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State aid control of regional development policy at 60: harder and sharper, but not yet crystal clear?

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EXECUTIVE SUMMARY

Competition policy provisions for the control of State aid have been in the Treaty from the outset. These articles have remained substantially unchanged, but a large body of law and decisional practice has evolved.

The origins of regional aid control go back to the 1956 Spaak Report and ECSC experience with subsidies. The Treaty of Rome banned State aid, but allowed for three regional policy related exceptions, closely tied to the interests of France, Germany and Italy. There have been a number of key drivers in regional aid control. Over time, the **European Courts** have entrenched key aspects of State aid policy through case law. **Theories of competitive harm** have evolved: in the 1960s and 1970s, the development of regional aid control was motivated by concerns at competitive outbidding and ambitions for a Community regional policy; by the 1990s priorities shifted to competition between firms and issues of market structure and dominance. More recent developments give primacy to economic efficiency and perceived incentive effect. **Accession** has forced new Member States to adapt regional aid policies, but **enlargement** has also heavily influenced regional aid control. **European regional policy** and regional aid control are interlinked, but relations are increasingly complex. **Wider policy agendas** have been a key part of the narrative of regional aid control: the 1992 Single European Market programme, the Lisbon Strategy and Europe 2020 have all been influential in different aspects of State aid control.

The **regulatory framework** for regional aid falls into **two phases**: pre-2000 and post-2000. The pre-2000 period is characterised by an **absence of legal clarity**, *ad hoc* decision-making and significant departures from published policy positions. Since 2000, regional aid guidelines (RAG) have operated. These have been enforced as 'appropriate measures' so have a clear legal basis, and are **characterised by fixed policy cycles** determining the parameters of regional aid control timed to coincide with Structural Fund plans. SAAP and SAM aimed to focus Commission scrutiny on aid schemes or measures that raise serious competition concerns, resulting in an emphasis on '**self-policing' through block exemptions** with fewer and fewer cases coming before the Commission. Maps approved on the basis of the RAG become an integral part of the RAG and form the basis for the exemption from notification on the basis of the GBER. **Over 60 percent of regional aid expenditure is now committed on the basis of GBER** exempt schemes. Fewer than 10 regional aid schemes and just five individual aid proposals have been scrutinised by the Commission since 2014.

Spatial coverage has consistently been one of the most controversial aspects of regional aid control. Approaches to spatial coverage in regional aid control fall into three distinct phases: in a **'black box' phase** running from the early 1970s to the late 1980s, the Commission took an increasingly interventionist, but opaque approach to disciplining regional aid maps; in a **second phase starting in 1988**, the Commission explicitly distinguished between 'a' regions and 'c' areas, and aimed to be more transparent about the methodology it had been using. However, the methodology began to unravel due to Member State criticism and the discrepancies between national and Structural Fund assisted areas. A compromise reached with the German authorities over the post-reunification regional aid maps formed the basis for an approach based on overall population ceilings, and this was used for the remainder of the 1990s. The **2000-6 Regional Aid Guidelines marked the beginning of the third phase** where EC-wide population ceilings were set, then distributed among Member States which then designated areas subject to the parameters in the guidelines. Subsequent guidelines have maintained overall population coverage discipline and fine-tuned the area designation criteria. Over time the **impact** of competition policy on **spatial coverage** and on the 'shape' of **assisted area maps** has been dramatic.

Commission perspectives on **forms of aid** are linked to two issues: first, the need to **measure and compare different types of support** – a grant equivalent; second, the desire to eliminate aid that 'props up' inefficient activities by supporting ongoing expenses. This led to early action against so-called **operating aids** in a number of countries, especially on accession. Opposition to operating aid contributed to the demise of some major instruments of regional policy, which resulted in a progressive narrowing of the forms of aid offered – by the late 1990s, the main form of regional aid was a capital grant in every Member State; operating aid is allowed in only two areas: outermost regions and sparsely-populated areas**.** However, the development of policy on operating aid has been tortuous – sometimes leading to curtailment of major operating aid schemes, but also extension of operating aid under the GBER, most notably enabling the compatibility of the Norwegian social security concession in a complete reversal of earlier policy.

The linking of **aid intensities** to the severity of the regional problem has been a core component of regional aid control since the outset**.** Initially, there was no direct calibration between the two **-** the Commission simply took the prevailing rates in the Member States as a starting point**.** Until the 2000s, **Commission ceilings did not bite**: 75% NGE was typical in many 'a' regions, but not necessarily affordable; generally, aid schemes became more discretionary and policymakers more value-conscious**.** Since 2000 **aid intensities have been lowered across** the board both in nominal terms and by using gross grant equivalent in place of NGE**.** This was partly motivated by competition concerns, as well as the affordability of high intensities for less prosperous countries. Aid intensities are **as low as 10% GGE in some 'c' areas,** raising questions about the **'incentive effect' of aid.**

The Commission was concerned from the outset that **large scale regional aid** could have undesirable effects, but Member States resisted Commission attempts at case-by-case scrutiny. The evolution of policy reflects the **tensions** between the need for **transparency** and mechanisms that capture aids with the most serious effects, and the resource implications of **case-by-case scrutiny**. An important step was the 1997 motor vehicle framework which subjected all regional aid over a given threshold to Commission scrutiny. However, Commission ambition was for a multisectoral approach to **limit capital-intensive aid** and balance benefits to regional development against competition effects. Its first attempt, the 1998 multisectoral framework (MSF), did not perform as intended. This was abandoned in favour of a further multisectoral framework in 2002, which imposed reduction formula on aid rate calculations and a notification threshold for exceptionally large projects or awards. This has now been integrated into the Regional Aid Guidelines, with some changes to the basis for Commission assessment. This comprises a **strong incentive to remain under the notification threshold** as it is increasingly likely that notification will trigger a full investigative procedure**.** For 'c' areas, large investment projects and large awards are no longer very relevant since **RAG 2014-20 mainly excludes aid to large firms in 'c' areas** except green-field projects.

In the early years, competition policy control of regional aid was itself perceived as an instrument of Community regional, now **Cohesion policy,** though bespoke European regional policy funding did not emerge until after UK accession in 1972. The implementation of the ERDF in the 1970s was **uncontroversial** since it mainly cofinanced nationally selected projects**.** The **1988 reform of the Structural Funds raised major issues in State aid relations**, primarily relating to spatial coverage, requiring compromise between the DGs for Competition and Regional policies. These tensions ultimately dissipated through the extension of Cohesion policy to all regions in 2007-13**. Cohesion policy State aid relations are now affected by a range of issues** that go beyond regional aid due to two major underlying trends. First, the **notion of State aid has expanded** along with the concept of economic activities. Second, **ESIF interventions now extend beyond basic infrastructure and grants to firms**, which in the past either did not entail aid or could be accommodated within the regional aid rules. **State aid has an increasingly high profile in Cohesion policy** due to the State aid modernisation initiatives (SAAP and SAM), the introduction and expansion of the GBER and the ‘upgrading’ of State aid considerations in the 2014-20 Common Provisions Regulation. RAG 2014-20 and GBER ‘nod’ to some Cohesion policy particularities, but a number of issues have been or are problematic, including: definitional issues, financial instruments and the treatment of simplified cost options. Although many Managing Authorities have bespoke systems for handling State aid, the error rate is high. The possibility of **audit results in a risk-averse approach to State aid compliance**, with borderline projects more likely to be funded from domestic sources alone.

Competition policy concerns with the **effectiveness of State aid** are comparatively **new.** They can be traced back to the SAAP emphasis on **economic analysis** and SAM concerns with the **efficiency of public spending**. RAG 2014-20 and GBER 2014 enable the Commission to authorise and limit the validity of large aid schemes, conditional on the outcomes of evaluation**.** Several major aid schemes are undergoing evaluation; however, the results of these studies and their impact on compatibility are as yet unknown**.**

Consideration of **post-2020 State aid reforms** seems to be at an early stage; there is currently no ‘high level’ State aid agenda like SAAP or SAM to provide a *leitmotif* for possible change. The Commission is taking soundings about the future of RAG and GBER, but there are no concrete outputs so far. Reapplication of the RAG 2014-20 post-2020 is subject to a large number of variables, including population coverage and thresholds, and other factors including data availability and NUTS boundary changes, which make outcomes difficult to predict. However, the current eligibility criteria suggests some changes to ‘a’ regions, with a reduction in some eastern European states, in part induced by a ‘Brexit effect’ on thresholds, with some southern European regions ‘regaining’ ‘a’ region status as a consequence of economic decline.

1. INTRODUCTION

It is 60 years since the Treaty of Rome was signed, setting out the basis for a system of subsidy or 'State aid' control that remains unique. Much has changed in the intervening period: the Treaty provisions on State aid have spawned an evolving body of case law, hard and soft law and decisional practice that operates in an economic, political and geographical context which the authors could scarcely have imagined.

The Treaty articles themselves remain practically unaltered. The basic provisions underpinning the control of regional aid have been interpreted and adapted against the backdrop of changing economic and political circumstances, successive enlargements and the emergence of European regional, now Cohesion policy, as well as shifts in Commission and domestic thinking about the role of business subsidies in economic development.

The control of State aid for regional development is set to enter another period of reflection. The key texts – the Regional Aid Guidelines and the General Block Exemption Regulation – are set to expire at the end of 2020, a schedule timed to coincide with the next round of Cohesion policy programming, which itself is already under review. These texts are important, and will continue to frame the main parameters of both domestic and Cohesion policy interventions. However, there has been a widespread retreat from the use of 'traditional' regional aids, partly due to competition controls, in favour of 'softer' forms of intervention such as service or infrastructure provision; in the context of *domestic* policy, much of this is beyond the purview of State aid control. In the case of Cohesion policy, intervention has also diversified beyond infrastructure and aid to productive investment, which were the mainstay of past Structural Fund interventions, to softer forms of support, including advisory services, support for research and innovation, social enterprises and business-related infrastructures. Also, and at the behest of the Commission, there has been increasing emphasis on more 'market-based' measures in the form of so-called financial instruments. At the same time, State aid control has extended into areas once considered beyond its scope, notably services or infrastructure traditionally provided by the State, but which may now be considered to involve economic activity. This has broadened the reach of what is subject to State aid control into areas where there is limited guidance or decisional practice, often creating uncertainty for those involved in policy implementation, especially in a more intensive audit climate.

Ironically, perhaps, the competition rules arguably now therefore have as many, if not more, implications for Cohesion policy than for purely domestic regional policy. This partly arises from the multifaceted nature of Cohesion policy intervention which may involve complex assessments about whether State aid is involved, and potential 'forum shopping' where it is. In addition, the scrutiny to which Cohesion policy intervention may be subjected through the audit process throws into sharp relief the penalties for getting such assessments wrong.

This paper takes the opportunity to look back at the origins and impact of State aid control on regional development policy. Taking a historical and thematic perspective, it explores the key drivers of change and their effects over the last six decades. The paper concludes with a brief consideration of future issues and raises some questions for discussion.

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2. KEY DRIVERS IN REGIONAL AID CONTROL

- The **origins** of regional aid control go back to the 1956 Spaak Report and ECSC experience with subsidies.
- Treaty of Rome **banned State aid**, but allowed for **three regional policy related exceptions** closely tied to the interests of France, Germany and Italy.
- Theories of competitive harm underpinning regional policy control have changed.
- 1960s and 1970s development of regional aid control was motivated by concerns at **competitive outbidding** and ambitions for a **Community regional policy.**
- By the 1990s concern shifted to **competition between firms** and issues of market structure and dominance.
- More recent developments give primacy to issues of **economic efficiency and perceived incentive effect.**
- **Accession** has forced new Member States to adapt regional aid policies, but **enlargement** has also heavily influenced regional aid control.
- **European regional policy** and regional aid control are interlinked, but relations are increasingly **complex.**
- **Wider policy agendas** have been a key part of the narrative of regional aid control: 1992 Single European Market; Lisbon Strategy; Europe 2020…
- **European Courts** have entrenched key aspects of policy such as ‘a’ region and ‘c’ area definition.

The current basis for the competition policy treatment of regional aid can be traced back to the Spaak report published in 1956.[1] The committee charged with developing proposals for the European Economic Community (EEC) implicitly rejected the approach under the European Coal and Steel Community Treaty (ECSC) which had outlawed the use of national subsidies. The ECSC experience made clear that some exceptions to a general prohibition would be needed otherwise the EEC rules ran the risk of being ignored as the ECSC provisions had been.[2] Reflecting this, the Spaak report proposed a general ban on State aid, but also identified areas, including regional aid, which would or might fall outside such a ban.

The extracts below (see Figure 1) shows clearly the extent to which the Spaak report was a forerunner to the Treaty of Rome provisions on State aid - its approach to prohibiting aid was adopted largely unchanged as Article 92(1) of the EEC Treaty.[3] However, its provisions on measures that would fall out of the scope of State aid and those on regional development were subject to considerable negotiation.

[1] Comité Intergouvernemental créé par la Conférence de Méssine (1956) *Rapport des chefs de délégation aux ministres des affaires étrangères*, Brussels, 21 April.

[2] Piernas López, J J (2015) *The Concept of State aid under EU law: from internal market to competition and beyond,* Oxford University Press.

[3] Now Article 107(1) TFEU,

Figure 1: The Spaak report –precursor to Article 92 of the Treaty of Rome

La règle générale est que sont incompatibles avec le marché commun les aides, sous quelque forme qu'elles soient accordées, qui faussent la concurrence et la répartition des activités en favorisant certaines entreprises ou certaines productions.

Ce critère permet immédiatement de mettre hors de cause une importante part des aides accordées par les Etats :

— des subventions bénéficiant aux consommateurs individuels, qui n'entrent pas dans le circuit de la production et qui ne sont pas en concurrence entre eux, sont un instrument de politique sociale et une méthode de redistribution des revenus qui restent entièrement aux mains des Etats ; à la condition d'être accordées sans discrimination liée à l'origine des produits, elles n'ont pas d'incidence sur le marché commun. La même considération vaut pour les aides aux établissements désintéressés : écoles, hôpitaux, centres de recherche, institutions charitables ;

— la politique générale peut attacher une importance essentielle au développement de certaines régions pour éviter des concentrations urbaines excessives ou au maintien d'un équilibre entre différents groupes sociaux. Les subventions dont elle userait à cet effet ne tendent qu'à compenser, pour les activités intéressées, les désavantages qui leur sont imposés en vue de l'avantage collectif. C'est sous cet angle qu'il conviendra en particulier de considérer les aides données à l'agriculture de certaines régions spéciales, telles que les montagnes ou les sols pauvres, aussi bien qu'au développement d'activités décentralisées susceptibles de réabsorber des agriculteurs en surnombre ou de leur offrir un emploi de complément.

In the course of the Treaty negotiations the Spaak report proposals on regional development aid evolved into three distinct exemptions from the prohibition – one under the *mandatory* exemptions, in favour of the so-called 'zonal border area' in Germany (Article 92(2)(c)) and two under the discretionary provisions (Article 92(3)(a) and (c)). Here, it is important to recall that negotiations were among just six Member States, and the influence of the three large countries was apparent: Germany, in the case of the zonal border area; Italy, where there were specific concerns about the competitiveness of the south and for which the *Cassa per il Mezzogiorno* had not long been established (1950) - hence the provision for 'a' regions; and France, where Claudius-Petit's 1950 *Pour un plan national d'aménagement du territoire* would lay much of the foundations of thinking on regional policy and the location of economic activity in years to come.

Figure 2: Article 92 of the EEC Treaty and the regional aid exemptions

1. Save as otherwise provided in this Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between Member States, be incompatible with the common market.

2. The following shall be compatible with the common market:

   (a) aid having a social character, granted to individual consumers, provided that such aid is granted without discrimination related to the origin of the products concerned;

   (b) aid to make good the damage caused by natural disasters or exceptional occurrences;

   (c) aid granted to the economy of certain areas of the Federal Republic of Germany affected by the division of Germany, insofar as such aid is required in order to compensate for the economic disadvantages caused by that division.

3. The following may be considered to be compatible with the common market:

   (a) aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment;

   (b) aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State;

   (c) aid to facilitate the development of certain economic activities or of certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest;

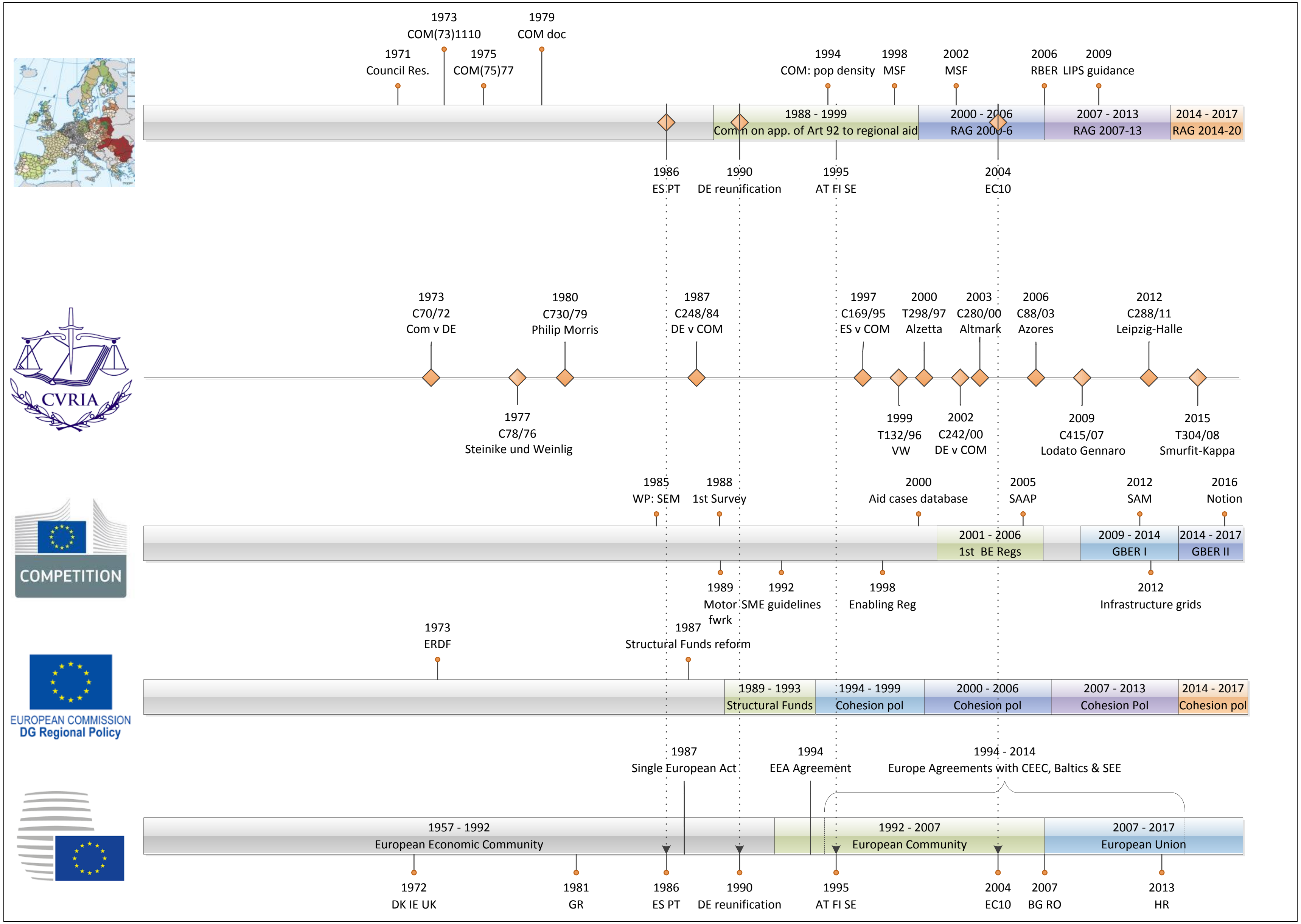
   (d) such other categories of aid as may be specified by decision of the Council acting by a qualified majority on a proposal from the Commission.

Against the background of these Treaty articles, regional aid was the first policy area in which the European Commission developed its mandate to regulate State aid. In the 1960s, the initial Commission proposals involved the case-by-case scrutiny of regional investment aid to assess the effects on competition and set the amount of aid.[4] This was rejected by Member States – though clearly elements of the approach resurfaced later and are present in the Commission's analysis of individual cases today. The first *formal* steps to regulate regional aid were not taken until the 1970s and the beginnings of a systematic policy did not emerge until the late 1980s.

Figure 3 summarises the main policy developments in the control of regional aid, along with wider developments that have been influential in shaping policy.

[4] Commission of the European Communities (1972) First Report of Competition Policy, Luxembourg.

Figure 3: The evolution of regional aid control 1957-2017



Source: EPRC research

The first steps in regional aid control were partly motivated by concerns at competitive outbidding for mobile investment; the restructuring of many 'traditional' industries was leading some Member States to attract inward investment through State aid.[5] This was linked to aspirations for a Community regional policy[6] - competition policy control of regional aid has always been perceived by the Commission as contributing to the reduction of regional disparities. The origins and evolution of regional aid control are also closely interlinked with other geopolitical developments and wider policy objectives.[7]

Successive ***enlargements*** of the European Community / Union have been instrumental: State aid control has not only shaped the regional economic development policies of every new Member State, but has itself also had to adapt to new economic geographies, such as the much poorer regions of the Iberian peninsula in the 1980s or the sparsely-populated areas of the Nordic countries in the 1990s. Later still, enlargement to EU25 required the recalibration of existing approaches to approving assisted areas in order to accommodate a large number of less prosperous countries. Enlargement has also influenced the regulatory architecture of State aid control: the Europe Agreements of the 1990s onwards required the pre-accession States to establish national monitoring authorities to 'self-police' State aid on the basis of EC State aid rules. With accession, formal responsibility for State aid control passed to the Commission. However, the pre-accession approach had provided a model whereby Member States could play a greater role in State aid discipline, culminating in the adoption of Block Exemption Regulations in the early 2000s.

In the late 1950s and early 1960s the European Commission had initiated a number of studies with a view to laying the foundations of a bespoke ***European regional policy***. None of this bore fruit at the time – the ERDF was not established until 1975 in the wake of UK accession - but some of the ideas did filter through into the control of regional aid, which was itself perceived by the Commission to be a component of regional development policy. Moreover, since the 1988 reform of the Structural Funds the two policy areas have exerted considerable influence over one another. Since 2000, the multiannual schedules of the Regional Aid Guidelines and Cohesion policy programmes have been aligned; the definition of the least prosperous regions – the 'a' regions and the Less-developed regions – is the same; and RAG 2014-20 makes some explicit adjustments in favour of Cohesion policy. That said, and as noted earlier, the multi-faceted nature of Cohesion policy means not only that assessments of whether State aid is involved can be complicated, but also that 'forum shopping' beyond the regional aid rules is required to ensure compliance.

Wider internal market and competition policy issues have been key. The White Paper on Completing the Internal Market,[8] together with the *Padoa-Schioppa*[9] and *Cecchini*[10] reports, had

[5] Jordan, J (1976) *The compatibility of regional aid systems with the Common Market,* European Law Review, 236-242.

[6] Commission of the European Communities (1969) *A regional policy for the Community*, OOPEC, Luxembourg.

[7] Wishlade, F (2003) *Regional State Aid and Competition Policy in the European Union*, Kluwer Law International, The Hague.

[8] Commission of the European Communities (1985) *Completing the Internal Market: White paper from the Commission to the Council,* OOPEC, Luxembourg.

[9] Padoa-Schioppa, T (1987) Efficiency, Stability and Equity: A Strategy for the Evolution of the Economic System of the European Community, report to the President of the European Commission.

[10] Cecchini, P *et al* (1988) *The European Challenge 1992: The Benefits of a Single Market,* Wildwood House, Aldershot.

stressed the need for strict control of State aids in the context of an internal market: in the absence of other forms of protectionism, which the ‘1992 programme’ was intended to outlaw, the impact of State aids was considered likely to increase and Member States were perceived to be tempted to boost spending on aid with a view to protecting or promoting national industries or attracting inward investment. These concerns culminated in an extensive survey of the State aids being offered by Member States. Only a summary of expenditure, as opposed to a full catalogue of schemes was published.[11] However, the information collected was used by the Commission to scrutinise and ultimately curtail or eliminate a number of major so-called ‘general’ investment aid schemes for large firms that had operated outside the assisted areas and formed the beginning of a more systematic approach to dealing with support for large firms under regional aid schemes too. Wider State aid policy developments have also been linked to high level policy aims: the *2005 State aid action plan* (SAAP)[12] was part of the wider Lisbon Strategy for growth and jobs, and aimed to achieve ‘less and better targeted aid’, a refined economic approach and shared responsibility between the Commission and Member States in enforcement. These aims fed into important changes in regional aid control in relation to lower assisted area coverage, more sophisticated scrutiny of aid to large investment projects and the Block Exemption Regulation for regional aid. The successor to SAAP, the 2012 *State aid modernisation initiative* (SAM)[13] was developed in the wake of the financial and economic crisis and linked to the Europe 2020 strategy for smart, sustainable and inclusive growth. SAM initiated a range of reforms, including a significant extension to GBER 2014 so that very few regional aid schemes now require ex ante scrutiny and approval by the Commission (or ESA). It also emphasised the need for ‘incentive effect’, which fed through into the exclusion of large firms from eligibility for investment aid in ‘c’ areas in RAG 2014-20, and formed the basis for the requirement for evaluation plans for schemes with large budgets in GBER 2014.

The Commission has wide discretion in the interpretation of the State aid rules, but that discretion is not unfettered. Various ***rulings from the European Courts***, whether confirming or constraining the Commission’s approach, have entrenched various aspects of policy. For example, case law from the 1980s[14] served to embed the distinction between ‘a’ regions and ‘c’ areas, with the former to be assessed in relation to the Community average and to concern “only areas where the economic situation is extremely unfavourable in relation to the Community as a whole.”[15] This in turn formed the basis for a first definition of ‘a’ regions in 1988,[16] which has remained largely unchanged ever since.

These ‘drivers’ of policy change have contributed to some important shifts in the evolution of regional aid control, as illustrated in Figure 4.

[11] Commission of the European Communities (1988) First Survey on State Aids in the European Community, SEC(88)1981, 13 December 1988.

[12] European Commission (2005) State aid action plan: less and better targeted aid – a roadmap for State aid reform 2005-2009, COM(2005)107 final.

[13] European Commission (2012) EU State aid modernisation, COM(2012)209 final.

[14] Case 730/79 *Philip Morris Holland BV v Commission of the European Communities* [1980] ECR 2671; Case 248/84 *Federal Republic of Germany v Commission of the European Communities* [1987] ECR 4013.

[15] Case 248/84 at p 4042.

[16] Commission communication of the method for the application of Article 93(3)(a) and (c) to regional aid, OJEC C212 of 12 August 1988.

Figure 4: Key developments in regional aid control

	Key features	Application
Principles of the 1970s	Set out principles in relation to: • aid ceilings • transparency (essentially 'measurability') • regional 'specificity' • sectoral repercussions	• Initially tentative: existing maps taken as basis for defining 'central' and peripheral areas • Prevailing aid ceilings in peripheral areas generally retained • Stance quickly toughened: Com sometimes imposed map on MS; or required withdrawal of operating aid • No MS regional policy untouched by Com (maps and forms of aid) • Com decision-making very lengthy and opaque

1988 Communication (1994 amendment)	• Explicit distinction between 'a' regions and 'c' areas:
	  ○ 'a' regions NUTS 2 regions GDP(PPS) ph <75% of EC av
	  ○ 'c' areas based on EC-adjusted indices of GDP & unemployment
	• Mix of net and gross grant equivalent ceilings; prevailing rate widely used
	• Enlargement (FI, SE) + NO EEA results in provision made for sparsely-populated regions (NUTS 3 12.5 inh per km^2) in 1994
		• Published in recognition of growing resentment at lack of transparency, 1988 method had been used by Com since early 1980s!
		• Maps reviewed 3-5 year cycles; still controversial – but now critique of method as well
		• Method began to unravel due to:
		  ○ Lack of coincidence between national and Structural Fund assisted areas (DG Regio DG Comp discord)
		  ○ DE reunification - forced more flexibility: population ceiling approach piloted with DE in 1991

RAG 2000-6	• First legal basis for regional aid control; application for fixed timescale • EU15 population ceiling: 42.7% • Top-down definition of 'a' regions aligned with Objective 1 • 'c' area population shared between MS (on basis of 1988 Communication index), then adjusted (inc for sparsely-populated areas) • MS select 'c' areas, subject to strict quantitative parameters • Reduction in aid intensities	• Principles re population ceiling had been applied since early 1990s, but not made explicit • Needed to adapt to Structural Fund map issues and upcoming enlargement (EU10 in 2004, mainly 'a' regions) • Reduction in spatial coverage in EU15 • Imposed through Art. 93 'appropriate measures' • Map negotiation highly contentious in some MS [including legal challenge to outcome and methodology by DE].
RAG 2007-13	• Broad continuation of RAG 2000-6 • EU25 population ceiling 43.1% (46.6% of EU27) • Area designation parameters relaxed • Reduction in aid intensities and use of gross grant equivalent • Reporting of aid to projects >€50m	• Less radical than RAG 2000-6, but significant impact of enlargement on 'a' regions in EU15 (statistical effect) • Incorporates 2002 Multisectoral framework on large awards • Regional BER adopted so few aid *schemes* scrutinised by COM; GBER supersedes RBER in 2009
RAG 2014-20	• Broad continuation of RAG 2007-13 • Largely excludes aid to large firms in 'c' areas • Increased population coverage – 47% of EU28 • Reduction in aid intensities • Links to Cohesion policy strengthened • Transparency – reporting of aid >€3m • Scope to link aid scheme approval to evaluation	• GBER extended to include almost all regional aid – some operating aid and individual cases fall under RAG • Little incentive to notify individual cases as investigative procedure very likely • 2017 GBER amendment extends coverage of operating aid

The key elements of regional aid control have been present since the formulation of policy in the early 1970s, namely regional 'specificity', the need for aid to be 'measurable' with implications for the form of aid, the calibration of aid intensity to the severity of the regional problem and a consideration of sectoral and competition issues. These remain the core of policy, but have been complemented by an increasingly formal framework, coordination with an evolving European regional policy, emphasis on reporting and an emerging focus on effectiveness. The sections below identify the main thematic trends in policy evolution.

3. REGULATORY ARCHITECTURE

- The regulatory framework for regional aid falls into two distinct phases: pre-2000 and post-2000.
- The **pre-2000 period** is characterised by an absence of legal clarity, *ad hoc* decision-making and significant departures from published policy positions.
- **Since 2000,** regional aid guidelines (RAG) have operated. These have been enforced as 'appropriate measures' so have a clear legal basis, and are characterised by fixed policy cycles determining the parameters of regional aid control timed to coincide with Structural Fund plans.
- SAAP and SAM aimed to **focus Commission scrutiny** on aid schemes or measures that raise serious competition concerns, resulting in an emphasis on 'self-policing' through block exemptions with fewer and fewer cases coming before the Commission.
- Since 2006 the regional aid guidelines have been complemented by **block exemption regulations**. Maps approved on the basis of the RAG become an integral part of the RAG and form the basis for the exemption from notification on the basis of the GBER.
- **Over 60 percent** of regional aid expenditure is now committed on the basis of **GBER exempt schemes**.
- **Fewer than 10 regional aid schemes** and just **five individual aid proposals** have been scrutinised by the Commission since 2014.

The regulatory architecture for regional aid control can be divided into two distinct phases. The ***early years*** were characterised by a distinctly *ad hoc* approach to regional aid control. In the 1970s various Communications set out the key principles on spatial coverage, rates of award and form of aid, and by the late 1980s, the Commission had intervened in relation to the maps and form of regional aid in virtually every Member State. However, actual Commission practice often departed markedly from its own guidelines, fuelling resentment among domestic policymakers at the opaqueness of decision-making. Transparency increased under the 1988 Communication[17] which included a method for approving assisted areas which the Commission had been using for some time. However, by the mid-1990s, Commission practice had departed from this Communication too. By the late 1990s, it was clear that reform was required. In principle, the 1988 Communication still applied, but in practice the Commission had adopted a different approach, based on population ceilings, which it had piloted with the German authorities in the period following reunification. At the same time, discrepancies between the assisted areas for the now comparatively mature Community regional policy had increased tensions within the Commission, and the prospect of enlargement called for a more systematic approach.

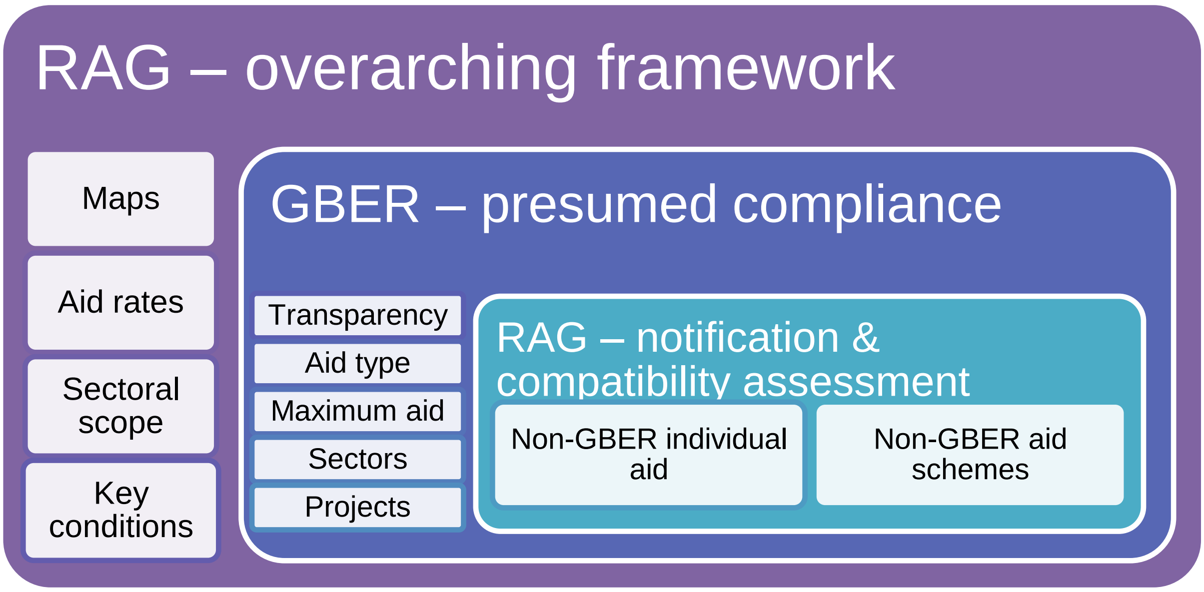
[17] Commission communication of the method for the application of Article 93(3)(a) and (c) to regional aid, OJEC C212 of 12 August 1988.

Figure 5: From soft law to hard law – evolution of the regional aid framework

1971 to 1999	From 2000
Several communications – 1971, 1973, 1975, 1979, 1988, 1994.	Regional aid guidelines (RAG 2000-6; RAG 2007-13; RAG 2014-20)
Legal basis unclear.	Successive RAGs imposed on the Member States as 'appropriate measures' under Article 108(1) TFEU. From 2006 block exemption regulations.
No end date. Each Communication supplements but does not replace its predecessor	RAG 2000-6 explicitly replaces all related Communications from 1971-1999. Each RAG specifies its duration.
Commission practice departs from stated policy. Regional aid relations are essentially bilateral.	Regional aid guidelines also bind the Commission and apply to all Member States simultaneously.
Map and scheme scrutiny by Commission is ad hoc, typically triggered accession or by notified changes. Decision times lengthy, sometimes involve Commission imposing maps on Member States and often long transitional periods.	RAG 2000-6 explicitly terminated validity of existing maps and required new maps and schemes to be notified and approved prior to implementation. Map approval under RAGs is for duration of RAG. Introduction and expansion of block exemption regulations means that COM rarely needs to scrutinise aid schemes, but map approval is key as provides spatial coverage and associated award rates.

A ***second phase*** began with the 2000-6 Regional Aid Guidelines,[18] which were a landmark in regional aid control. They were imposed on *all* Member States by means of (then) Article 93(1) appropriate measures, thereby withdrawing the existing maps at the end of 1999 and applying the same period of validity to all national assisted area maps. Subsequent regional aid guidelines (for 2007-13 and 2014-20) have operated in the same way. Crucially, these have been complemented by so-called block exemption regulations which have meant that, once the regional aid maps and award rates are approved under the RAG, the Commission now rarely has occasion to examine either regional aid schemes or individual awards.

Figure 6: Regulatory framework for regional aid control

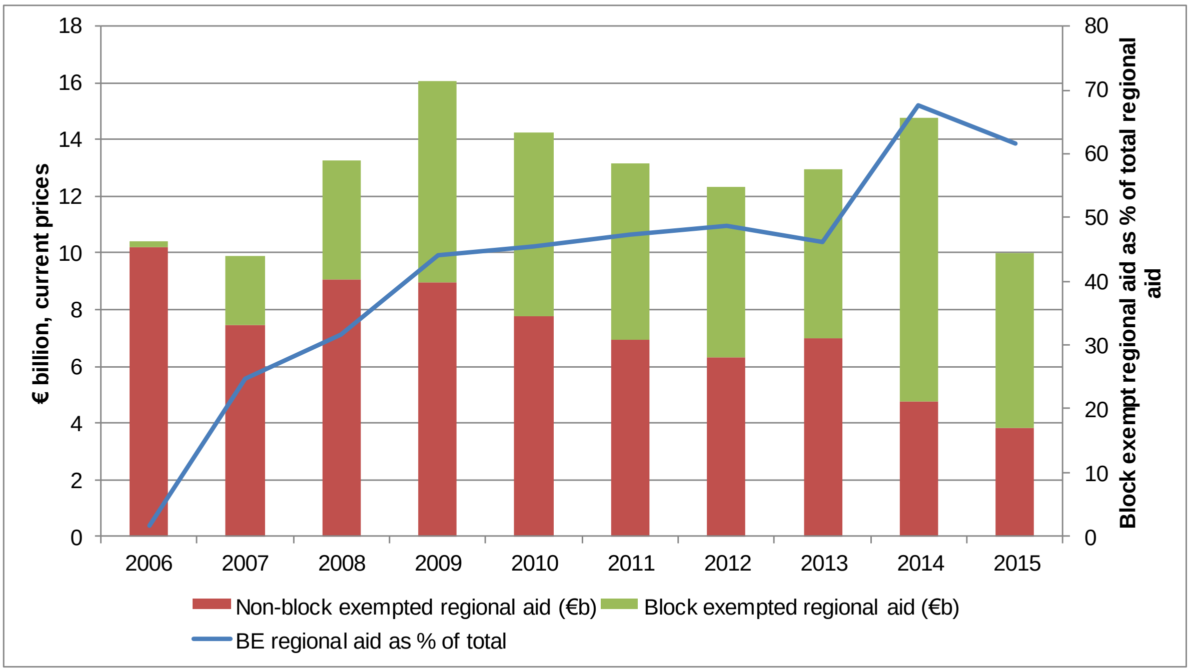


Source: EPRC

[18] Guidelines on national regional aid, OJEC C74/9 of 10 March 1998.

Indeed, under RAG 2014-20, it appears that the Commission has examined fewer than 10 aid schemes[19] and just five individual cases.[20] The EFTA Surveillance Authority (ESA) performs the same functions for the EEA members and here too most schemes fall within the GBER (though ESA was responsible for handling the single largest notified scheme, this being the Norwegian social security concession (RDSSC)). In GBER 2014-20 notification is essentially limited to schemes that lack the transparency to fall under the GBER; moreover, GBER 2014-20 also extends the scope of exempted ad hoc regional aid, so that fewer individual awards would fall to be considered under the regional aid guidelines. This is reflected in the declining proportion of spend on notified (as opposed to block-exempted) regional aid (see Figure 7), though in absolute terms the former remains surprisingly high.

Figure 7: Share of regional aid under block-exempted measures (EU28)



Source: EPRC calculations from European Commission State Aid Scoreboard: http://ec.europa.eu/competition/state_aid/scoreboard/index_en.html

[19] In addition to approving the regional aid maps and associated aid rates for each country.

[20] According to DG Competition's register of cases as at end August 2017: http://ec.europa.eu/competition/elojade/isef/index.cfm?clear=1&policy_area_id=3

4. SPATIAL COVERAGE

- Spatial coverage has consistently been one of the most **controversial aspects** of regional aid control.
- Approaches to spatial coverage in regional aid control fall into **three distinct phases**.
- In a '**black box' phase** running from the early 1970s to the late 1980s, the Commission took an increasingly interventionist but opaque approach to disciplining regional aid maps.
- In a **second phase** starting in 1988, the Commission explicitly distinguished between 'a' regions and 'c' areas, and aimed to be more **transparent** about the methodology it had been using.
- The **methodology began to unravel** due to Member State criticism and the discrepancies between national and Structural Fund assisted areas.
- A compromise reached with the German authorities over the post-reunification regional aid maps formed the basis for an **approach based on overall population ceilings**, and this was used for the remainder of the 1990s.
- The 2000-6 Regional Aid Guidelines marked the beginning of the **third phase** where EC-wide population ceilings were set, then distributed among Member States which then designated areas subject to the parameters in the guidelines.
- Subsequent guidelines have maintained **overall population coverage discipline** and fine-tuned the area designation criteria.
- Over time the **impact** of competition policy on spatial coverage has been **dramatic**.

The spatial coverage of regional aid has been one of the most controversial elements of State aid control since the outset. Three distinct phases in the development of policy can be distinguished.

In a first ***'black box' phase,*** the starting points for the Commission were the existing assisted area maps of the Member States, but its initial focus was on controlling regional aid in the so-called central areas and containing Member State attempts to extend assisted area coverage. Thus, as far back as 1971, the Commission objected to State aid in Nordrhein-Westfalen which the *Land* authorities had initially offered in coal-closure areas, but wanted to extend throughout the *Land.* In the 1970s and 1980s, the Commission approach to assessing assisted area coverage was opaque and regional aid map relations with the Member States consequently often fraught. The Commission also on occasion imposed its own regional analysis when countries sought to amend assisted area maps or in the context of its periodic reviews.

Figure 8: Phases in the development of Commission policy on spatial coverage

	Basis	Key features
'Black box' decision-making on spatial coverage	1971 resolution	• Distinguished central and peripheral regions (latter were: FR *prime de développement industriel* areas; IT *Mezzogiorno;* DE: Berlin and *Zonenrandgebiet).* Initially control only covered central regions. • Regional aid should not cover entire national territory (except Luxembourg) • Boundaries of eligible areas should be identified clearly • Regional aid should not involve pinpointing (except in the case of growth poles)
	1975 communication	• Distinguished 5 categories of region: 1. Greenland, Ireland, Northern Ireland, *Mezzogiorno* 2. West Berlin and *Zonenrandgebiet*

	Basis	Key features
		3. *Prime de développement industriel* areas (FR); assisted areas in Centre-North (IT); assisted areas (UK) 4. Northern development area, Bornholm, Ærø, Samsø and Langeland (DK) 5. 'Other regions'
Methodology exposed, but increasingly abandoned in practice	1988 Communication	• Explicit distinction between 'a' regions and 'c' areas • 'a' regions are NUTS 2 regions where most NUTS 3 regions have GDP(PPS) per head below 75% of EC average • 'c' areas based on two stage analysis: 1. NUTS 3 regions with either GDP(PPS) per head below the national threshold or unemployment rate above the national threshold. Thresholds set per country to reflect national situation in a community context. 2. Scope to take other indicators into account. • 1994 Communication recognises sparsely-populated areas as 'c' areas
Population ceilings and 'a' regions drive coverage	Regional aid guidelines (from 2000)	• Sets an EC wide population ceiling on initial coverage • Top-down definition of 'a' regions (NUTS 2 with GDP(PPS) per head <75% of EC average • Remaining eligible population divided between MS on basis of Stage 1 of 1988 Communication 'c' area method, subject to 'adjustments' • Greater *apparent* freedom for Member States in area designation

The publication of the 1988 Communication marked a ***second phase*** and was an important turning point. It was driven by a number of factors: there was Commission recognition that the lack of transparency in map decisions had bred resentment and that there was a need for greater cooperation; enlargement to include Spain and Portugal had widened existing disparities; the Single European Act introduced new provisions on economic and social cohesion, and these were underpinning the reform of the Structural Funds. Reflecting a recent court ruling, the 1988 Communication made explicit reference to 'a' regions and 'c' areas. In practice, however, the publication of the methodology exposed it to Member State criticism, especially in relation to its over-reliance on quantitative indicators. A long-running dispute between the Commission and **France** in the early 1990s provides a good illustration of the arguments espoused by many Member States.

Figure 9: Negotiation of the French *prime d'aménagement du territoire* map 1990-95

The issues arose from the Commission examination of the *prime d'aménagement du territoire* (PAT) map undertaken as part of its regular review process. This resulted in the Commission proposing as appropriate measures that substantial parts of the French assisted areas map - notably large parts of western and south-western France - be dedesignated.[21] This met with considerable opposition from the French authorities, because the changes proposed did not take into account the nature of the regional problem. One of the principal aims of French regional policy was to counter the domination of Paris and to support areas with a declining population. Such areas predominated in south-western France, which the Commission proposed to dedesignate. However, the problems faced by such regions did not show up in measures of unemployment and GDP per head used by the Commission.

The use of unemployment data for rural areas was regarded as inappropriate since many such areas are characterised by strong out-migration trends. This can result in unemployment rates below the national average, but which reflect the lack of job opportunities rather than a buoyant local economy. Moreover, these migration patterns contribute to higher unemployment in urban areas. In the French context, the case for maintaining the designation of rural areas concerned was not supported by GDP data either: excluding the Paris region, disparities in GDP per head at NUTS III in France were not particularly wide. Overall, a strict application of the Commission methodology would have led not only to the dedesignation of areas whose development the French authorities perceived to be an integral part of regional policy, but also the inclusion in the map of areas which they did not seek and which would have been out of line with national regional policy priorities.

Source: D. Yuill *et al* (1992), *European Regional Incentives 1992-3,* Bowker-Saur, London.

Ultimately this and similar map disputes with other countries were overtaken by wider regional policy events. Specifically, a major disagreement between DG Competition and DG Regional Policy erupted over the lack of coincidence between the Structural Fund areas and those eligible for domestic regional policy areas. This resulted in a number of short-term compromises being sought, but longer term further contributed to the unravelling of the 1988 Communication methodology.

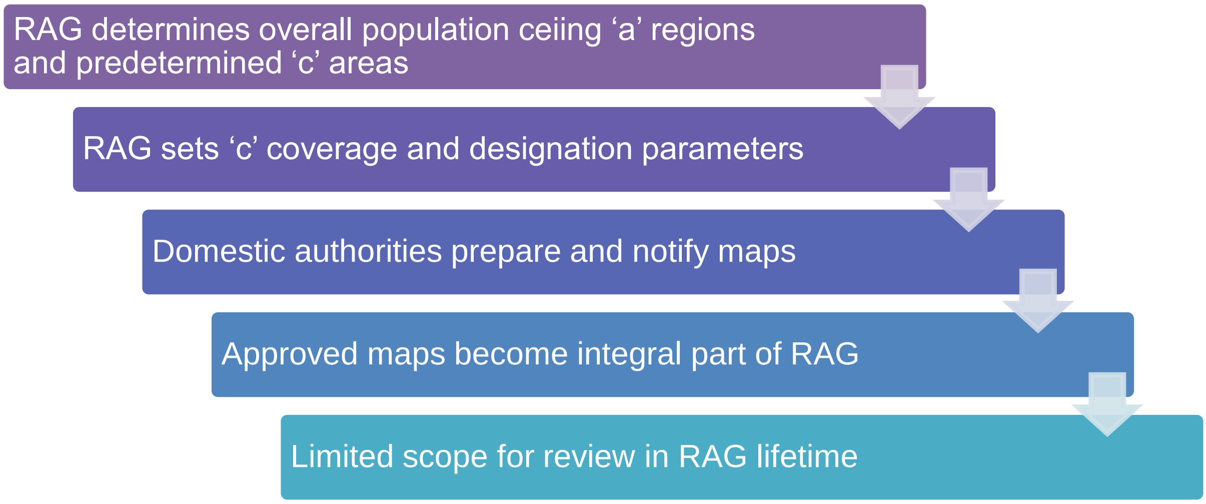
The roots of the ***third phase,*** which did not formally begin until the adoption of the 2000-06 Regional Aid Guidelines, lie in Commission regional aid map negotiations with Germany in 1991. The reunification of **Germany** presented a particular challenge for map negotiations since it coincided with both Commission pressure for a reassessment of the *Zonenrandgebiet* and the need for a domestic review to take account of the specific issues facing eastern Germany. Following reunification, the Commission was keen to dispense with the Article 92(2)(c) provisions which provided for a *de jure* exemption from the general ban on State aid in recognition of the regional impact of the division of Germany. In practice, the negotiations were much less contentious than anticipated, largely due to a flexible approach on the part of the Commission which, instead of imposing the 1988 Communication two-stage analysis for 'c' areas on the German authorities, opted to set a population ceiling and allow more freedom in the selection of actual areas. This was certainly facilitated by the approach to area designation in Germany which is based on the so-called synthetic index – a number of published indicators which are weighted and ranked - and which would have provided reassurance that a robust method underpinned the selection of areas. This decision formed the basis of an (undisclosed) methodology which was used for other Member States for the remainder of the 1990s – including the imposition of a population ceiling on **Austria** when it joined the Community in 1995.

This internal method was in turn the starting point for the negotiating a new approach to spatial coverage with the Member States, culminating in the 2000-6 Regional Aid Guidelines. The third phase of policy on spatial coverage has been characterised by three elements. First, ***overall population coverage and its distribution among Member States***, what 'floors' and 'ceilings' should be applied and what transitional arrangements should apply. Second, the parameters within which domestic

[21] Commission of the European Communities, *XXth Report on Competition Policy* (Luxembourg 1991).

authorities can ***select assisted areas*** and propose maps to the Commission. These two elements are negotiated ex ante. The third element comprises the ***decisions approving the national assisted area maps***, which themselves become an integral part of the regional aid guidelines. Since 2006, this has also formed the basis for the compatibility of regional aid under the block exemption regulations.

Figure 10: Spatial coverage under the regional aid guidelines (post 2000)



In essence, since the 1990s and the piloting of the population approach, the overall population ceiling has become a proxy for regional aid discipline and a reflection of the principle that regional aid should be exceptional and therefore cover less than 50 percent of the population.

Over the long term, regional aid has had a significant impact on the coverage and shape of assisted areas maps in many countries. In addition, Commission intervention has eliminated the multiple assisted areas that existed in some countries,[22] with support under such measures typically being reduced to *de minimis* levels or restricted to SMEs. In **France**, for example, a separate map operated for the local business tax concession (*exonération de la taxe professionnelle*), but Commission intervention realigned this map with that for the *prime d'aménagement du terrirtoire*.

In terms of spatial coverage, the principles of RAG 2007-13 and RAG 2014-20 do not differ markedly from RAG 2000-06. However, an important feature is the role of GDP(PPS) per head, coupled with the population ceiling. Levels of GDP(PPS) per head determine 'a' region coverage and special provision is made for any region losing 'a' status in the new period. This has meant that successive enlargements to include less prosperous countries has reduced coverage in more prosperous countries in order to remain within the overall ceiling. Also significant for some countries are the provisions on population density. Importantly, however, these are absolute, rather than relative measures, with the result that the eligibility of sparsely-populated regions has been unaffected by enlargement.

The general trend has been for assisted area coverage to come under pressure in the more prosperous older Member States – thus in the Netherlands and Denmark, for example, coverage has fallen from around 27 percent to eight percent or less between 1980 and 2014. However, this pattern

[22] The exception to this is operating aid which is only compatible in the case of sparsely-populated and outermost regions so may operate on the basis of different geography.

has not been linear or even: coverage *increased* in 2014 in Belgium, France and Austria, reversing, or at least halting the longer term decline in coverage.

Figure 11: Trends in Assisted Area Coverage (% of population)

	1980	1985	1990	1995	1999	2000	2004	2007	2009	2014	2017
BE	39.5	33.1	33.1	35.0	35.0	30.9	30.9	25.9	25.9	29.95	29.95
FR	38.2	39.0	41.9	40.9	42.4	36.7	36.7	25.3	18.4	24.17	24.17
DE	36.0	28.4	38.0	38.5	37.6	34.9	34.9	29.6	29.6	25.85	25.85
IT	59.0	59.0	59.0	48.8	48.9	43.6	43.6	39.7	34.1	34.07	35.52
LU	100.0	100.0	100.0	79.9	42.7	32.0	32.0	21.1	16.0	8.00	8.00
NL	27.4	25.0	19.9	15.6	17.3	15.0	15.0	9.9	7.5	7.50	7.50
DK	27.0	24.0	20.7	19.9	20.2	17.1	17.1	11.3	8.6	7.97	7.97
IE	100.0	100.0	100.0	100.0	100.0	100.0	100.0	75.0	50.0	51.28	51.28
UK	45.4	37.8	37.8	36.8	38.1	30.7	30.7	23.9	23.9	27.05	27.78
GR		100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.00	100.00
PT			100.0	100.0	100.0	100.0	100.0	95.9	76.7	85.02	85.02
ES			58.6	58.6	75.9	79.2	79.2	72.0	59.6	68.66	68.66
AT				35.2	35.2	27.5	27.6	22.5	22.5	25.87	25.87
FI				41.6	41.6	42.2	42.2	33.0	33.0	26.03	26.03
SE				18.5	18.5	15.9	15.9	15.3	15.3	12.26	12.26
CY							100.0	66.0	50.0	50.00	50.00
CZ							100.0	96.3	88.6	88.10	88.10
EE							100.0	100.0	100.0	100.00	100.00
HU							100.0	100.0	100.0	76.71	76.71
LV							100.0	100.0	100.0	100.00	100.00
LT							100.0	100.0	100.0	100.00	100.00
MT							100.0	100.0	100.0	100.00	100.00
PL							100.0	100.0	100.0	100.00	100.00
SK							100.0	96.4	88.9	88.48	88.48
SI							100.0	100.0	100.0	100.00	100.00
BG								100.0	100.0	100.00	100.00
RO								100.0	100.0	100.00	100.00
HR										100.00	100.00

Source: EPRC research based on Yuill D *et al* (eds). European Regional Incentives, various editions and Commission regional aid guidelines.

The population coverage driven approach, coupled with enlargement, has meant that assisted area coverage is affected by *relative* levels of prosperity. Enlargement since 2004 has lowered average levels of GDP(PPS) excluding some regions from eligibility as ‘a’ regions through the statistical effect of enlargement, rather than absolute changes in prosperity. The impact of this is reflected in Figure 12 which shows that, except for 2004-06, overall coverage has always been in the range 42 to 50 percent. One of the aims of RAG 2000-6 was to manage EC15 spatial coverage downwards (hence the fall from 46.7 percent of the population in 1999, to 43.2 percent in 2000 after the revised maps were authorised). Enlargement in 2004 raised coverage to over 52 percent, but RAG 2007-13 reduced coverage further in EC15 (and in some new Member States) to bring overall coverage below 50 percent from 2007, and lower still in 2009 once transitional periods had expired.

Looking at longer-term trends, it appears that, in spite of fraught regional aid policy relations between Member States and DG Competition, there was limited Commission success in containing spatial coverage until RAG 2000-6: between 1980 and 1999 coverage in the EC9 fell by less than four percentage points; by contrast, between 1999 and 2009, it fell by almost 15 percentage points.

Figure 12: Assisted area coverage and enlargement

	1980	1985	1990	1995	1999	2000	2004	2007	2009	2014	2017
EC9	**43.9**	40.2	42.6	39.8	40.2	35.4	35.4	28.6	25.5	26.5	26.9
EC10		**42.4**	44.7	41.9	42.3	37.7	37.7	31.1	28.1	29.0	29.4
EC12			**48.1**	45.5	47.8	44.2	44.4	37.9	33.4	35.4	35.7
EC15				**44.6**	46.7	43.2	43.3	37.0	32.8	34.5	34.7
EU25							**52.5**	46.8	42.9	43.7	43.8
EU27								**49.9**	46.1	46.7	46.8
EU28										**47.2**	47.2
NMS10/12/13							100.0	95.2	97.9	95.6	95.6

Source: EPRC calculations based on Figure 11.

As mentioned earlier, the provisions on low population density are important for some countries, most notably Sweden and Finland in the EU, and Norway and Iceland in the EEA.[23] The population quotas for ‘c’ areas are based on the population of NUTS 2 regions with a population density of less than 8 inhabitants per km^2 and NUTS 3 regions with a population density of less than 12.5 km^2.

Figure 13: Assisted area coverage in the EEA

	1995/6	2000/1	2007	2008	2014
NO	25	25.79	27.5		25.51
IS	40.8	33.2	31.6	37.5	36.5

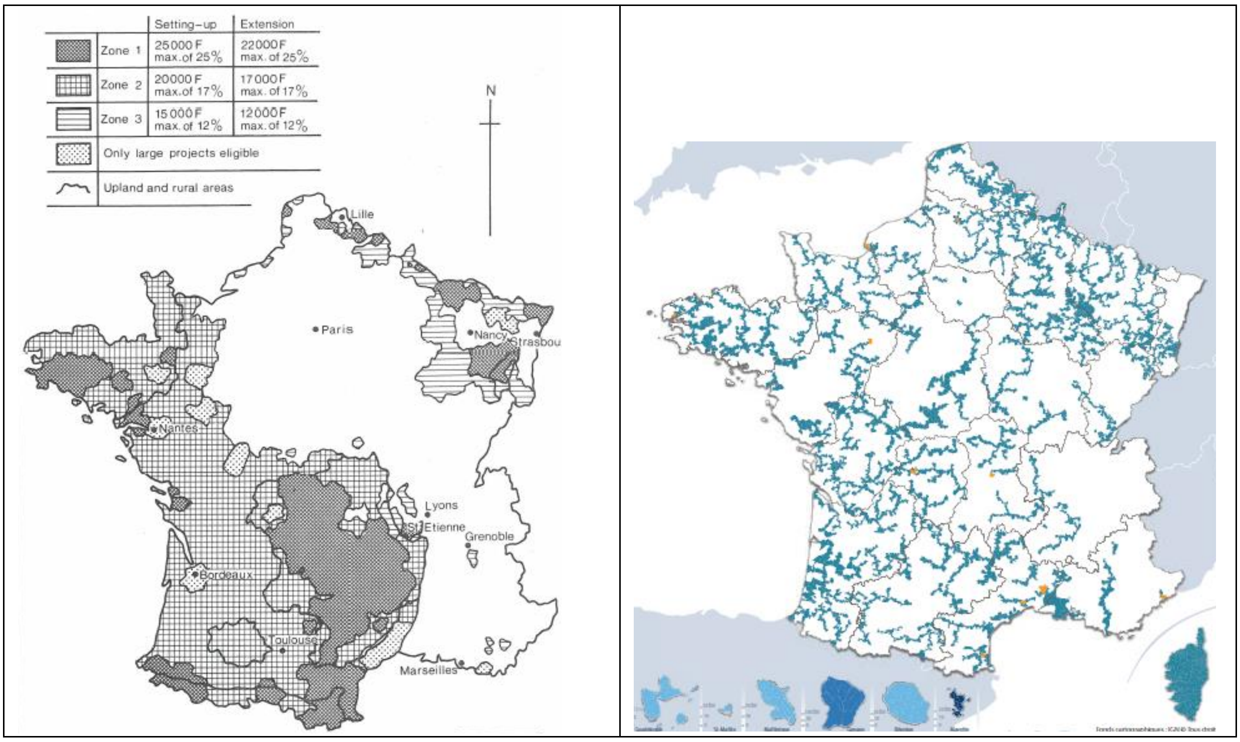
Source: EFTA Surveillance Authority decisions.

Because these are absolute criteria unaffected by enlargement, population coverage on the basis of population density has been sustained – in Norway, for example, the coverage of the regional investment aid map has even increased slightly since EEA membership. In Iceland, RAG 2000-6 resulted in a decrease in coverage, but a judicious redrawing of the NUTS boundaries applicable from 2008 resulted in an increase in coverage.

Downward pressure on assisted area coverage has also affected the appearance of the assisted area maps. In RAG 2000-6 the *quid pro quo* for the imposition of a population ceiling was, in principle, greater flexibility for Member States in the actual selection of areas. However, the Commission was anxious to avoid pin-pointing or ‘leopard skin’ maps design to circumvent the ceiling by focusing on areas of economic activity without including significant residential population. In consequence, the selection of assisted areas must conform to certain parameters. These rules have been relaxed somewhat since RAG 2000-6 under which the Commission sought to impose a ranking of ‘c’ areas and a strict cut-off once the population ceiling was reached. The fine-tuning involved in designing assisted area maps that maximise the available population quota is clearly evident in the current regional aid maps compared to their predecessors as the following maps from selected EC9 Member States show.

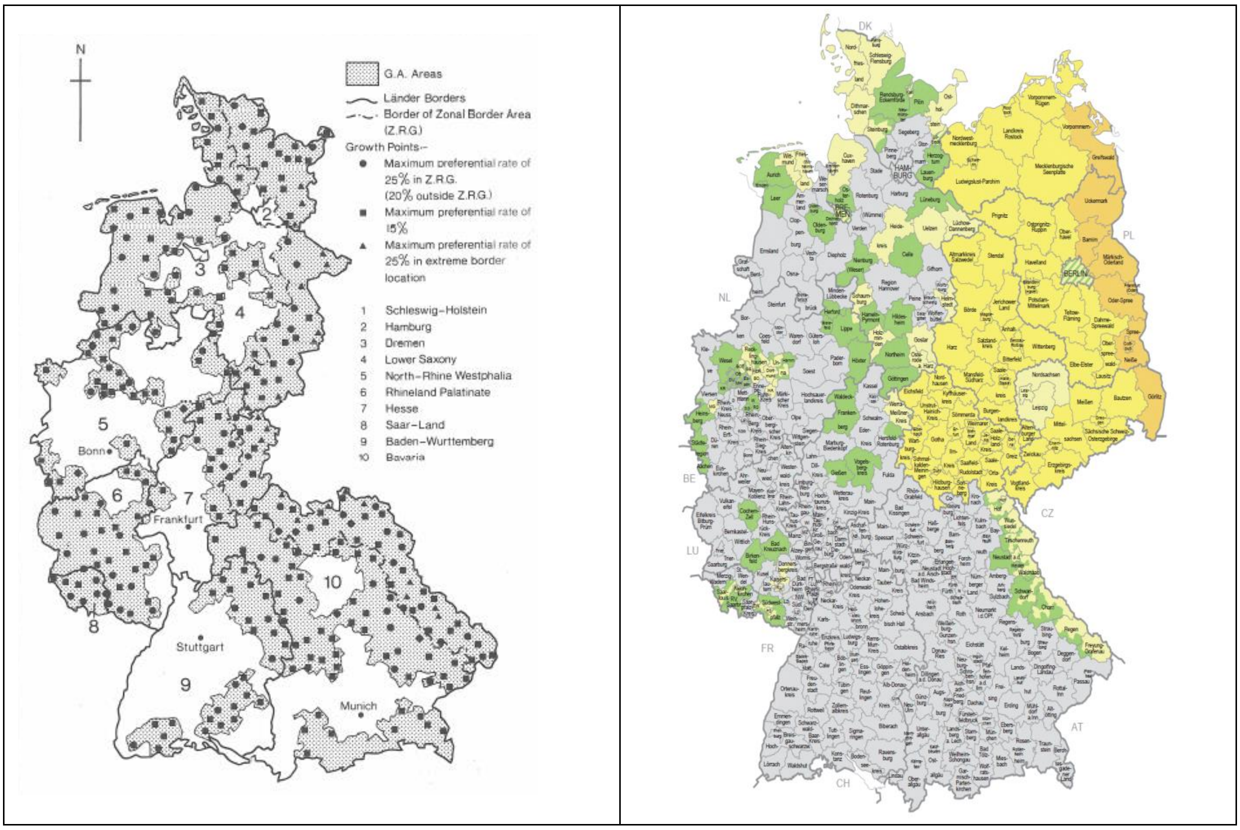
[23] Sweden, Norway, and Iceland rely entirely on population density to determine assisted area coverage; in Finland, a small proportion of ‘c’ areas (1.85 percent of the population) is non-predefined.

Figure 14: Assisted areas in France 1979 and 2014-20



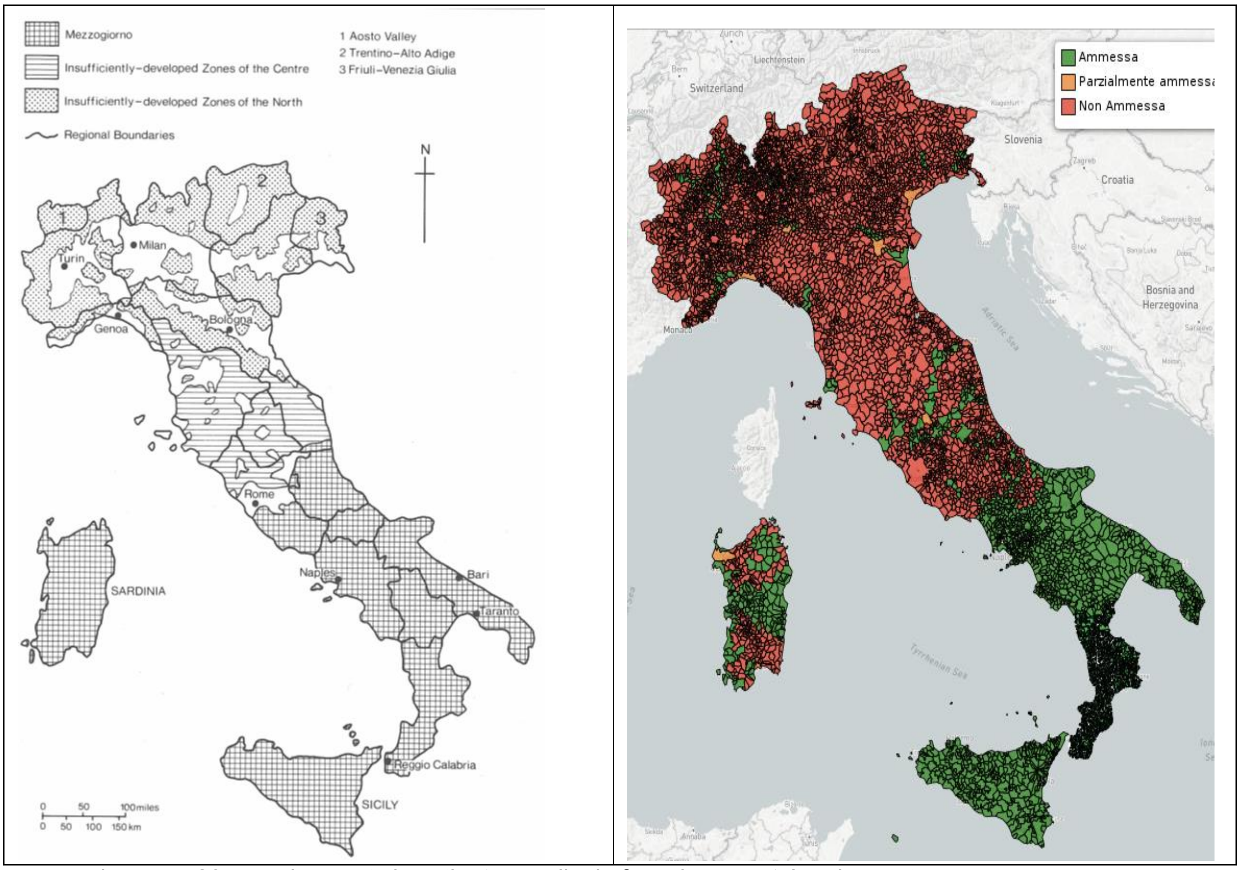
Sources: Yuill, D and Allen, K (1980) European Regional Incentives and CGET.

Figure 15: Assisted areas in Germany 1979 and 2014-20



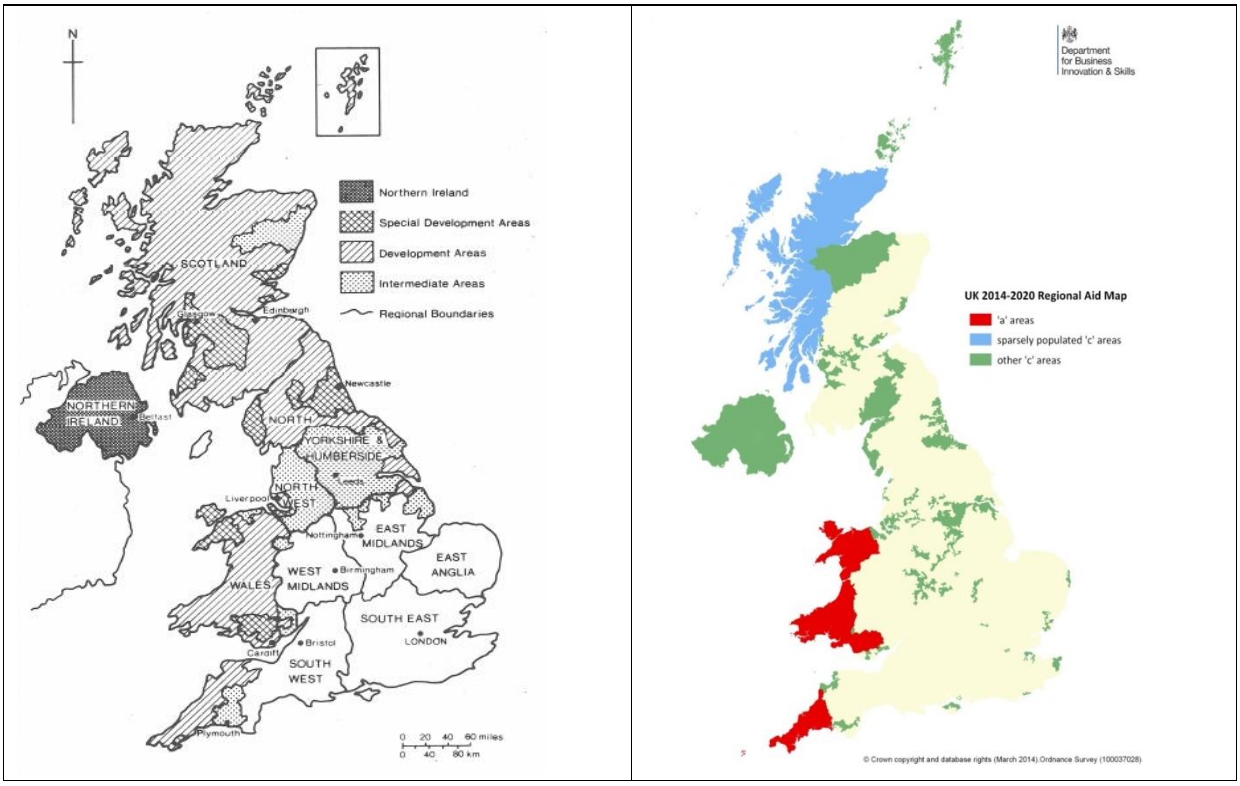
Sources: Yuill and Allen *op cit* and Bundesministerium für Wirtschaft und Energie.

Figure 16: Assisted areas in Italy 1980 and 2014-20



Note: The 2014-20 map does not show the 'upgrading' of Sardegna to 'a' region status – see Annex I.
Sources: Yuill and Allen, *op cit* and http://www.aiutidistato.org/project/carta-degli-aiuti-di-stato-regionali-italia/

Figure 17: Assisted areas in the United Kingdom 1979 and 2014-20



Note: The 2014-20 map does not show the 'upgrading' of Tees Valley & Durham to 'a' status – see Annex I.
Sources: Yuill and Allen *op cit,* and BEIS.

5. FORMS OF AID

- Commission perspectives on forms of aid are linked to two issues: first, the need to **measure and compare different types of support** – a grant equivalent; second, the desire to **eliminate aid that 'props up' inefficient activities** by supporting ongoing expenses.
- This led to **early action against so-called operating aids** in a number of countries, especially on accession.
- Opposition to operating aid contributed **to demise of some major instruments** of regional policy.
- Progressive **narrowing of forms of aid** offered – by late 1990s, main form of regional aid was capital grant in every Member State.
- Operating aid allowed in two areas: **outermost regions** and **sparsely-populated areas.**
- **Development of policy tortuous** – sometimes leading to curtailment of major operating aid schemes, but also extension of operating aid with GBER.

Commission action on forms of aid is closely-linked to considerations of transparency. The first principles considered that the requirement that "aid be transparent constitutes an essential condition for the coordination and assessment of the systems of aid." For the purposes of the principles of co-ordination, aid was transparent or measurable when the 'common method of assessment' could be applied to it.

The common method of assessment involved a number of conventions and assumptions which aimed to make aid comparable and measurable; it was based on relating the amount of aid to the amount of investment, expressed as a percentage of the aid after tax - net grant-equivalent (NGE). Implicit in this was that operating aid could not be transparent in these terms. Opposition to the use of operating aids, which was reinforced in successive versions of the regional aid principles in the 1970s, led the Commission increasingly to question the types of aid offered by the Member States. For example, in the **Netherlands**, investment premia which included scope to assist replacement investment were deemed permanently to reduce firms' running costs and therefore discourage them from adapting to market conditions; such aid could not, in the Commission's view, "facilitate the development of certain economic activities or certain economic areas".[24]

Successive enlargements saw countries forced to change regional aid packages either in the course of accession negotiations or shortly after. Thus, major elements of the **United Kingdom** regional aid package were altered as a consequence of Commission intervention. The Regional Employment Premium (REP), for example:[25]

> "seemed to infringe almost every canon of compatibility in that it constituted a continuing subsidy to operating costs available to all firms in the assisted areas and was unconditional upon any investment activity…"

[24] *Seventh Report on Competition Policy*, point 184.

[25] M. C. MacLennan 'Regional Policy in a European Framework' in D. Maclennan and J. R. Parr, *Regional Policy: Past Experience and New Directions* (Martin Robertson, Oxford, 1979) p. 251.

The Commission did not insist on the REP being withdrawn immediately, but maintained "periods of pragmatic silence and flexibility"; the REP was eventually abolished in 1977. In the course of the 1980s and 1990s, the Commission blocked the implementation or forced the amendment of significant regional operating aid schemes in several Member States. For example in **Spain**, legislation provided for a social security concession within the regional aid package, but the Spanish authorities were prevailed upon by the Commission not to implement the measure, this in exchange for concessions on the reference interest rate to be used in aid calculations. In **Italy**, Commission approval of a package of measures had been conditional on a given budget so that the refinancing of the measures required further Commission authorisation. In authorising this, the Commission took the opportunity to insist that a package of tax concessions should be converted into tax credits in order to relate their value to investment costs.[26] This quite systematic and opportunist approach to dismantling major existing operating aid schemes contributed to a high degree of homogeneity in the principal regional incentives of the Member States; by the end of the 1990s, the main element of the regional aid package in almost every Member State was a capital grant.[27] In the 2000s, the State aid compliance of the Special Economic Zones were a highly contentious issue in accession negotiations with **Poland** leading to a reduction in the timeframe for their implementation and the capping of values such that aid is not open-ended.[28]

In the main, the Commission has exerted considerable pressure to contain or eliminate operating aid. The major exception to this trend has been the ***retention of operating aid in the Outermost Regions (OMRs) and low population density areas.***

The Commission first outlined the circumstances in which it might authorise operating aid in the 1988 Communication and explicitly in relation to 'a' regions. In the case of **Portugal** the Commission was able to accept, at least initially, the tax provisions for Madeira, which allowed for significant reductions in corporation tax, among other things. Over time, however, the corporation tax concession has come under intense scrutiny from the Commission, resulting in its value being reduced considerably and explicitly linked to job creation.

Enlargement to include **Finland** and **Sweden**, which did not have 'a' regions, but did have distinctive regional disparities reflected in low population density, required a new approach. This was undertaken in an amendment to the 1988 Communication,[29] which defined of low population density areas (NUTS 3 areas with fewer than 12.5 inhabitants per head) and provided scope for transport aid related to additional costs incurred within such areas. Under the EEA agreement, parallel provisions applied to **Norway** and **Iceland**, with ESA responsible for supervision. This led to difficult negotiations and all three Nordic countries being forced either to 'reshape' social security concessions into transport aid, or to operate them on a *de minimis* basis only. Competition policy relations over the regionally-differentiated social security concession (RDSCC) in **Norway** have been particularly convoluted and protracted – see Figure 18.

[26] Commission Decision of 9 December 1992 on the refinancing of Law No 64 of 1 March 1986 on special aid to the Mezzogiorno, OJEC L117/22 of 13 May 1993.

[27] D. Yuill *et al* (eds.), *European Regional Incentives 1999*.

[28] Kislowska, M. (2006) The future of Special Economic Zones in the Aftermath of Poland's Accession to the European Union, Journal of International Business and Law, 5(1).

[29] Commission notice concerning an amendment to Part II of the communication on the method for the application of Article 92(3)(a) and (c); OJEC C364 of 20 December 1994.

Figure 18: Regional aid control and the Norwegian RDSCC – from outlawed to mainstream?

Action	Outcome	Timing
ESA review of NO RDSSC	Begins review in 1995 and proposes 'appropriate measures' to NO to adapt RDSCC into transport aid scheme	Dec 145/97/COL; May 1997
NO letter Ministry of Finance	NO refuses to comply	Letter of 24 July 1997
ESA investigative procedure		Dec 246/97/COL; November 1997
ESA conditional negative decision	RDSCC is incompatible with Article 61(3) EEA Treaty unless adapted into transport aid scheme and sectoral restrictions applied	Dec 165/98/COL; July 1998
NO challenges ESA Decision before EFTA Court	Suspension of application of ESA decision until Court ruling. NO contends that RDSSC is not State aid and that ESA has failed to take account of employment policy issues.	
EFTA Court ruling	EFTA Court finds in favour of ESA	E-6/98; May 1999
NO notifies amended RDSSC	Specifies excluded sectors, including: hydropower production, mining of metal ores and certain minerals, gas and oil production, shipbuilding, steel, telecommunications, financial services, and freight transport by road	September 1999
ESA positive decision	Approves RDSSC to end 2003 concluding that it can be accepted as indirect compensation for additional transport costs	Dec 228/99/COL; September 1999
RAG 2000-6	***Retains definition of SPA as <12.5 inh. per km^2; allows for transport aid in SPA***	***Adopted March 1998, applies January 2000***
COM negative decision on SE SSC	COM concludes that Swedish SSC scheme is incompatible; puts ESA conclusion in doubt and prompts re-examination of NO RDSSC	OJ L244/32; December 2000
ESA proposes appropriate measures	In light of COM decision on SE scheme, concludes that NO should take steps to render scheme compatible with Art 61(3) EEA by 1 January 2004.	Dec 172/02/COL, September 2002
NO notifies RDSSC and transport aid	Transition to Zone 1 rates in Zones 3 and 4 over 2003-07; new transport aid scheme in low population density areas	March 2003
ESA opens investigative procedure		Dec 141/03/COL, July 2003
Common accord of EFTA States	***Decision that RDSCC in Zone 5 is compatible with EEA Treaty due to exceptional circumstances***	***No 2/2003/SC, July 2003***
ESA positive decision	Approves transitional arrangements to phase-out RDSSC for Zones 2, 3 and 4 for 2004-07; no decision required on Zone 5 due to common accord of EFTA states	Dec 218/03/COL, November 2003
NO notifies change to RDSSC	Proposes that certain sectors (not exposed to competition) should not be subject to transitional rates	April 2004
ESA opens investigative procedure		Dec 245/04/COL, October 2004
ESA negative decision	Rejects notification of April 2004, but ESA Decision of November 2003 remains in force	Dec 298/05/COL, November 2005
RAG 2007-13	*LPD areas defined as NUTS 2 <8 inh. per km^2 or NUTS3 <12.5 inh. per km^2; allows for operating aid other than transport aid in least populated regions (NUTS 2 <8 inh. per km^2)*	*Adopted April 2006, applies from January 2007*
NO notifies revised RDSSC	Lower assisted area coverage (17.7% rather than 23.4%) but SSC rates revert to pre-transition decision levels (i.e. 2003).	June 2006
ESA positive decision		Dec 228/06/COL, July 2006
RAG 2014-20	***LPD area definition retained, but greater burden of proof on need for operating aid. Sectoral restrictions exclude energy and transport from RAG.***	***Adopted July 2013; takes effect July 2014***
NO notifies revised RDSSC	Higher assisted area coverage (19.7%), same SSC rates as 2014-20.	May 2014
ESA positive decision	Difficult negotiations over sectoral constraints (but ultimately imposed by ESA); also, major evaluation required given scale of budget	Dec 225/14/COL, June 2014
GBER 2014-20 revised	***New provisions: remove energy and transport sectors from regional aid exclusion wrt to regional operating aid schemes (art. 13(a)); and add provision for operating aid in very sparsely-populated areas up to 20% of labour costs.***	***Reg 2017/104 amending GBER 2014-20 (Reg 651/2014)***

Source: EPRC research.

At almost NOK 14 billion (€1.5 billion) annually, the RDSCC is currently the single largest regional aid scheme in the EEA31 in budgetary terms and pre-dated Norwegian membership of the EEA. As an operating aid, it came under the immediate scrutiny of ESA in 1995, with successive attempts to phase out the measure or ‘shoe-horn’ it into a transport aid scheme. However, what is striking is the extent to which competition policy has ultimately been reshaped around the RDSSC, rather than the other way around. The key steps in competition policy control of the RDSCC are summarised in Figure 18: changes to the various iterations of the regional aid guidelines (together with a common accord of the EFTA states that the northernmost zone faced exceptional circumstances), have progressively brought the treatment of regional operating aid for sparsely-populated areas into the mainstream. In a final ‘twist’ the 2017 revisions to the GBER essentially bring the scheme within the ambit of the block exemption regulation (budgetary issues and the requirement for an evaluation plan notwithstanding). As a result, more than 22 years on and in spite of changes in the interim, the current RDSCC is largely indistinguishable from its 1995 predecessor.

6. AID INTENSITY

- The **linking of aid intensities to the severity of the regional problem** has been a core component of regional aid control since the outset.
- Initially, there was no direct calibration, the Commission took the **prevailing rates** in the Member States as a starting point.
- Until the 2000s, Commission **ceilings did not bite**: 75% NGE was typical in many ‘a’ regions, but not necessarily affordable; generally, aid schemes became more discretionary and policymakers more value-conscious.
- Since 2000 **aid intensities have been lowered** across the board both in nominal terms and by using gross grant equivalent in place of NGE.
- This was partly motivated by **competition concerns**, as well as the **affordability** of high intensities for less prosperous countries.
- Aid intensities are as low as 10% GGE in some ‘c’ areas, raising questions about the **‘incentive effect’** of aid.

The linking of aid intensities to the severity of the regional problem has been a part of regional aid discipline since the outset; curiously, very early proposals even suggested that there should be aid minima, as well as aid maxima in order to ensure a level playing field![30] This suggestion was, unsurprisingly, not carried through into the regional aid principles of 1971 and 1973, which instead tended to take the prevailing aid ceilings as the starting point for aid ceilings in the assisted areas, while setting a limit of 20 percent in the central regions.

By 1979, the Commission had developed a more comprehensive matrix and complemented this with aid per job ceilings as an alternative. That said, the focus of attention in controlling regional aids was on their form and spatial coverage; the principles related to aid intensities tended not to ‘bite’, and were consequently less controversial, largely owing to the very high levels authorised.

Figure 19: Aid intensities under the 1979 principles

Region	Maximum capital intensity	Aid per job ceilings
Group 1: Ireland, Mezzogiorno, Northern Ireland, West Berlin, DOMs	75 % NGE	€ 13,000
Group 2: *Prime de développement régional* zones (FR); other Italian designated areas; Industrial Development Act assisted areas (UK)	30 % NGE	€ 5,500, subject to overall maximum of 40 % NGE
Group 3: Zonenrandgebiet (DE); Special Development Area and islands (DK)	25 % NGE	€ 4,500, subject to overall maximum of 30 % NGE
Group 4: other regions	20 % NGE	€ 3,500, subject to overall maximum of 25 % NGE

Source: Communication of the Commission on Regional Aid Systems, OJEC C31/9 of 3 February 1979.

As discussed earlier, the 1988 Communication explicitly distinguished ‘a’ regions and ‘c’ areas for the first time. The 1988 Communication set the maximum ceiling for ‘a’ regions as 75 percent net grant-

[30] Commission of the European Communities (1969) A regional policy for the Community, OOPEC, Luxembourg.

equivalent, effectively the same as under the 1979 principles. However, it stressed that aid levels should be adjusted in line with the severity of the regional problem and stated that the Commission would use its discretionary power to require regionally-differentiated aid ceilings below the 75 per cent ceiling. The Communication did not provide any indication of how rates would be set.

For the ‘c’ areas, Annex III provided a listing of regions, and corresponding award rate maxima, approved for regional aid under Article 87(3)(c) as at 1 October 1987. Curiously, given the emphasis on the common method of assessment and the need for comparability, award values were set in gross grant equivalent terms in some countries, but net in others, with maximum rates of award ranging from 7 percent NGE to 45 percent NGE (around 30 percent NGE was typical), with no real explanation of the basis for the rates set. Annex III explicitly excluded the *Zonenrandgebiet* and West Berlin, which were eligible for aid on the basis of (then) Article 92(2)(c), but would soon be the subject of a compromise with the Commission outside this specific provision.

As in other aspects of regional aid control, the 2000-6 Regional Aid Guidelines aimed to bring some order to the setting of aid maxima (though actual rates were those proposed by Member States and approved by the Commission within these limits).

Figure 20: Maximum rates of award by firm size under RAG 2000-06

Assisted area type	Large (% nge)	Medium	Small
‘a’ region (OMR)	65	+10% GGE	+15% GGE
‘a’ region (GDP<60% EC15 average)	50	+10% GGE	+15% GGE
‘a’ region (OMR with GDP > 60% EC15 average)	50	+10% GGE	+15% GGE
‘a’ region (GDP > 60% EC15 average)	40	+10% GGE	+15% GGE
‘c’ area Norther Ireland	40	+10% GGE	+15% GGE
‘c’ area low population density	30		
‘c’ area (standard)	20	+10% GGE	+15% GGE
‘c’ area (GDP > EC15 av. & unemployment < EC15 av.)	10	+10% GGE	+15% GGE

Note: Supplements of 10 per cent and 15 per cent gross for SMEs generally applied on top of these ceilings.
Source: Assembled from RAG 2000-06, point 4.8.

Overall, the RAG 2000-06 rates involved a substantial reduction in the ceilings applicable compared with the previous situation: typically, in an ‘a’ region rates would fall from 75 percent NGE to 40-50 percent NGE; in a ‘c’ area the reduction would be from 25-30 percent down to 10-20 percent NGE.

Figure 21: Maximum rates of award by firm size under RAG 2007-13 (% GGE)

Assisted area type	Large	Medium	Small
‘a’ region < 45% EU25 GDP; OMR < 75% EU25 GDP	50	60	70
‘a’ region < 60% EU25 GDP	40	50	60
‘a’ region < 75% EU25 GDP; OMR > 75% EU25 GDP	30	40	50
Statistical effect	30→ 20	40→ 30	50→ 40
‘c’ area low population density	15	25	35[b]
‘c’ area (standard)	15	25	35
‘c’ area (GDP > EC25 av. & unemployment < EC25 av.)	10	20	30

Source: Assembled from information in RAG 2007-13, paragraphs 44-48.

RAG 2007-13 continued this trend, but the combined effects of enlargement from EU15 to EU25 on GDP thresholds and the shift from net to gross grant-equivalents complicate comparisons between the position under RAG 2000-06 and RAG 2007-13. Nevertheless, it is clear that the reduction is *dramatic*: the shift from NGE to GGE alone might typically be around a quarter (i.e. 20% GGE is roughly equivalent to 25% NGE). In addition, the absolute rates fall too - in the case of ‘c’ areas they fall from 20 percent NGE to 15 percent NGE

RAG 2014-20 further reduces aid intensities across the board, except for the very poorest regions and the sparsely-populated areas.

Figure 22: Maximum rates of award by firm size under RAG 2014-20 (% GGE)

Assisted area type	Large	Medium	Small
‘a’ regions GDP <45% EU27 av.	50	60	70
‘a’ regions GDP per head < 60% EU27 av.	35	45	55
‘a’ regions GDP per head <75% EU27 av	25	35	45
‘c’ areas – ex ‘a’ regions until 31.12.2017	15	25	35
‘c’ areas – sparsely populated/border	15	25	35
‘c’ areas	10	20	30

Note: Rates for OMRs are increase by up to 20 percent for those with GDP per head at or below 75 percent of the EU average and 10 percent for the remainder. In ‘c’ areas (at NUTS 3 or below) that are adjacent to ‘a’ areas, the aid intensity may be increased so that the differential does not exceed 15 percentage points.
Source: Assembled from information in RAG 2014-20, para 171-177.

7. LARGE FIRMS, LARGE INVESTMENT PROJECTS AND LARGE AMOUNTS OF AID

- Commission was concerned from outset that **large scale regional aid could have undesirable effects**, but Member States **resisted Commission attempts at case-by-case scrutiny.**
- Evolution of policy reflects **tension** between need for **transparency** and mechanism that **captures aid with most serious effects**, and **resource implications** of case-by-case scrutiny.
- Initial approach **sectoral** – textiles, synthetic, fibres, shipbuilding – but different rules applied.
- **Motor vehicle framework 1997** subjected all regional aid over a given threshold to Commission scrutiny.
- Commission ambition was for **multisectoral approach** to limit capital-intensive aid and balance benefits to regional development against competition effects.
- First attempt – **1998 multisectoral framework (MSF)** – did not perform as intended.
- Breakthrough in 2002 MSF which imposed **reduction formula on aid rate** calculations and **notification threshold** for exceptionally large projects or awards; now integrated into Regional Aid Guidelines, with some changes to basis for Commission assessment.
- **Strong incentive to remain under notification threshold** as increasingly likely that notification will trigger full investigative procedure.
- For **'c' areas, large investment projects and large awards no longer very relevant** since RAG 2014-20 mainly excludes aid to large firms except greenfield projects.

From the first steps to control regional aid in the 1970s, the Commission expressed concern at the sectoral repercussions of aid and was keen to have a mechanism through which to assess large awards or those with potentially significant trade or competition effects. However, not only was such an approach resisted by Member States but it was also difficult to implement in practice. In consequence, an ad hoc and sector-specific approach was adopted for a number of industries considered to be overcapacity – notably synthetic fibres, shipbuilding and later motor vehicles, but in the main regional aid was operated simply on the basis of assisted area maps and corresponding aid ceilings until the late 1990s. However, the Commission's ambition was to have a more horizontal or 'multisectoral' approach to containing large individual awards and to attenuate the impact of the differences between Member States in their budgetary capacity for regional aid.

> It is important to ensure that state expenditure, far from representing a positive contribution to the competitiveness fo a region, does not become a covert anti-competitive mechanism which inhibits structural adjustment. Moreover, the effectiveness of the Community's policies to promote greater cohesion could be improved by some progressive reduction in aid intensities in the central and more prosperous regions.
>
> The link between the control of state aids and economic convergence covers several aspects. Existing aid ceilings for the purposes of regional development need to be rigourously enforced. It is not so much the quantity of aid granted as the importance of the differential between existing aid schemes which acts as the spur for foot-loose industrial location. Less developed Member States can therefore make significant budgetary savings provided that the appropriate differentials on a low level are maintained. In addition to national state aids, the granting of aid in cash or kind by sub-national (regional or local) authorities needs to be monitored, since it adds to the total volume of aid and probably aggravates counter-cohesive distortions since authorities in more prosperous parts of the Community are able to offer more generous incentives.

Source: European Commission (1990) Industrial Policy in an Open and Competitive Environment, COM(90)556.

Commission attempts to gain some control over large awards have been hard-fought, as reflected in Figure 23.

Figure 23: Evolution of treatment of large regional aid awards

Basis	Requirement	Analysis
Regional aid principle of 1970s	Member States to notify sectorally oriented measures for Com scrutiny	No evidence that this was done, at least systematically.
Code on aid to synthetic fibres 1977, 1996 (OJEC C94; 30.3.1996)	Any plan to offer aid to this sector to be individually notified in advance	Focus on sectoral consequences only and largely excluded possibility of aid for this sector
Framework on State aid to the motor vehicle industry 1997, OJEC C279; 15.9.1997)	Individual notification of aid exceeding €5m or to investments exceeding €50m in the motor vehicle sector	Imposed as an 'appropriate measure'. Com takes cost-benefit approach measuring costs in comparator plants to determine aid levels.
Multisectoral framework on regional aid for large investment projects, OJEC C107; 7.4.1998 (MSF1998)	Does not apply to sectors where already specific rules Individual notification if: • either: total project costs exceed € 50 million, aid level proposed > 50% of regional aid ceiling and > € 40,000 per job • or: total aid > € 50 million.	Com formula quantifies competition effects ('structural overcapacity' and market share), capital intensity (to limit aid to highly capital intensive projects) and regional impacts (direct and indirect job creation) to determine what rate of award the Commission would authorise; alternatively, it could open the investigative procedure.
Multisectoral framework on regional aid for large investment projects, OJEC C70 19 March 2002 (MSF2002)	Applied to all sectors. Reduction formula' applied to all regional aid schemes to lower aid ceilings: • investment <€50m, 100% of regional aid ceiling • investment >€50m,<€100m, 50% of regional aid ceiling • investment >€100, 34% of aid ceiling Notification if planned aid exceeds amount €100m investment could qualify for under formula	Notified projects ineligible for aid beyond threshold if over 'market screens' ie either: • beneficiary accounts for >25% of product sales; • or, capacity created is >5%, except in rapidly growing markets. If no market power or capacity concerns, reduction formula applies to whole investment. If doubts, Com obliged to open investigative procedure.
RAG 2007-13, para 64-70 incorporated MSF2002 largely unchanged; Criteria for an in-depth assessment of regional aid to large investment projects OJ 2009 C223/3 (LIPS guidance)	Reduction formula and notification threshold as for MSF2002, *but note that award ceilings had been lowered by RAG 2007-13*	If project over 'market screens' ie either: • beneficiary accounts for >25% of product sales; • or capacity created is >5%, except in rapidly growing markets, the aid can only be approved after investigative procedure and detailed analysis based on LIPS guidance. If no market power or capacity concerns, reduction formula applies to whole investment. If doubts, Com obliged to open investigative procedure.
RAG 2014-20 and GBER 2014-20	Reduction formula and notification thresholds as for RAG 2007-13, *but note that award ceilings lower further AND eligibility of large firms in 'c' areas severely curtailed.*	Market screens dropped (following *Smurfit Kappa*); all projects exceeding notification threshold subject to 'compatibility assessment' in RAG2014-20.

Commission proposals floated in the early 1990s focused on reducing the capital intensity of State aid through cost-per-job approaches, but these proposals were not made public and failed to gain traction with the Member States. Nevertheless, from the late 1990s, the Commission started to exercise greater control over aid to large firms and/or large amounts of aid, starting with the 1997 Motor Vehicle Framework (reflecting the widespread use of regional aid to influence the location or expansion of car and truck component manufacturing) and a more horizontal approach under the 1998 Multisectoral Framework (MSF 1998).[31] In broad terms, MSF 1998 provided that any proposal to offer aid over given thresholds (see Figure 23) had to be notified and approved prior to implementation. The Commission then quantified the competition effects and regional impacts to determine the rate of award (or, if in doubt, open the investigative procedure). [32]

In practice, MSF 1998 did not function as anticipated. The number of aid proposals notified was about half what had been expected (probably because policymakers offered awards just below the ceiling). In most cases that *were* notified, MSF1998 did not result in lower rates of award. This partly owed to national budgetary constraints and the emphasis on value-for-money, but also to the poor design of the formula.

The Commission drew lessons from its experience with MSF 1998, notably the need for simplification, the reduction of the administrative burden and the need for more predictability.[33] The result was a revised multisectoral framework adopted in 2002 (MSF2002). The core elements of this were subsequently incorporated into RAG 2007-13 and RAG 2014-20. In fact, as Figure 23 shows, the basic award reduction formula in RAG 2014-20 remains unchanged since MSF2002. However, the formula has become ***significantly more restrictive over time*** due to the reduction in rates of awards discussed earlier (see 6). For instance, in 2000-6 typical maximum rates were 40-50 percent NGE for 'a' regions, and 20 percent NGE in 'c' areas. By 2014-20 these were 25-50 percent GGE in 'a' regions; ***in 'c' areas RAG 2014-20 virtually eliminated the possibility of supporting investments by large firms***, but for eligible projects the prevailing rate is generally 10 percent GGE.

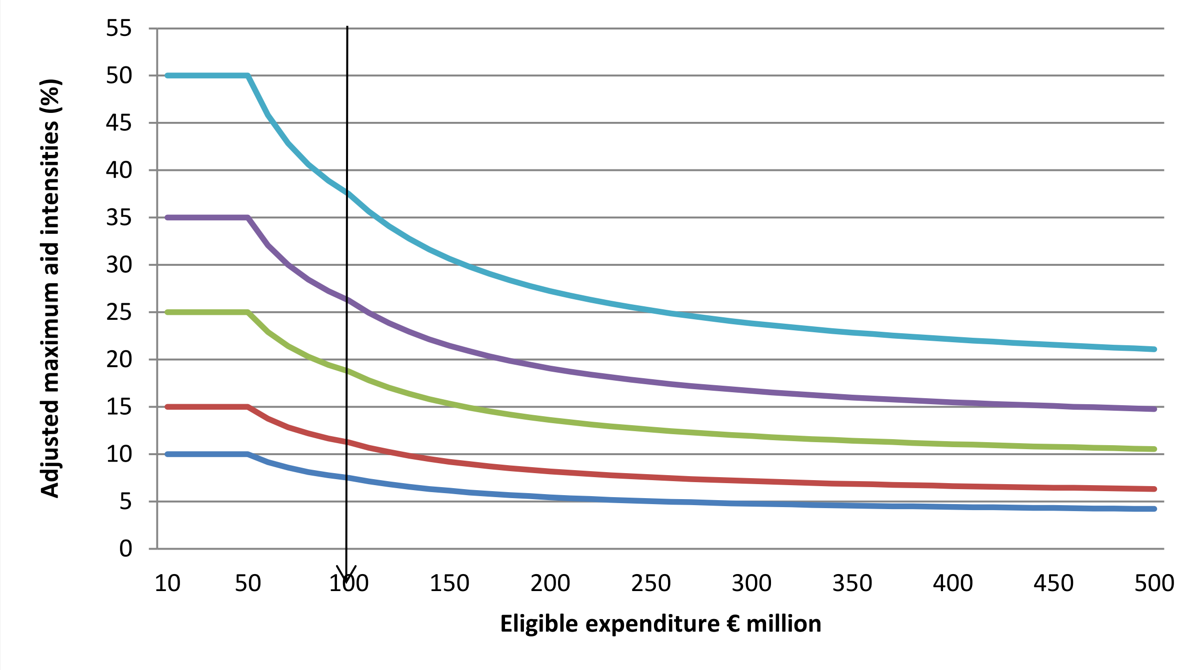
Importantly, notified aid to large firms must be limited to the minimum necessary to induce the investment to take place, calculated on a 'net extra cost' basis, in order to fulfil the proportionality criterion under the compatibility assessment. The rates illustrated in Figure 24 therefore act as a cap on the minimum necessary.

[31] Multisectoral framework on regional aid for large investment projects, OJ 1998 C107/7.

[32] For more details on the operation of MSF 1998 see F. Wishlade (2008) *The Control of Regional Aid to Large Investment Projects: Workable Compromise or Arbitrary Constraint?* EStAL 7(3) and M. Merola (2010) *Regional Aid: Recent Trends and Some Historical Background – with special focus on large investment projects,* EStAL 9(3).

[33] K. Junginger-Dittel (2007) 'Economic and legal problems of regional aid to larger investment projects' *The law and economics of European State aid control,* European School of Management and Technology, Berlin, 8-9 October 2007.

Figure 24: Adjusted aid intensities by maximum rate and eligible expenditure



Note: The initial rates vary according to the maximum aid intensity for the region, then decline for eligible expenditures over €50 million; where the proposed aid amount is higher than that for which a €100 million eligible investment would qualify (€7.5 million in a 10 percent area; €11.25 million in a 15 percent area, etc), then aid must be notified. However, in any event the adjusted aid amount is a ceiling.
Source: Calculated on the basis of RAG 2014-20, para 20(c).

The changes introduced in 2014 reflect the shift in the theories of competitive harm prioritised by the Commission since the late 2000s. In the early years of regional aid control, policy was primarily motivated by concerns at competitive outbidding for mobile investment – i.e***. competition between regions and nations***. The main emphasis was on seeking to define and contain the geographical areas in which regional aid could be available. It is worth recalling here that until the 1980s, many Member States provided support to large firms *throughout* their territories in the form of so-called 'general aids' which, from the 1970s, the Commission sought to discipline through the imposition of explicit regional aid maps. In this period, it could be argued that the control of regional aid was more concerned with *where* regional aid could be justified, rather than whether competition was distorted and how.

MSF 1998 marked the beginning of a second phase, in which the impact of aid on ***competition between firms*** was explicitly addressed in the case of very large projects; part of the analysis considered the impact of aid on capacity in a given sector and was the first attempt to consider the effects on market structure and competition between rivals. The reforms introduced under MSF 2000 and RAG 2007-13 in the treatment of large firms maintained the focus on market structure, with screens to identify cases most likely to raise issues of concern related to market power or sectoral capacity.

The 2009 LIPS Guidance saw the emergence of a third phase, which gives ***primacy to issues of economic efficiency and the perceived incentive effect of aid***. RAG 2014-20 confirms this trend, eliminating the market screens as the trigger for in-depth scrutiny, and, on the basis of a perceived *lack* of incentive effect, curtails the eligibility of large firms for aid in 'c' areas. In addition, the SAM concerns with the 'efficiency and effectiveness of public spending' are reflected in the GBER requirement to notify high budget schemes and the scope to impose an external evaluation as a condition of scheme approval.[34]

[34] RAG 2014-20, para 142-44.

8. COHESION POLICY RELATIONS

- In the early years **competition policy control of regional aid** was itself perceived as an instrument of Community regional policy.
- The implementation of the ERDF in the 1970s was uncontroversial since it mainly cofinanced nationally selected projects.
- The 1988 reform of the Structural Funds **raised major issues**, primarily relating to **spatial coverage,** requiring compromise between DGs for Competition and Regional policies. These tensions ultimately dissipated through the extension of Cohesion policy to all regions in 2007-13.
- Cohesion policy State aid relations are now affected by a range of issues that go beyond regional aid due to **two major underlying trends**.
    - First, the **definition of State aid has expanded** along with the concept of economic activities
    - Second, ESIF interventions now **extend beyond basic infrastructure and grants** to firms, which in the past either did not entail aid or could be accommodated within the regional aid rules.
- **State aid has an increasingly high profile in Cohesion policy** due to: SAAP and SAM; GBER introduction and expansion; ‘upgrading’ of State aid considerations in 2014-20 CPR.
- RAG 2014-20 ‘nods’ to Cohesion policy, but **a number of issues outside regional aid *per se*** have been or are **problematic**, including: definitional issues, financial instruments.
- The implications of **audit result in a risk-averse approach to State aid compliance**, with borderline projects more likely to be funded from domestic sources alone.

Since the 1988 reform of the Structural Funds, relations between European regional or Cohesion policy and competition policy control of State aid have often been strained. In the early years, the focus of tension was on the discrepancies in the ***spatial coverage*** of the Structural Funds compared to the national assisted areas. There were two main underlying reasons for the lack of coincidence. First, different indicators and time periods were used by DG Competition from those provided for in the Structural Funds Regulation. Second, Structural Funds area designation was essentially focused on *Community* averages whereas DG Competition’s method for ‘c’ areas (where most of the ‘non-coincidence’ arose) took account of both national and Community averages.

The emergence of two different sets of assisted area maps was of *practical* relevance for two reasons. First, the reformed Structural Funds placed special emphasis on the encouragement of *productive investment* for which State aids were a key policy instrument. Accordingly, it had been agreed that the Structural Funds could part-finance aid schemes implemented by the Member States under the Community Support Frameworks (CSF).[35]

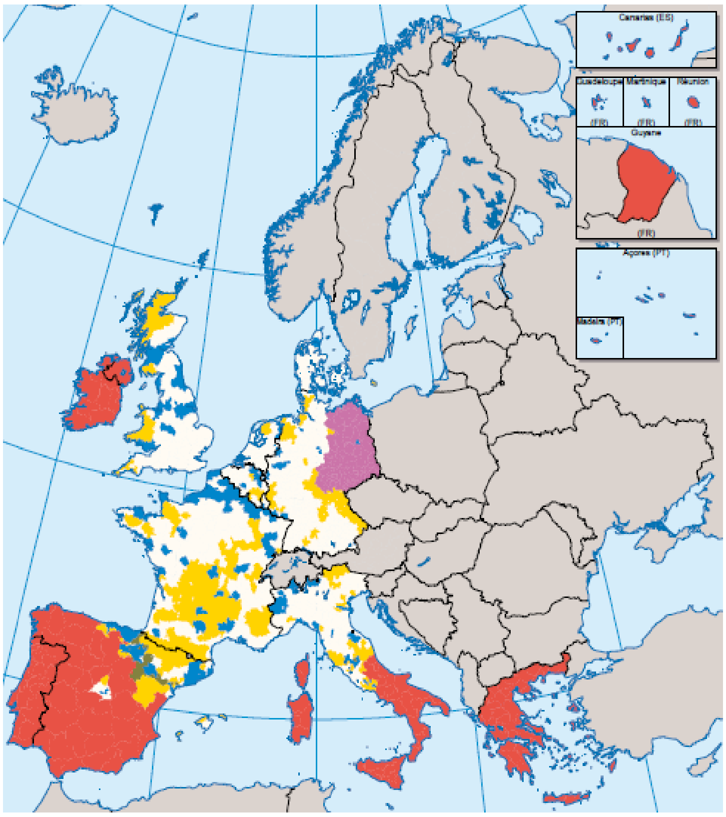
[35] Community Support Frameworks were the outcome of the negotiation process following the submission of regional plans by the Member States to the Commission. These set out the broad parameters of what was agreed in terms of strategic priorities and financing and were implemented through Operational Programmes (OP).

Second, in line with the Framework Regulation,[36] it was stressed that only aid notified and approved in advance in accordance with the State aid provisions of the Treaty (now Articles 107 and 108) could be considered for part-financing. Reflecting this provision, a standard clause was included in all the CSFs to the effect that all measures constituting aid should be identified in applications for Community assistance and that new aid proposals and changes to existing schemes should be notified in line with standard procedures.

Figure 25: Incoherence and uncertainty in area designation – the Abruzzi example

The national assisted area status of the Italian region of Abruzzi, designated as Objective 1 for the period 1988-1993 was due for review by DG Competition before the end of 1990, just a year into the five-year regional development plan agreed under the CSF. The outcome of the review was that Abruzzi should *lose* its 'a' region status, the level of GDP per head being significantly above the eligibility threshold. This was scarcely surprising since GDP per head in Abruzzi was well above the formal threshold for Objective 1even in 1988. This caused obvious difficulties within the context of the regional development plans agreed. Only after protracted discussion was agreement reached between DG Competition and DG Regio on the treatment of Abruzzi.

Figure 26: The 'coherence' of assisted area coverage 1989-1992

Type	% of population	Structural Fund Assisted Areas 1989-92
1. 'a' regions	20.6	
2. 'c' areas	24.2	
3. National assisted areas	44.8	
4. Objective 1	21.5	
5. Objective 2	16.3	
6. Objective 5b	5.2	
7. Structural Fund areas	43.0	
8. Common coverage	37.0	
9. National aid *only*	7.8	
10. Structural Funds *only*	6.0	
11. Combined (8+9+10)	50.8	

Source: Data kindly provided by DG Competition, European Commission; map by DG REGIO.

Lengthy and rather arcane debates ensued over issues of coincidence, coherence and cohesion.[37] These were largely resolved through a compromise between the Commissioners for Competition and

[36] Regulation (EEC) No 2052/88.

[37] See Wishlade, F (2003) Regional State aid and Competition Policy in the European Union, Kluwer Law International, pp145-180.

Regional Policy for the remainder of 1989-93, but the relationship between the maps was a major issue in the negotiation of the 1994-99 Structural Fund Regulations, and led to a dilution of DG Competition's reviews of *national* regional aid maps in the 1990s. As mentioned earlier, the dispute also contributed to the unravelling of the 1988 Communication on 'a' regions and 'c' areas. However, it was instrumental in determining the starting point for the EU-wide population ceiling post 2000; this was set at 42.7 percent of the population, which was judged to be the minimum necessary to enable Structural Fund assisted areas to be contained within national assisted areas, if Member States so desired. Debates over map coherence disappeared from the agenda thereafter since the 2007-13 Structural Fund Regulations applied EU-wide.

It is true that the 2014-20 Regional Aid Guidelines and GBER 'nodded' at the need for greater coherence between State aid control and Cohesion, but the scope of the adaptations was rather limited and in practical terms mainly involved some modest changes to ease State aid compliance for European Territorial Cooperation programmes. More generally, Cohesion policy State aid relations have been affected by a ***broader range of issues*** and trends that go well beyond regional policy concerns. This owes to two major underlying trends. First, ***the notion of State aid has expanded***. The liberalisation of certain sectors that were once purely the domain of the State has extended the range of activities that can be considered to be economic, and therefore subject to State aid control. Second, Cohesion policy intervention is increasingly diverse. The types of intervention financed by the Structural Funds now extend well beyond basic infrastructure and grant-based support to firms, which had been the mainstay of intervention in the early years, to include projects at the margins of market-based or economic activity. In addition, ***DG Competition's reform agenda*** and new ***developments in Cohesion policy,*** while simplifying some elements, have made others more challenging.

Figure 27: Current issues in Cohesion policy and State aid compliance

Definition of State aid	• 'Notion of State aid' Communication • But, fall-out from Leipzig-Halle
Expansion of GBER	• Extends range of exempt aid • Shifts compliance responsibilities to MS • Transparency requirements onerous
Emphasis on financial instruments	• State aid compliance issues more complex for FIs than grants • Differential treatment of shared management and EU level FIs
CPR 'upgrade' of State aid compliance	• No mention of 'State aid' in 1988 SF Regulation; CPR 2013 mentions 40 times! • Ex ante conditionalities on State aid

The 2005 State aid action plan and its successor the 2014 State aid modernisation programme overhauled the Commission's approach to disciplining State aid, revising guidelines across a number of areas and introducing new ones in policy areas not previously covered explicitly. The final element of the package involved addressing the ***definition of State aid***,[38] which some domestic policymakers had sought for a long time, in the hope that it would sharpen the scope of Article 107(1) and provide a practical tool for deciding whether a given measure fell within the scope of State aid. In practice, the notice did not alter the substance of policy – which ultimately relies on rulings form the European Courts – and is more a convenient restatement of extant case law in a single document than a policy toolkit. However, the fact that this runs to some 50 pages and broaches topics such as health care, education and research show how far the notion of State aid has come since the Spaak report, which stated explicitly that such activities would fall outside the scope of State aid (see Figure 1).[39]

Issues around the definition of State aid had been thrown into sharper relief for some domestic policymakers by the 2012 Leipzig-Halle[40] decision.[41] Following ***Leipzig-Halle**,* so-called 'analytical grids' for the assessment of the State aid implications of different infrastructures were developed, though for several years they appeared only under the auspices of the COCOF and were not explicitly published by DG Comp.[42] This led some, such as the Greek Managing Authority, retrospectively to reassess, and if necessary notify ESIF-cofinanced infrastructure projects. In this context, several port investments and gas pipeline projects which had not been considered to involve aid were notified and found to comprise aid, though this was deemed to be compatible aid.

Definitional issues in State aid ESIF cofinanced projects are not limited to infrastructure – some Managing Authorities cite projects with ***social objectives*** that have become ensnared by State aid considerations, reflecting the wide notion of 'undertaking'. Examples include support for youth centres and elderly day care centres, charitable organisations selling second-hand goods and employing disabled people. The social objectives of these projects are clear; however, the extensive reach of the State aid definition has meant that active consideration has had to be given to whether or not aid is involved and, if so, whether it can be accommodated within either the GBER or *de minimis* provisions.[43]

The ESIF cofinanced investment in the Messara museum is an interesting example of a case notified for legally certainty, though ultimately found not to involve State aid, albeit on somewhat surprising grounds. The Commission could arguably have concluded that the activities of the museum were not really capable of being commercial since the revenues would not cover the operating costs over a 15-year period in an area of activity from which the private sector was excluded by law. However, this decision illustrates the reach of the concept of economic activity, and the fact that it is not always straightforward to anticipate what will fall within it.

38 Commission Notice on the notion of State aid as referred to in Article 107(1) TFEU, OJEU C262/1.

39 This text was not carried through into Article 92 in its entirely, but it nevertheless makes clear that these areas would fall beyond the purview of the Commission for State aid purposes.

40 C-288/11 P, *Freistaat Sachsen and others v European Commission (Leipzig Halle)* *http://curia.europa.eu/juris/document/document_print.jsf?doclang=EN&text=&pageIndex=0&part=1&mode=lst&docid=131967&occ=first&dir=&cid=17784*

41 Others concluded that the outcome was implicit in the earlier *Aéroports de Paris case:* T-128/98 Aéroports de Paris v European Commission: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:61998TJ0128:EN:HTML

42 These are now produced explicitly as a DG Competition document: http://ec.europa.eu/competition/state_aid/studies_reports/state_aid_grids_2015_en.pdf

43 Wishlade, F and Michie, R (2009) ***Pandora's Box and the Delphic Oracle: EU Cohesion policy and State aid*** *compliance, IQ-Net Thematic Paper 24(2).*

Figure 28: Example of *economic activity – Messara Archaeological Museum*[44]

The Greek authorities considered that the construction of a new archaeological museum in Crete was non-economic because:

a) the safeguarding and exhibition to the public of unique Greek archaeological monuments is provided exclusively by the State according to the constitution and no private bodies are allowed to offer such services;

b) the main aim of the project was to protect antiquities and conservation and not to promote tourism or any other inherently commercial activity; and

c) the museum is not expected to result in profits – indeed the profitable exploitation of archaeological monuments is illegal under Greek law and any revenue would be channelled back into purely cultural purposes without benefiting any commercial activity.

The Commission was of the view that the existence of an economic activity could not be ruled out since the museum would provide a service against remuneration. The exclusion of third parties from providing a certain service did not rule out the existence of an economic activity, nor did the absence of profit. However, the Commission concluded that, largely owing to the remote location, the project would not have an effect on intra-EU trade.

It was common ground that the provision of canteen services and construction works *were* economic activities, however, in both cases the contractors either had been or would be appointed on the basis of open, transparent, non-discriminatory and unconditional tender procedures organised in line with EU Directive 2004/18/EC; there was no *advantage* accorded to the construction firm and as the museum had no effect on intra-EU trade, then nor could the canteen.

A by-product of the wide definition of State aid is the extended use of ***de minimis*** and / or ***block exemption regulations***. The Commission increasingly steers Managing Authorities towards these frameworks as a way of obviating the need for determining whether there is State aid present at all. This does provide some security from an audit perspective, however, not only does it blur the distinction between the existence of aid under Article 107(1) and the compatibility of aid under Article 107, but compliance with *de minimis* and GBER is not negligible in terms of administration.

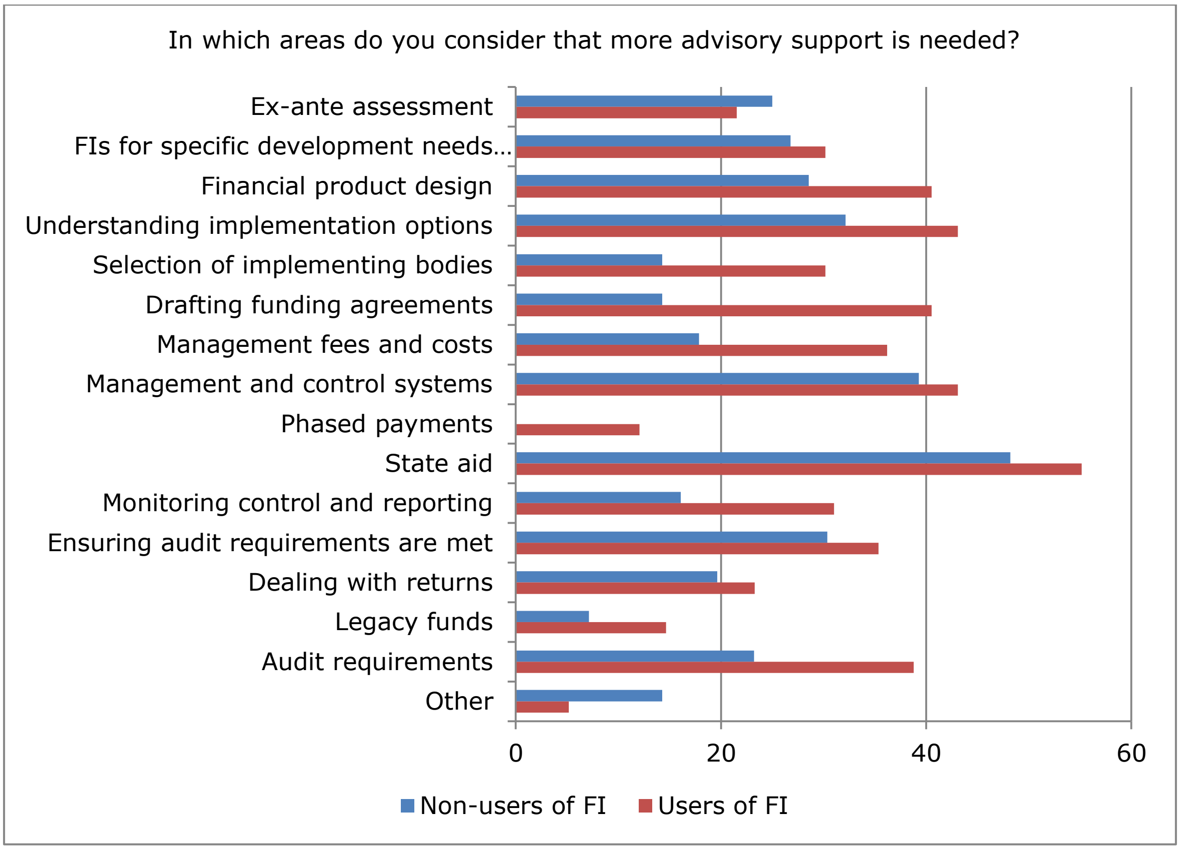
The 2014 General Block Exemption Regulation covers a very wide range of policy areas and has been subject to numerous clarifications from the Commission in response to so-called FAQ. As mentioned earlier, it has become increasingly important in reducing the number of notifications made to the Commission and decreasing the Commission's workload on 'routine' aid schemes; in 2014 90% of new aid measures were reported under the GBER. Importantly, it ***shifts the burden of policing aid onto national authorities***. This requires significant administrative capacity to monitor and report aid, especially in countries where numerous tiers of government and a range of agencies can potentially offer State aid. In addition, some Managing Authorities report difficulties in reconciling the simplified cost options provided for under the Common Provisions regulation (CPR) with the eligible expenditure requirements under the GBER; it remains unclear whether these concerns have been satisfactorily resolved in the revised GBER adopted in June 2017.[45]

The recent emphasis on the use of ***financial instruments*** entails multilevel State aid compliance assessments to ensure that aid at the level of the investor, the beneficiary and the final recipient are all compatible with the Treaty (or that no aid is present). These assessments more complicated for financial instruments than for grants, and it is clear that many Managing Authorities lack the capacity needed to assess compliance.

[44] Commission Decision SA.36581 (2013/NN) – *Greece – Construction of Archaelogical Museum Messara, Crete,* 6 November 2013.

[45] Commission Regulation (El) 2017/1084 amending Regulation 751/2014, OJEU L156/1 of 20 June 2017.

Figure 29: Advisory support needs among Managing Authorities



Source: Wishlade, F, Michie, R. Robertson, P and Vernon, P (forthcoming) Improving the take-up and effectiveness of financial instruments.

A further issue regarding financial instruments concerns the differences in the State aid treatment of shared management and EU level instruments. In this context, some have promoted the SME Initiative (SMEI) as a 'hybrid' option which avoids the State aid and procurement issues faced by tailor-made instruments and yet allows a degree of adaptation to specific conditions. However, it is premature to draw conclusions on the performance and satisfaction with SMEI as time is needed to understand to what extent SMEI meets regional requirements, and / or potentially undermines capacity building.

The 2014-20 Structural Fund Regulations have ***reinforced compliance with the State aid rules*****.** The 1988 Regulation referred more or less in passing to a need for the Structural Funds to comply with the competition rules and did not explicitly mention 'State aid' at all; 25 years on, the CPR mentions 'State aid' 40 times.

Under the ESI Funds Managing Authorities are responsible for the compliance of OP spend with the State aid rules – though ultimately a complaint would involve the Member State. Audit authorities undertake checks and report to the Commission. In almost all countries there also are national State aid units. These can be consulted in cases of doubt about the existence of aid or its compatibility. Their authority varies – some have a *mandatory* role and can prevent a transaction going ahead; others have an *advisory* role and need not be consulted in all cases and cannot prevent an ill-advised transaction from going forward.

It can be said that for Cohesion policy there is a relatively structured system for ensuring the compliance of ESI Fund spend with the State aid rules; this does not necessarily exist for *domestic* economic development policies, especially at the subnational level. Nevertheless, the European Court of Auditors reports suggest that State aid issues are the third most significant type of error (after procurement and eligible costs).

Figure 30: ECA State aid checks on ESIF cofinanced projects in 2010-2014

- 1573 projects
- 269 (17%) State aid relevant
- 50 (19%) contained State aid errors:
  - Aid intensity too high (11 cases)
  - Absence of incentive effect (7 cases)
  - *Undetected State aid or no notification (18 cases)*
  - Monitoring or formal requirements not met (14 cases)

Source: European Court of Auditors (2016) More efforts needed to raise awareness of and enforce compliance with State aid rules in Cohesion policy, Special report 24/2016.

A key innovation in the CPR is the introduction of so-called ***ex ante conditionalities*** in relation to State aid, requiring:

- Arrangements for the effective application of EU State aid rules
- Training and dissemination of information for staff involved in the implementation of ESI Funds
- Arrangements to ensure administrative capacity.

Action plans to achieve these objective were required in five Member States,[46] though it is interesting to note the Court of Auditors observation that the highest State aid error rates were not necessarily among the Member States that did not meet the ex ante conditionalities.

Even among countries that have not been required to adopt State aid action plans, there are signs that State aid discipline is being increased in ESI fund implementation. There is a heightened awareness among Managing Authorities of the need to identify when operations involve State aid. Examples of the approaches and steps taken include:

- Assessment of State aid implications from the outset – ie. 'call for projects' stage or earlier.

- Self-declaration of State aid relevance. For example, in Poland and in England, ERDF applicants must specify the State aid implications of their bid when they apply for funds. If they consider that no aid is involved, they must explain why; if State aid *is* involved, they must specify on what basis – for example, *de minimis* or GBER – they consider that support can be allowed.

- Increased role for State aid units. These are sometimes existing national units that play a wider role in State aid discipline, as in England, or newly established units responsible for State aid compliance in all OPs, as in Greece. However, some are dedicated units within the Managing Authority which must approve the approach taken to State aid compliance.

[46] Czech Republic, Croatia, Italy, Romania, Slovakia.

- Use of checklists drafted by State aid units to give Managing Authorities greater certainty in assessing whether or not there is State aid.
- Audit trails. Emphasis on explicitly recording the State aid assessment of all proposed operations and providing the justification for the view that there is no aid, or, if there is, on what basis it is compatible.
- Last, many national State aid units have provided State aid training programmes for Managing Authority staff, as well as providing advisory services on an ad hoc basis

In sum, there is evidence of an ***upgrading of the importance of achieving State aid discipline*** under the ESI Fund programmes. However, it also seems that ESI Funds Managing Authorities have become increasingly risk-averse in dealing with State aid issues. The systems have been tightened up and audit authorities can check the compliance of any transaction; lax procedures and failure to understand the State aid rules can lead to suspension of payments or delays, and the risk of losing funds. As a result, there is therefore a strong incentive to ensure the State aid compliance of ESI funds.

This, in turn, means that transactions which are potentially problematic are more likely to be funded through domestic finance. Outside the Managing Authorities, the State aid rules are typically less well understood, especially at the subnational level. Also, while there is an obligation to comply with EU law and the State aid rules, there is not necessarily a systematic mechanism for checking the State aid implications of every transaction. As a result, the presence of State aid may well emerge from complaints from citizens or competitors, or media reports, as has happened in several of the high profile sports stadia cases.

Nevertheless, there has been a growing emphasis on disseminating information on the State aid rules, and on the provision of advice – for example in Italy, Poland and Scotland the State aid units have become more proactive in providing training courses, developing internet based information, newsletters, etc.

At the same time, some are concerned that the approach to State aid should not become so risk averse that it jeopardises economic development policies. In the UK, and more recently in Germany, there is explicit reference to a “risk based” approach to State aid. In deciding whether to take a ‘no aid’ approach or to seek the legal certainty provided by notification and approval this involves the following:

- first, assessing the strength of the argument that the measure is not State aid;
- second, evaluating the likelihood of legal challenge or of the Commission discovering the measure (if the State aid ‘verdict’ is unclear);
- third, analysing the consequences of such a decision and how difficult they would be to remedy (for instance the impact on firms of having to repay funds, or the damage to political credibility).

A checklist of questions to consider is included in the UK State aid guidance.[47] It is important to stress that this approach is not about the risk of *disregarding* the rules, but rather about taking an informed approach to their interpretation and the possibility that the Commission view might differ.

Where there *is* aid, compliance with the GBER is clearly the preferred option for domestic policy as it is for ESI Funds. That said, most consider the document difficult to navigate and some requirements onerous. Also, the sense persists that some forms of intervention that were not previously considered to be State aid at all, are now brought within the scope of the GBER, with all that this entails in terms of monitoring and reporting.

[47] Annex E – A risk-based approach to State aid in BIS (2015) The State Aid Manual, BIS/15/148: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/607691/bis-15-148-state-aid-manual-update.pdf

9. EFFECTIVENESS AND EVALUATION

- Competition policy concerns with the **effectiveness** of State aid are comparatively new.
- Can be traced back to SAAP emphasis on **economic analysis** and SAM concerns with **efficiency of public spending.**
- RAG 2014-20 and GBER 2014 enable Commission to authorise and limit validity of large aid schemes conditional on **outcomes of evaluation.**
- Several major aid schemes undergoing evaluation; results and **impact on compatibility unknown.**

Competition policy concerns with the ***effectiveness*** of State aid are comparatively new. The 2005-9 SAAP was set in the context of the Lisbon agenda and critical of the lack of economic analysis in State aid cases: "most of the analysis in the practice of European state aid control is not firmly rooted in economic principles".[48] In response, policy shifted towards a more explicit balancing of the competition effects and wider benefits, reflected in the 2009 LIPS Guidance,[49] on the criteria it would take into account in making the in-depth assessment of very large investment projects. This deals with the positive effects of aid, including a consideration of the objectives of aid, the appropriateness of the aid instrument, the incentive effect and proportionality, and considers the negative effects, including the crowding-out of private investment and the effects on trade, before 'balancing' these elements. In *Dell Poland*, the Commission applied this guidance for the first time.[50]

SAM[51] provided for a re-focusing of State aid control against the backdrop of Europe 2020, as well as the effects of the economic and financial crisis. What is noteworthy in SAM is the perception that "State aid control is crucial in order to improve the efficiency and effectiveness of public spending"; this is accompanied by an emphasis on the identification and targeting of market failure and the promotion of measures with 'incentive effect'.

Against this background, among the new developments in both RAG 2014-20 and GBER 2014-20 is the scope for the Commission to make aid authorisation conditional on its approval of an evaluation plan. RAG 2014-20 provides the possibility for the Commission to limit the validity of aid schemes to four years in order for an evaluation to be carried out.[52] The precise terms of any requirement to undertake an evaluation[53] are defined in the approval of the aid measure. However, evaluations must by undertaken by experts independent from granting authorities, on the basis of a common methodology (which the Commission may provide) and must be made public. The circumstances in which an evaluation would be imposed as a condition of approval are limited to those with large budgets, schemes with novel characteristics or in areas where significant market, technological or

[48] H. Friederiszick, L-H Röller and V. Verouden (2008) *European State Aid Control: An Economic Framework,* in P. Buccirossi (ed.) Handbook of Anti-Trust Economics, MIT Press, Cambridge, Massachusetts.
[49] Communication from the Commission concerning the criteria for an in-depth assessment of regional aid to large investment projects OJ 2009 C223/3.
[50] Decision 2010/54/EC *Dell Poland* OJ 2010 L29/8.
[51] European Commission (2012) EU State aid modernisation – SAM, COM(2012) 209 final, 8 May.
[52] RAG 2014-20, para 27.
[53] See also: http://ec.europa.eu/competition/state_aid/modernisation/evaluation_issues_paper_en.pdf

regulatory changes are envisaged. Evaluations must be carried out in sufficient time for the results to feed in to the Commission decision on any extension of the scheme proposed, or at expiry.[54]

GBER 2014-20 provides for the expiry of GBER cover after six months for schemes with annual budgets exceeding €150 million, pending the approval by the Commission of an appropriate evaluation plan. In effect, this means that unless a Member State is able to provide an evaluation plan that is acceptable to the Commission, then GBER cover would be withdrawn and the scheme in question would need to be notified. As the whole scheme would then be subject to appraisal under RAG 2014-20, with the delays inherent in the notification process, there is a strong incentive for domestic policymakers to reach early agreement with the Commission on the evaluation plan.

GBER 2014-20 sets out the minimum requirements for an evaluation plan;[55] this should set out:

- the objectives of the aid scheme
- evaluation questions
- result indicators
- the methodology envisaged
- data collection requirements
- proposed timing, including the date of submission of the final report
- description of the independent body conducting the evaluation or the criteria to be used for selecting the evaluator
- mechanisms for publicising the evaluation.

A provisional supplementary information sheet for the submission of an evaluation plan is available. Its use is not yet mandatory as this requires changes to the Implementing Regulation. However, its use is recommended and it refers Member States to a staff working document on a common methodology for evaluation.[56] A version of this document had been subject to consultation at the end of 2013, and many Member States expressed concern at the ambition of the proposal and, more fundamentally, at the competence of the Commission to require evaluations of the effectiveness of measures financed with purely domestic resources.

The approval of the social security concession in **Norway** by ESA[57] provides for quite an exhaustive evaluation designed to assess the impact of the scheme on job opportunities and employment in the eligible regions, using results indicators that measure the impact which lowering employment costs through the scheme has on a range of factors including labour market participation rates and employment growth in the public and private sector. In addition, the evaluation is to assess the impact of the scheme on competition and trade, including issues related to size of undertaking and

[54] RAG 2014-20, para 144.

[55] GBER 2014-20, Article 2(14).

[56] Commission Staff Working Document "Common methodology for State aid evaluation, 28 May 2014, SWD(2014) 179 final
http://ec.europa.eu/competition/state_aid/modernisation/state_aid_evaluation_methodology_en.pdf

[57] EFTA Surveillance authority Decision of 18 June 2014 on regionally-differentiated social security contributions 2014-20 (Norway), Dec no: 225/14/COL: http://www.eftasurv.int/media/state-aid/Consolidated_version_-_Decision_225_14_COL__NOR_Social_Security_contributions_2014-2020.pdf

international competition. A detailed timeline for the evaluation, as well as the participation of ESA in a methodological workshop, was also provided for with the delivery of the evaluation to ESA envisaged by end 2018. Domestically, the process began with a feasibility study which was the subject of a wider consultation.[58] This led to the appointment of the successful tenderer late in 2015.

Figure 31: Evaluation plans under RAG and GBER

Country	Scheme	Basis	Annual budget	Reference
Norway	Regionally-differentiated social security contribution (RDSSC)	RAG	€1404 million (NOK 13 billion)	Dec no: 225/14/COL
United Kingdom	Regional Growth Fund (RGF)	GBER	€4352 million (£3.2 billion – rounds 5 and 6, not all of which is State aid)	SA.39273
Germany	GA support for productive investment	GBER	€585 million	SA.39460
Poland	Special Economic Zones (SEZ)	GBER	€507 million (PLN 2.14 billion)	SA.40523, SA.38830
Poland	Competitiveness of SMEs under Regional Programme 2014-20	GBER	€226 million	SA. 43142
Portugal	Inovação Empresarial	GBER	€350 million	SA.42136
Italy	Tax credit for productive investment	GBER	€617 million	SA.45184

Elsewhere, evaluation plans were reported on the basis of the GBER rather than the RAG (which was adopted earlier). In other words, the evaluation requirement was triggered by the budget of the scheme rather than through the notification process under RAG 2014-20.

At the time of writing, none of the evaluations are complete so the impact of the results cannot be known, but it would mark a new departure in State aid control if regional aid schemes were disallowed on the basis of evaluation outcomes.

[58] Evaluation of the Regionally Differentiated Social Security Contribution scheme in Norway – a feasibility study: https://static1.squarespace.com/static/576280dd6b8f5b9b197512ef/t/57c6b2222994ca88ec544609/1472639524524/R16-2015+RDSSC+scheme+feasability+study.pdf

10. REGIONAL AID GUIDELINES POST-2020?

- Consideration of post-2020 State aid reforms seems to be at an **early stage**; there is **no 'high level' State aid agenda** like SAAP or SAM.
- Commission is taking **soundings about the future of RAG and GBER**, but no concrete outputs yet.
- Reapplication of the RAG 2014-20 eligibility criteria suggests some **changes to 'a' regions,** some induced by Brexit.
- **Can same / similar method be used** for 'c' coverage as in the past?
- Outcomes may be affected by further recent **NUTS changes.**

Consideration of the future of the Regional Aid Guidelines and the General Block Exemption Regulation seems to be at an early stage. The Commission is taking soundings from Member States, but there are no concrete outputs from this process yet. In some countries, thought is being given to how the Regional Aid Guidelines might change. In **Germany**, for example, a major reform of regional policy has been agreed by the Federal government,[59] and a commissioned study has indicated some changes to the Regional Aid Guidelines that would facilitate German regional policy in the context of (anticipated) lower population coverage. These include an increase in the overall population ceiling and more consideration of domestic disparities and at a finer level of geography than at present in order to reflect local conditions. In **Norway**, by contrast, the authorities are content with the present framework, reflecting the inclusion of the RDSSC in the RAG / GBER, and the relative stability of the approach to sparsely-populated areas which allows for Norwegian regional policy issues to be accommodated.

In looking forward, there are a large number of variables that could affect spatial coverage of future maps, as well as other dimensions of regional aid control.

Regarding ***spatial coverage,*** the starting point concerns which of the parameters are potentially open for adjustment, assuming the overall scheme of the RAG remains substantially unchanged, which itself remains unclear. Key questions include:

- What would be the overall initial population coverage?
- Would the 'a' threshold remain unchanged, adjusted for Brexit (ie NUTS 2 regions with GDP(PPS) per head less than 75 percent of the EU27 (ex UK) average?
- Would any adjustment be made, if required, for 'a' regions losing that status due to Brexit?
- Would the same system of 'predefined' and non-predefined 'c' areas be applied?
- How would the non-predefined 'c' area population be divided between countries?
- What 'floors', 'ceilings' and transitional arrangements might apply?

[59] German federal government (2017) *Fortschrittsbericht der Bundesregierung zur Weiterentwicklung eines gesamtdeutschen Fördersystems für strukturschwache Regionen ab 2020*, Berlin, September 2017

Figure 32: Key spatial coverage parameters

	2014-20	**Post-2020?**
Initial population coverage	46.53% EU27 (ex HR)	% population EU27 (ex UK) ?
GDP data NUTS 2 (‘a’ areas)	2008-2010 (initial) 2012—2014 (mid-term review)	2015-2017 (initial)
GDP data NUTS 3 (‘c’ areas)	2008-10	2015-17
Unemployment data at NUTS 3 (‘c’ areas)	2010-12 [partial]	No longer published at NUTS 3 – use NUTS 2? 2017-19
‘a’ region threshold	GDP(PPS) per head <75% EU27 (ex HR) average (+OMR)	GDP(PPS) per head <75% EU27 (ex UK) average? (+OMR)
Predefined ‘c’ areas – former ‘a’ regions	Areas losing ‘a’ region status	Areas losing ‘a’ region status; also areas losing ‘a’ region status due to ‘Brexit effect’?
Predefined ‘c’ areas – sparsely-populated regions	NUTS 2< 8 inh per km^2 NUTS 3 <12.5 inh per km^2	NUTS 2< 8 inh per km^2 NUTS 3 <12.5 inh per km^2

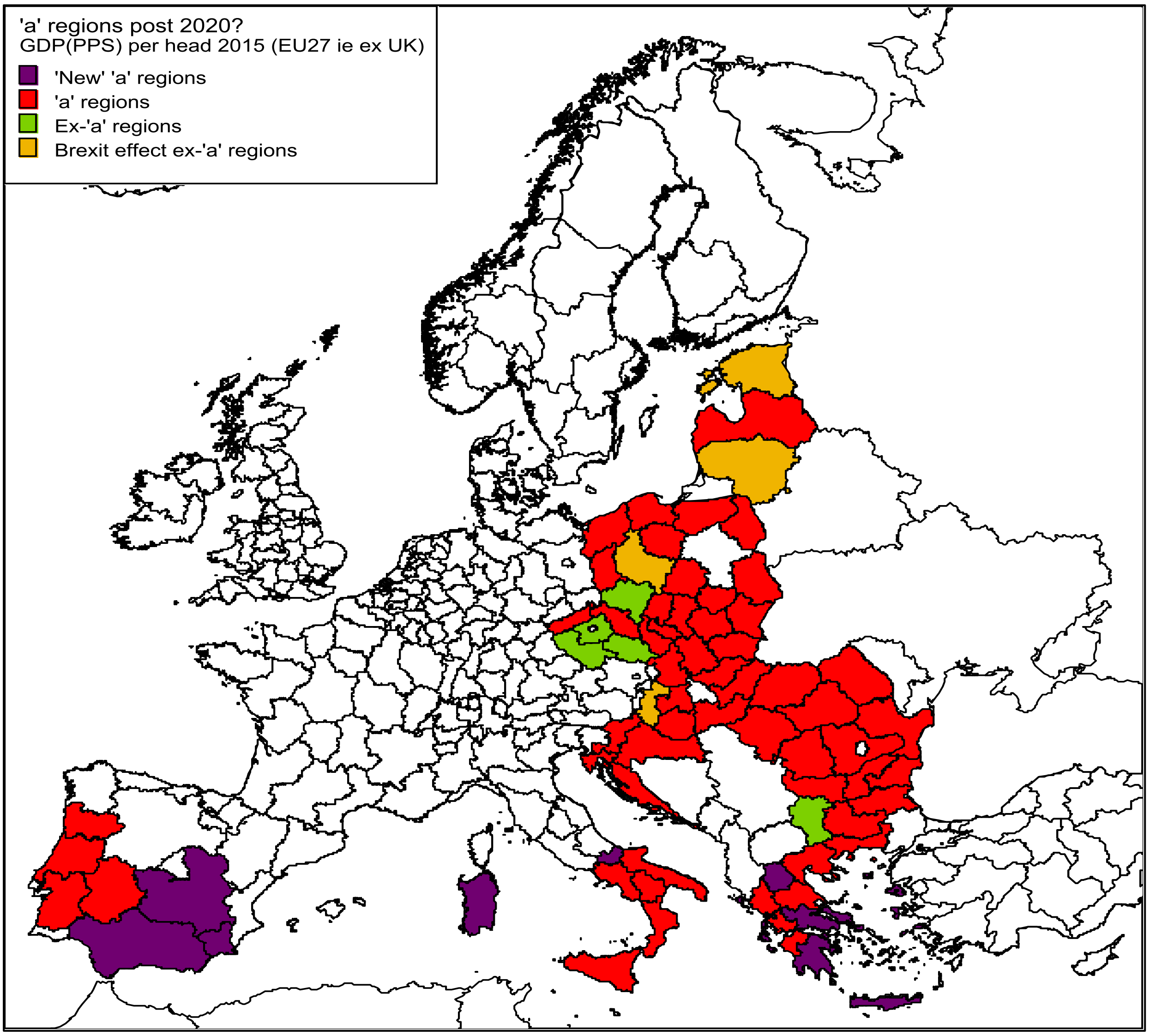
Against this background, it is difficult to speculate about what approaches might be taken and their impact. Moreover, in a number of countries – notably Latvia, Ireland and Poland ***2016 NUTS boundary changes*** also seem set to have an impact on eligibility.

Notwithstanding these uncertainties, Figure 33 indicates what a ‘rolling forward’ of the current approach might imply. This uses 2015 data (likely the first year of the three-year average to be used) and excludes the United Kingdom from the calculations – i.e. the average is EU27 (EU28-UK) – and the geography is NUTS 2013.

There are several points to note from this:

- Molise and Sardegna in Italy and several regions in Greece and Spain would ‘***regain’ ‘a’ region status,*** having ceased to qualify in 2007 – though most were reclassified at the 2016/17 mid-term review (see Annex I).
- Strední Cechy, Jihozápad and Jihovýchod (CZ), Dolnoslaskie (PL) and the Sofia region in Bulgaria (Yugozapaden) would cease to quality as ‘a’ regions, having ***outgrown the ‘a’ region threshold***
- Lithuania, Estonia, Nyugat-Dunántúl (HU) Wielkopolskie (PL) would ***lose ‘a’ region status as a consequence of Brexit,*** owing to the fact that, for 2015, UK GDP(PPS) per head is above the EU average, so removing the UK from the data has a statistical effect on the threshold. (Were the United Kingdom to remain, and data be calculated on the basis of EU28, Tees Valley & Durham and South Yorkshire would qualify as ‘a’ regions, in addition to West Wales & the Valleys and Cornwall & the Scillies, as now).

Figure 33: 'a' regions post 2020 and post Brexit?



Source: EPRC calculations from Eurostat data.

Several other dimensions of regional aid control are explicitly or implicitly linked to decisions on spatial coverage. For example, if controls over the eligibility of large firms for regional aid in 'c' areas remain tight, then there may be scope to relax aspects of the designation criteria for 'c' areas. However, it remains to be seen whether reforming the Regional Aid Guidelines has essentially reached its limits: successive communications and guidelines have dramatically reduced assisted area coverage in many countries, instigating a recasting of the assisted area maps; aid intensities have been reduced by as much as two-thirds; support for large firms has been largely eliminated in the 'c' regions; and the continued approval of schemes with large budgets has been made conditional on the outcome of evaluations of their effects and effectiveness. What now remains for the Commission to address save fine-tuning?

11. CONCLUDING ISSUES

This paper has taken a long-term perspective on the evolution of State aid control over regional development in recognition of a policy 60 years in the making.

Over time, every dimension of regional aid policy has come under scrutiny and often been subject to change. The focus of the paper has been on the changes brought about by competition policy, but it is certainly the case that, in some areas, the Commission was pushing against an open door: few, if any, countries now would contemplate large scale regional aid grants that automatically subsidised any new investment by any size of firm located in designated areas. Related, the reduction in aid intensities across the board has arguably been successfully in containing subsidy races for mobile projects in a way that more informal arrangements in other jurisdictions (such as the US) have been unable to achieve.

This paper has suggested that, for the most part, domestic regional aid relations and the RAG are settled: there is scope for tinkering with eligibility – especially for transitional areas – and for easing the area designation criteria for ‘c’ areas further, especially as support for large firms in these areas is largely eliminated so that the only effect is to change maximum aid intensities for SMEs.

This paper has also argued that State aid relations with Cohesion policy have become more complex because of the combined effects of the expanding concept of State aid and the increasing diversity of Cohesion policy interventions. These tensions are exacerbated by the role of audit, which creates a tendency to ‘fudge’ decisions about whether transactions involve aid and blur them with issues of compatibility. At the same time, the GBER does not readily accommodate all Cohesion policy needs, and, specifically, the treatment of financial instruments currently discriminates against FIs under shared management in comparison with EU level instruments.

ANNEX I: REGIONAL AID MAP CHANGES – MID-TERM REVIEW

The 2014-20 Regional Aid Guidelines make provision for a limited review of assisted area coverage in 2016.[60] In June 2016, the Commission issued a Communication indicating the scope for changes to assisted areas with effect from 1 January 2017.[61] The Communication mainly concerned Article 107(3)(a) regions ('a regions') and rates of award, but also confirmed the possibility to amend Article 107(3)(c) areas ('c areas'). In all cases, Member States wishing to amend their maps had to notify the proposed changes to the Commission by 1 September 2016.

Table A: NUTS 2 regions eligible for 'a' region status from 1 January 2017

Member State	Region	GDP(PPS) per head 2008-2010 EU27=100	GDP(PPS) per head 2012-2014 EU27=100
Greece	Dytiki Makedonia	83.67	69.00
	Ionia Nisia	82.67	66.67
	Sterea Ellada	83.33	64.67
	Kriti	83.33	62.00
Spain	Castilla-La-Mancha	82.33	72.67
	Andalucía	78.00	68.00
	Murcia	85.67	74.67
	Melilla	83.67	68.67
Italy	Sardegna	79.00	74.00
United Kingdom	Tees Valley and Durham	77.33	73.67

Source: European Commission Communication (see footnote 61).

The regions listed in Table A could be proposed for 'a' region eligibility with a maximum rate of award of 25 percent of eligible expenditure. Of key importance, the change in status also enables more flexibility in aid to large firms, since support for large firms in 'c' areas is essentially limited to green-field investments. All four countries mentioned in Table A took up the option to 'regrade' the regions concerned to 'a' status.[62]

In addition, in **Greece** and **Portugal** a decline in GDP per head in regions which already had 'a' status meant that higher rates of award could be applied (see Table B). In both case the national authorities took up this option.[63]

[60] Para 183-5, Guidelines on regional State aid for 2014-20 [hereafter 'RAG 2014-20'], OJEU C209/1 of 23 July 2013.

[61] Communication for the Commission amending Annex I to the Guidelines on regional aid for 2014-20, OJEU C231/1 of 25 June 2016.

[62] State aid cases: SA.46320 – Greece; SA. 46099 – Spain; SA.46199 – Italy; and SA.46361 – United Kingdom.

[63] State aid cases: SA.46320 – Greece; and SA.46356 – Portugal.

Table B: Changes in aid intensity 2017-20

Member State	Region	GDP(PPS) per head 2008-2010 EU27=100	GDP(PPS) per head 2012-2014 EU27=100	Aid intensity 2017-20 (%)
Greece	Anatoliki Makedonia, Thraki	68.00	51.67	35
	Kentriki Makedonia	72.33	57.33	35
	Thessalia	69.33	55.33	35
	Ipeiros	63.33	51.67	35
	Dytiki Ellada	65.00	55.00	35
	Peloponnisos	74.00	59.67	35
	Voreio Aigaio	75.00	57.33	35
Portugal	Madeira	104.00	73.00	45

Source: European Commission Communication (see footnote 61).

There was also scope to review 'c' area coverage. The changes could involve up to 50 percent of the non-predefined 'c' area population. In some counties (namely **Spain**, **Italy**, and the **United Kingdom**), the 'c' area population which could be amended was reduced because of the eligibility of new 'a' regions; understandably, none of these countries opted to amend the map of 'c' areas, with the result that coverage in these countries for 2017-20 is slightly higher than in 2014-2016.

In others, the scope to amend the 'c' areas did not apply because there were no existing 'c' areas or the country was already designated in its entirety (Bulgaria, Czech Republic, Estonia, Greece, Croatia, Latvia, Lithuania, Malta, Poland, Romania, Slovakia, Slovenia), or because all the 'c' areas were 'pre-defined' by the population density criterion (Sweden).

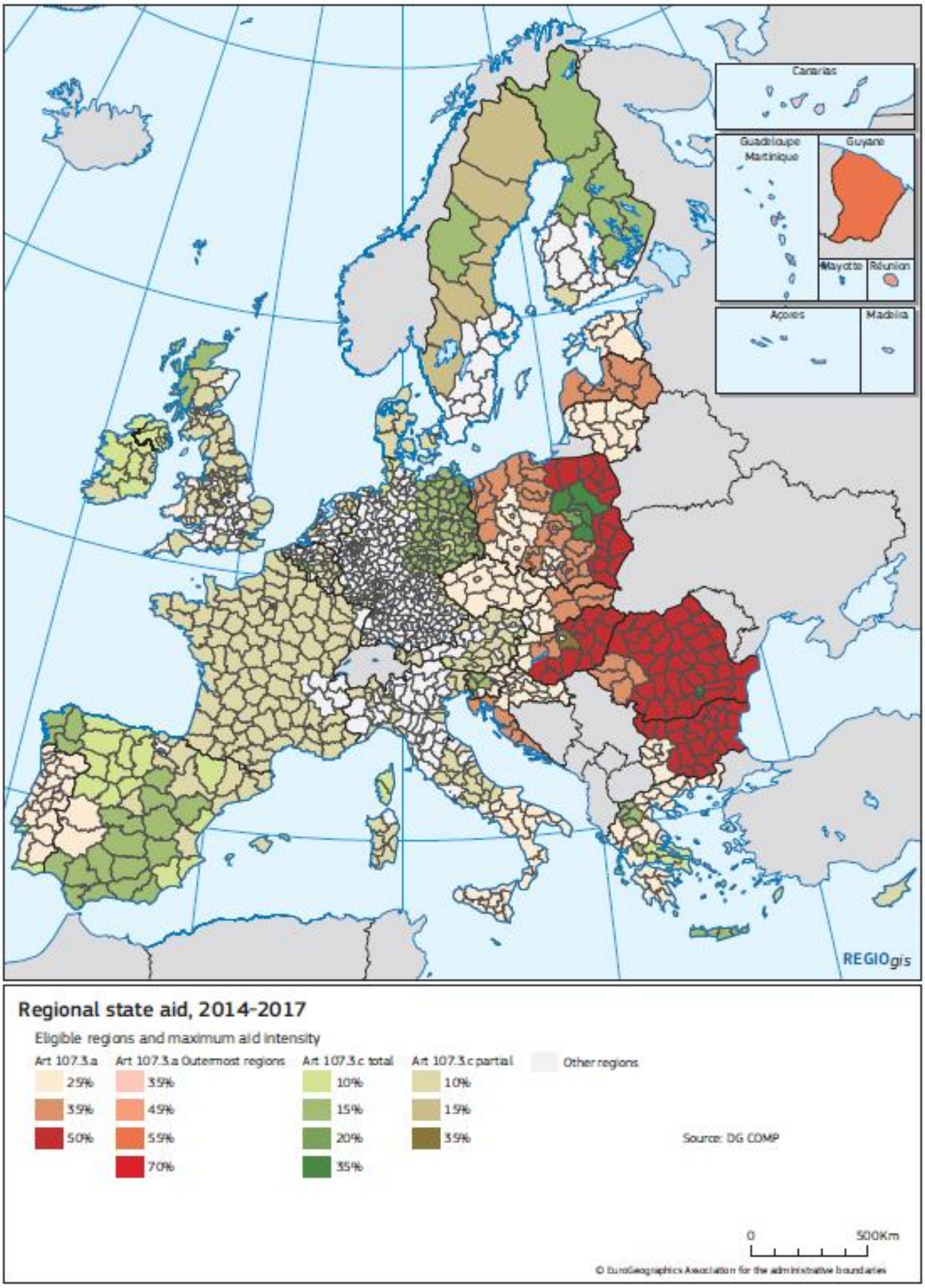
Among the remaining countries, few decided to make changes and these were minor: in **Finland** a small adjustment was made in involving several LAU2 areas, slightly increasing the overall population coverage (Finland had not used its full 'c' area quota at the outset).[64] In **Germany**, the NUTS 3 areas within Mecklenburg-Vorpommern were realigned with the new boundaries; this had no impact on population coverage but involved a minor change to the population covered by a higher aid intensity.[65] In **Hungary** the exchange of LAU2 areas involved a very slight reduction in population coverage.[66] No other countries proposed any mid-term review of 'c' areas.

Separate from the mid-term review process, **France** opted to make a second use of the population reserve. The French authorities did not use the full 'c' area quota at the outset, initially leaving a population reserve of 233,757 inhabitants (0.36 percent of the national population), reduced to 172,207 inhabitant after the first use of the reserve. In 2017 the Commission agreed to the proposal to add 52 municipalities comprising a population of 128,060 to the assisted areas map,[67] still leaving a reserve of 44,147 for potential future use.

[64] State aid case no. SA.46345 – Finland.
[65] State aid case no. SA.46343 – Germany.
[66] State aid case no. SA.46346 – Hungary.
[67] State aid case no. SA.47094 – France.

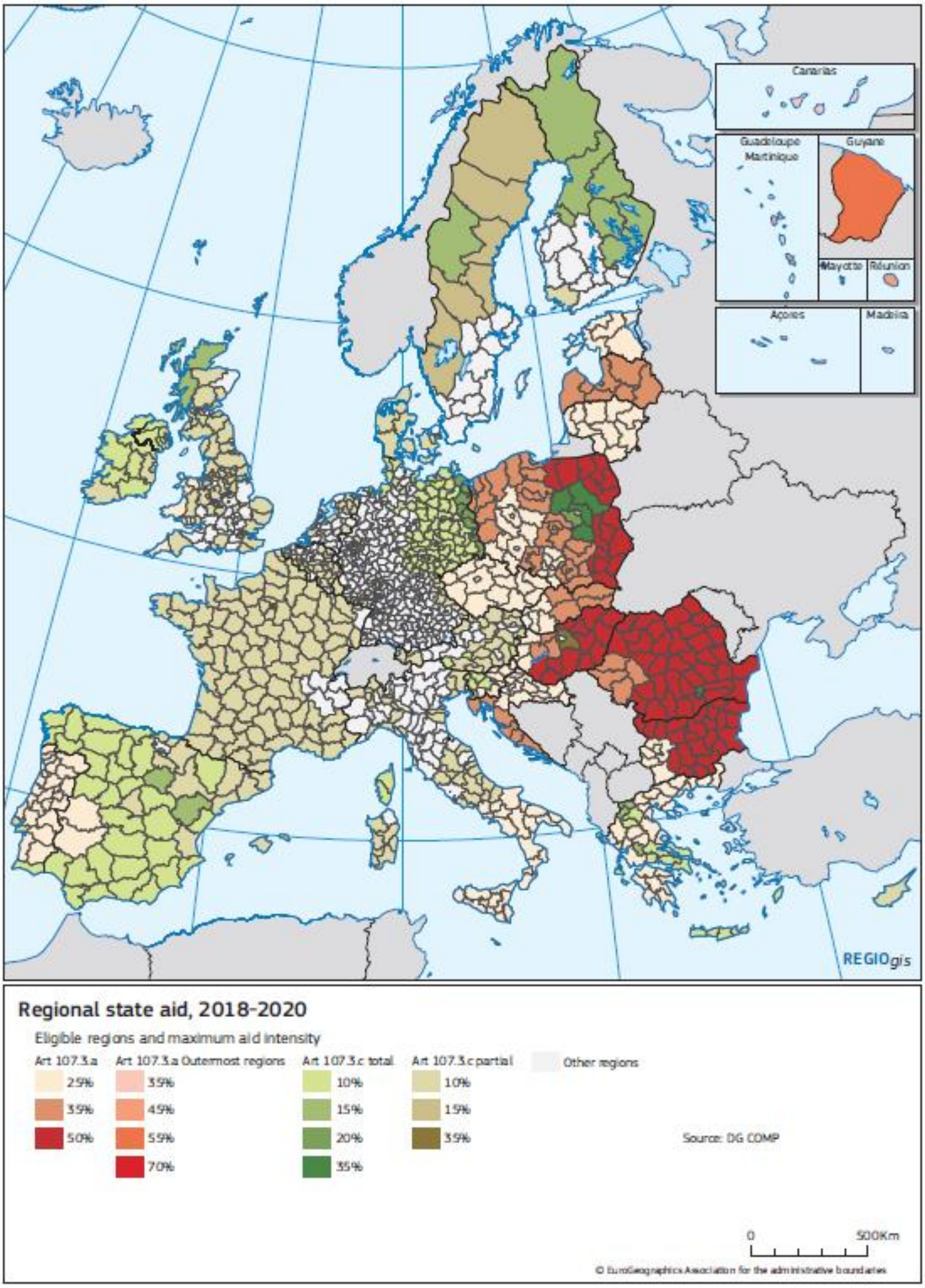
ANNEX II: ASSISTED AREA MAPS 2014-20

Regional aid ceilings 2014-17



Source: DG COMP.

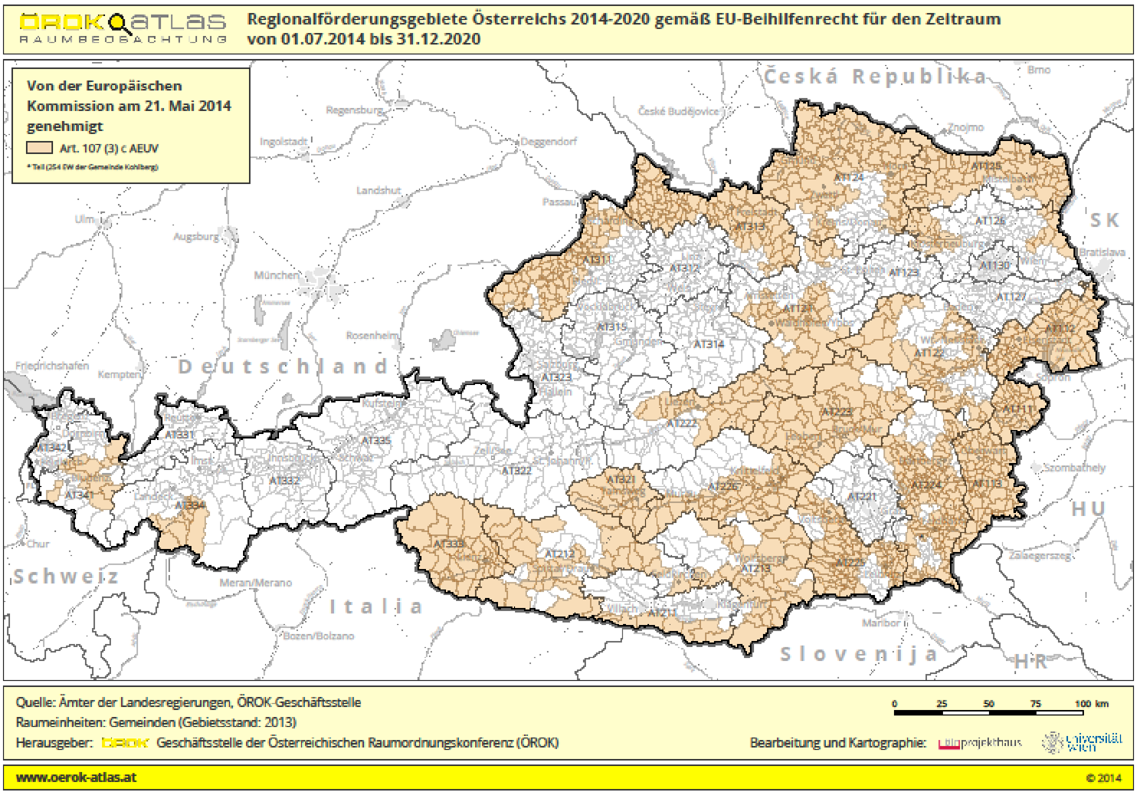
Regional aid ceilings 2018-20



Note: Subject to notifications and approvals following on from Commission Communication amending Annex I to the Guidelines on regional aid for 2014-20, OJEU C231/1 of 25 June 2016.
Source: DG COMP.

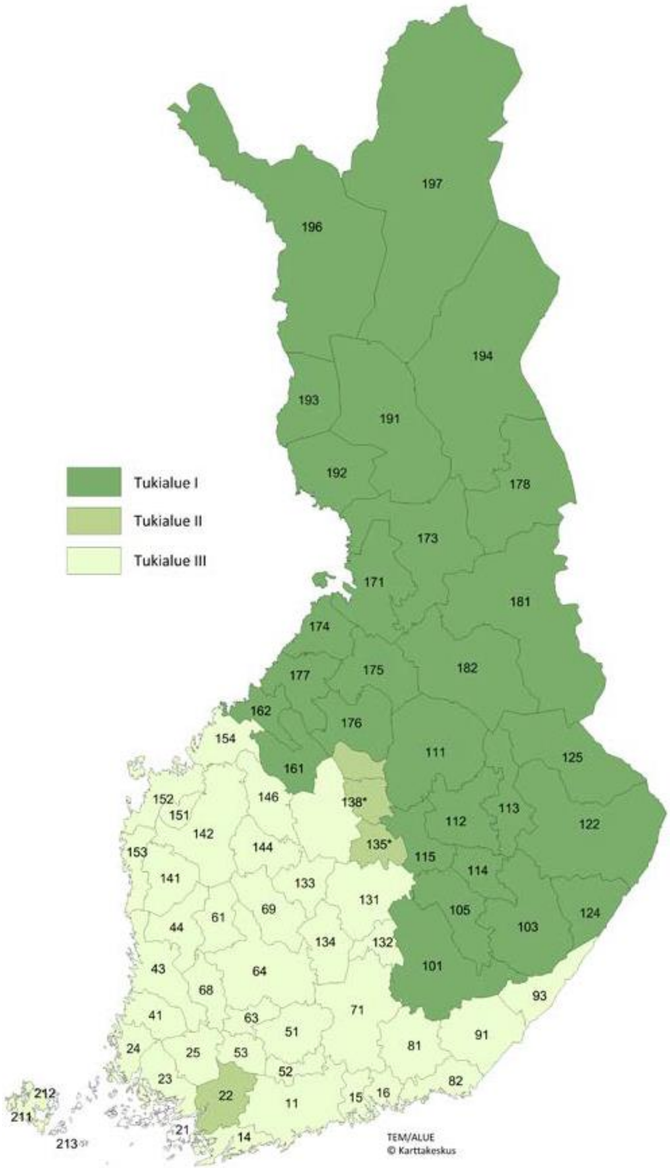
ANNEX III: NATIONAL ASSISTED AREA MAPS 2014-20

Assisted Areas in Austria 2014-20

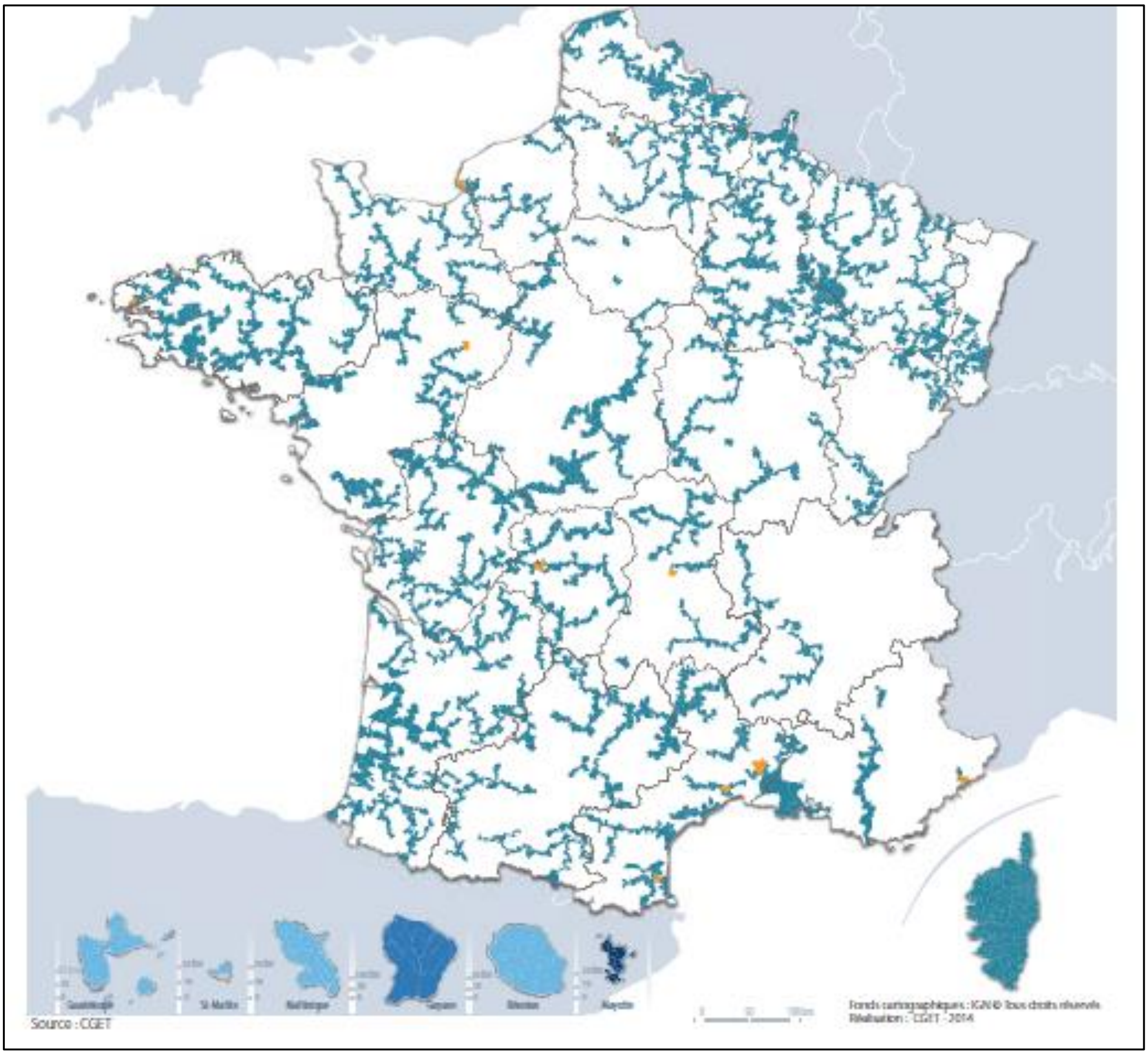


Assisted Areas in Finland 2014-20

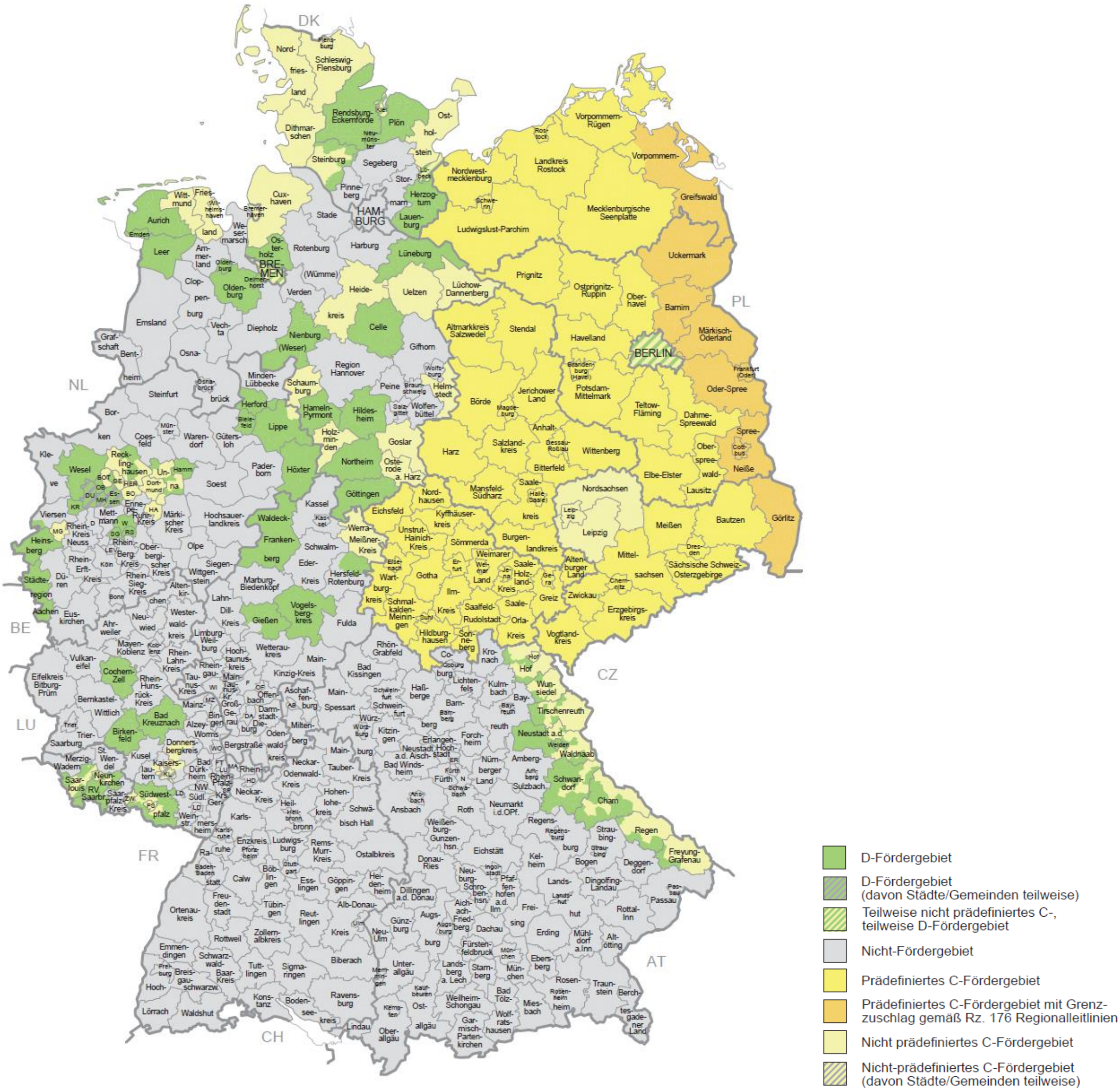
Aid Area 1	**Article 107(3)(c) predefined**
Central Ostrobothnia	
Kainuu	
Lapland	
Northern Karelia	
Northern Ostrobothnia	
Northern Savonia	
Southern Savonia	
Aid Area 2	**Article 107(3)(c) non-predefined**
Salo	
Äänekoski	
Viiitasaari	
Pihtipudas	



Assisted Areas in France 2014-20

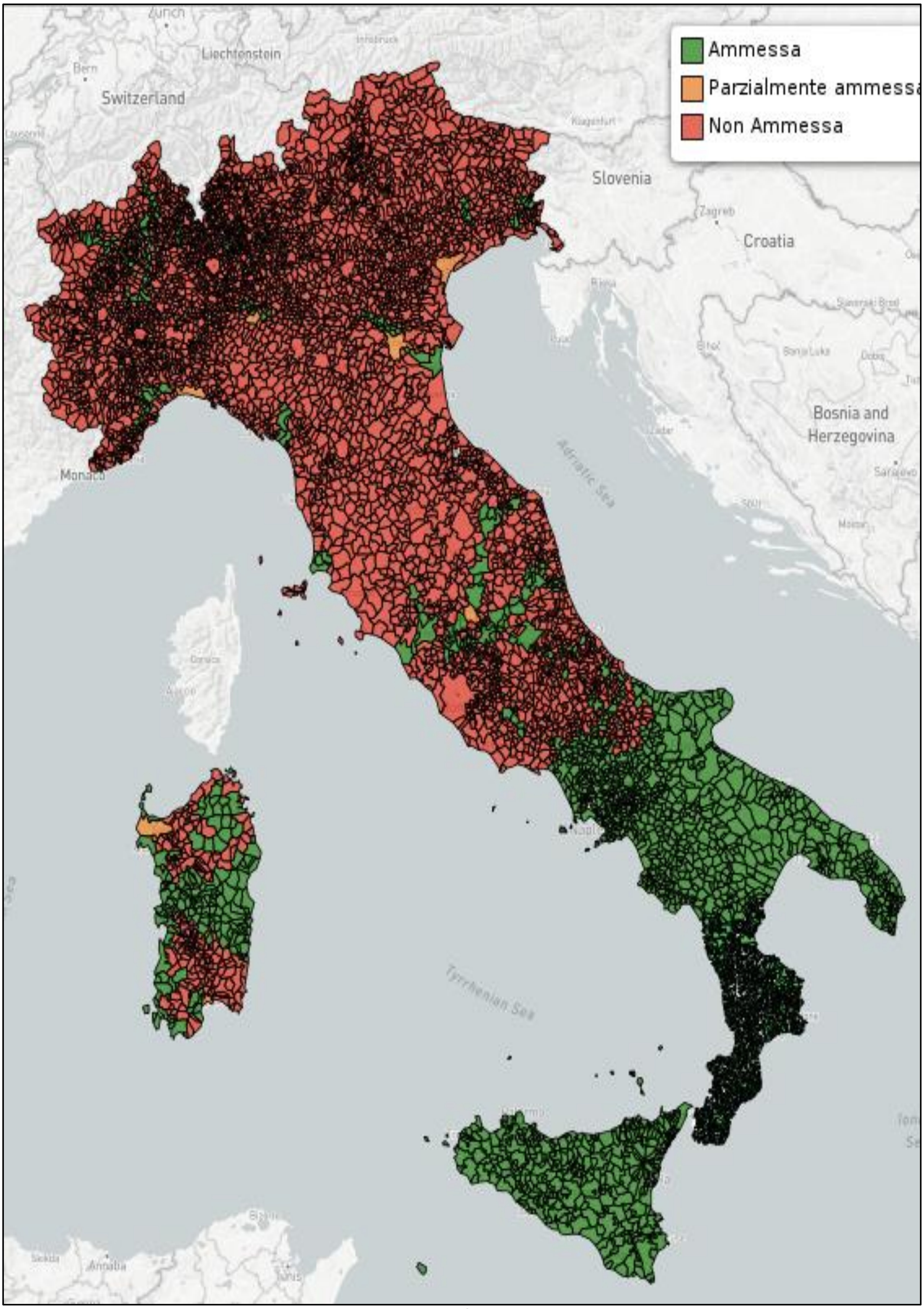


Assisted Areas in Germany 2014



Source: Federal Ministry for Economic Affairs and Energy

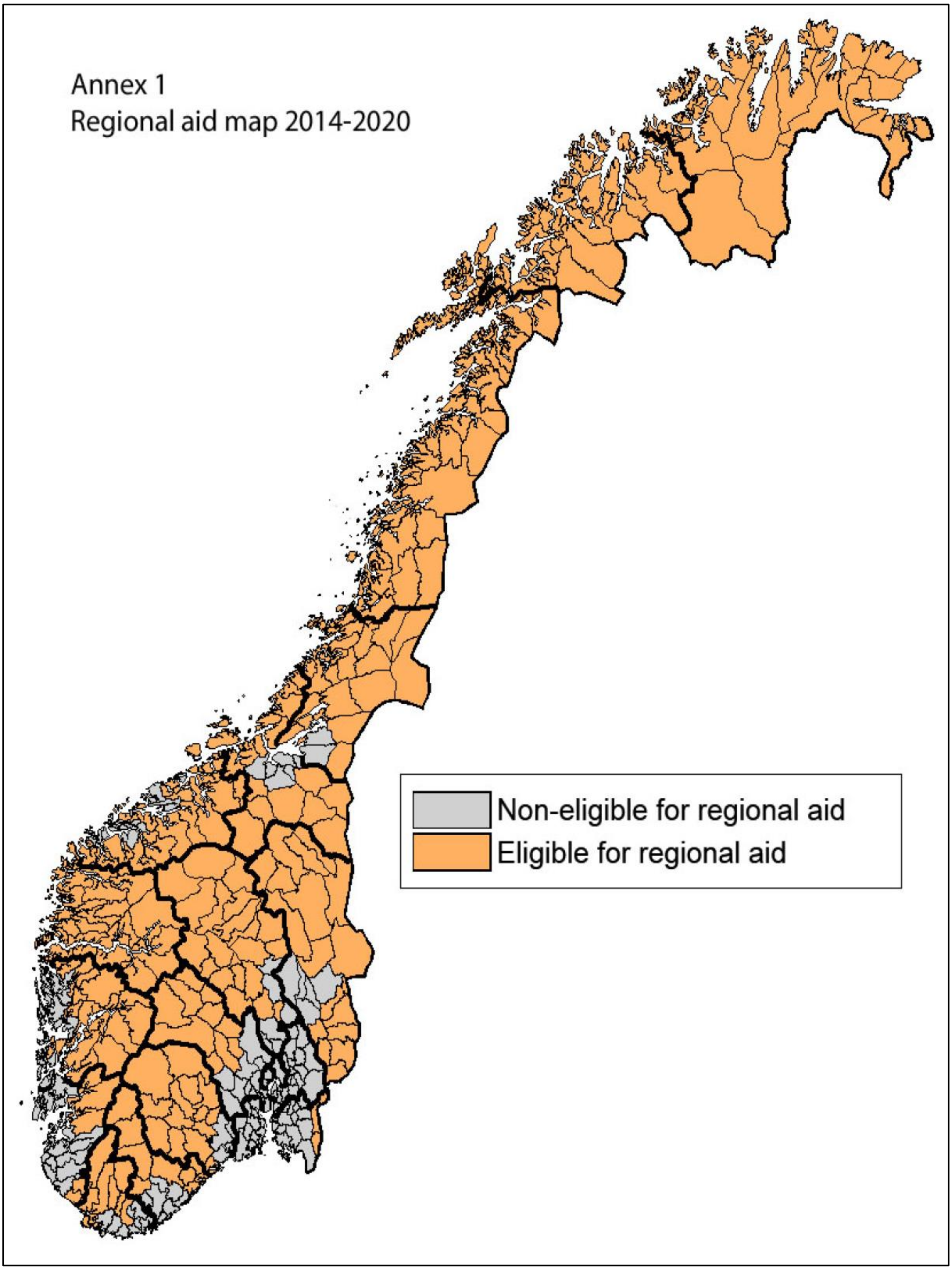
Assisted areas in Italy



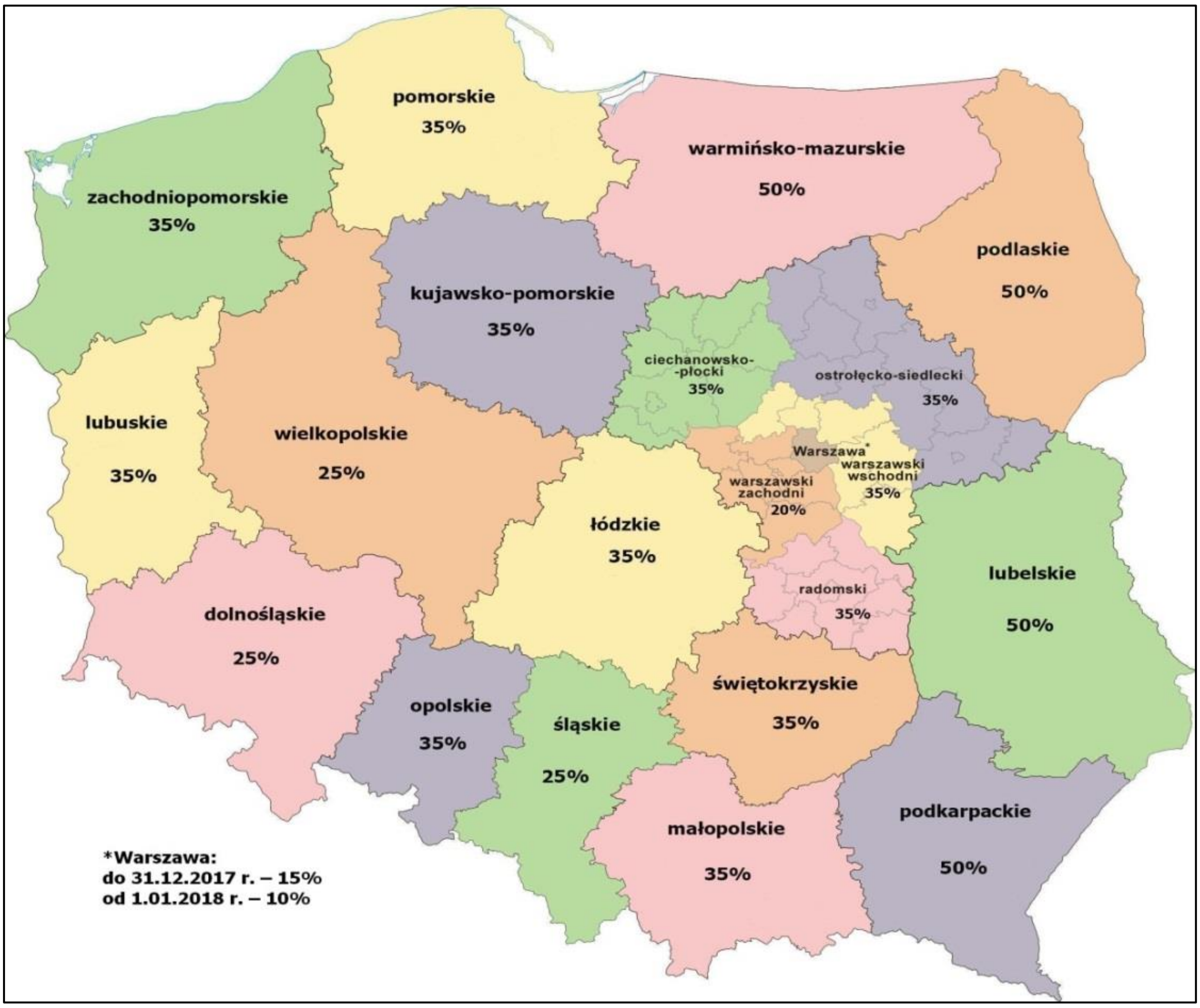
Note: The 2014-20 map does not show the 'upgrading' of Sardegna to 'a' region status – see Annex I.

Sources: http://www.aiutidistato.org/project/carta-degli-aiuti-di-stato-regionali-italia/

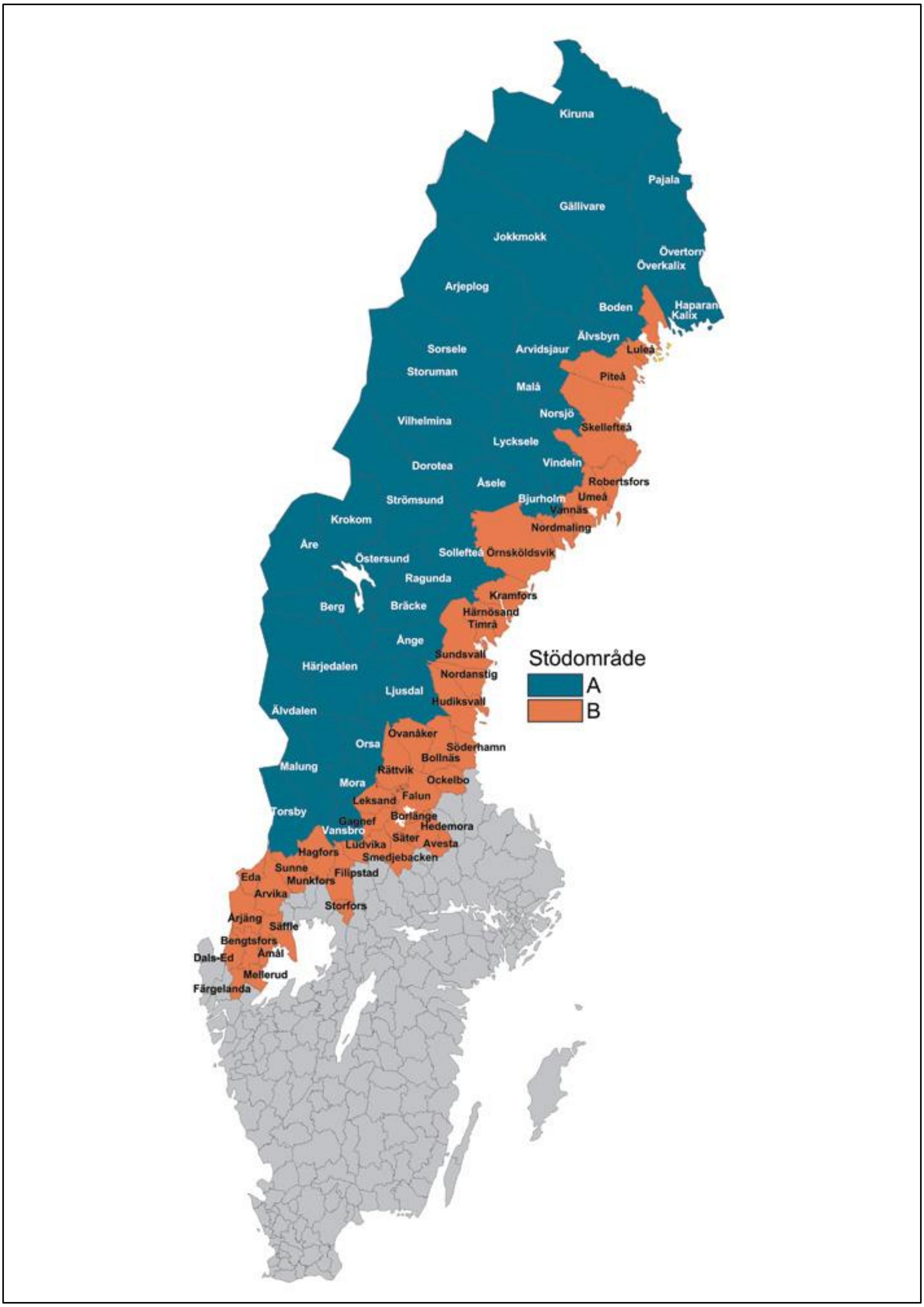
Assisted Areas in Norway 2014-20 (Investment Aid)



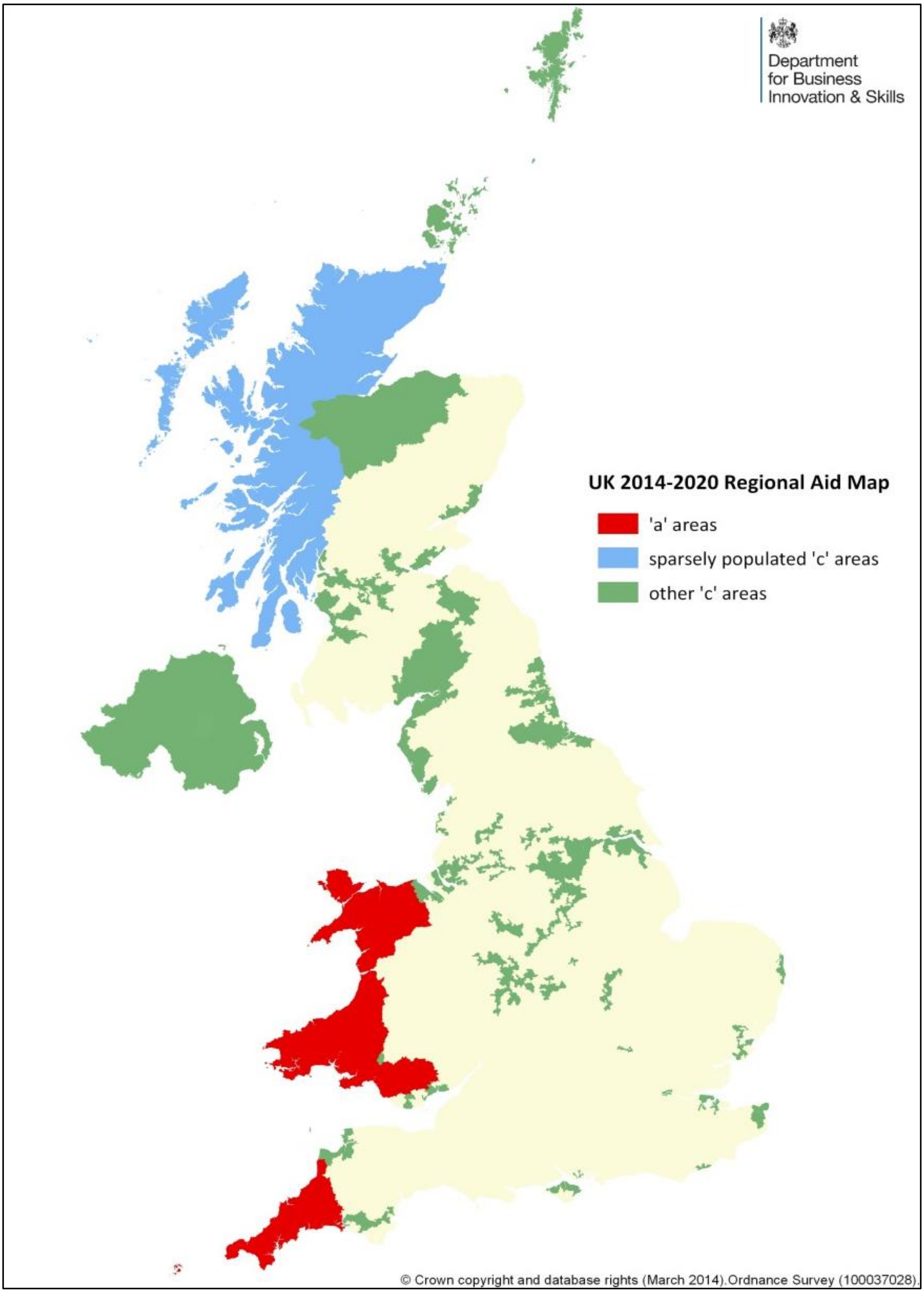
Assisted Areas in Poland 2014-20



Assisted Areas in Sweden 2014-20



Assisted Areas in the United Kingdom 2014-20



Note: the map does not show the 'upgrading' of Tees Valley and Durham to 'a' region status – see Annex I.

EoRPA Research

This paper has been written by Fiona Wishlade of the European Policies Research Centre (EPRC), initially drafted as a report produced for the EoRPA (European Regional Policy Research Consortium), which is a grouping of national government authorities from 12 European countries. The Consortium provides sponsorship for EPRC to undertake regular monitoring and comparative analysis of the regional policies of European countries and the inter-relationships with EU Cohesion and Competition policies. EoRPA members have comprised the following partners:

Austria
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Finland
- Työ- ja elinkeinoministeriö (Ministry of Employment and the Economy), Helsinki

France
- Commissariat Général à l'Egalité des territoires (General Commissariat for Territorial Equality, CGET, previously DATAR), Paris

Germany
- Bundesministerium für Wirtschaft und Energie (Federal Ministry for Economic Affairs and Energy), Berlin
- Ministerium für Wirtschaft, Wissenschaft und Digitalisierung (the Ministry for Economic Affairs, Science and Digitalisation), Saxony-Anhalt

Italy
- Agenzia per la Coesione Territoriale (Agency for Territorial Cohesion), Rome

Netherlands
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Norway
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Portugal
- Agência para o Desenvolvimento e Coesão (Agency for Development and Cohesion), Lisbon

Sweden
- Näringsdepartementet (Ministry of Enterprise and Innovation), Stockholm

Switzerland
- Staatssekretariat für Wirtschaft (SECO, State Secretariat for Economic Affairs), Bern

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