuring subsidies in the EU. In the context of the current Covid crisis, the

Commission has released guidance to Member States on measures that are allowed and compatible with the Treaty rules.

The regional aid guidelines basically “means test” subsidies by two measures: geography, size and type of the project. Wealthy areas may not provide any regional aid at all (so, for example, Amazon.com’s HQ2 project, would not have qualified for any aid in financial or political centers such as Paris). And big-ticket projects are permitted only shrinking rates of subsidization as the total capital investment rises.

The regional aid guidelines set a different aid maximum, or cap, for every region of the European Union, ranging from 0 percent for the richest regions to an aid intensity of 50 percent of the investment to large firms for the poorest (based on per capita income). Most of these “50 percent” regions are located in the former Communist states of Eastern and Central Europe, such as Bulgaria, Romania, Poland, etc. Put another way, governments can only assist poorer regions.

In addition, these aid caps are scaled down for projects with investment costs over €50 million, by half for the increment between €50 million and €100 million, and by 66 percent for any incremental investment over €100 million. Thus, a large investment project in a 50 percent region could receive a maximum subsidy of 50 percent for the first €50 million, 25 percent for the next €50 million, and 17 percent for all capital expenditures above €100 million.

Effectively, these aid caps and scale-down formulas mean that subsidy packages worth a billion or even multiple billions of dollars, as we sometimes see in the United States, are not possible in the EU.

## Glossary

**Aid intensity:** A metric that enables one to compare the rate of subsidization rather than its absolute size. The formula is simple: NPV of subsidy/NPV of total eligible investment costs. (NPV = net present value.)

**Member State:** The six original Member States of the now-European Union are France, Italy, Germany, Belgium, the Netherlands, and Luxembourg. In 1973, Denmark, Ireland, and the United Kingdom joined, bringing the number to nine. Greece joined in 1981, followed by Spain and Portugal in 1986, bringing the total

to 12. In 1995, Sweden, Finland, and Austria joined, followed in 2004 by Malta, Cyprus, Estonia, Latvia, Lithuania, Poland, Hungary, the Czech Republic, Slovakia, and Slovenia. Bulgaria and Romania joined in 2007, and Croatia in 2013, bringing the total to 28. With Brexit, the United Kingdom withdrew from the EU in January 2021, giving us the current total of 27 Member States.

**Regional policy:** Economic policies to enhance the well-being of a territorially defined region. Besides business subsidies, it includes infrastructure (road, rail, water/sewer, broadband, etc.), training, and other elements. Analogous to economic development policy.

**Regional aid:** Analogous to the United States' economic development subsidies, including tax breaks, cash payments, project-specific spending, etc. As stated in the Regional Aid Guidelines, the population of assisted areas should be less than half of the EU's population. The figure currently is set at 47 percent.

**Cohesion:** One of the primary goals of the European Union, "cohesion" is a commitment to raise the standard of living in the poorest regions of the Union.

**Structural Funds:** A group of European Union-level funds (European Regional Development Fund, European Social Fund, Cohesion Fund, European Agricultural Fund for Rural Development, and European Maritime and Fisheries Fund) that aim to enhance the economic situation of poorer regions and poorer individuals by addressing structural needs, including infrastructure, training, and attracting investment to less-developed regions. Taken together, the Structural Funds now account for one-third of the EU's budget.

**Aid maximum:** The highest amount of subsidy that can be given in a particular region, expressed in terms of aid intensity. Regional aid maxima vary inversely with a region's per capita income. Rich regions cannot give regional aid at all; regions with less than 45 percent of EU GDP per capita can give large firms up to 50 percent of the value of an investment, subject to the above-detailed scaling down for investments of more than €50 million.