# OBSERVATIONS TO THE DRAFT GUIDELINES ON REGIONAL STATE AID FOR THE PERIOD 2014-2020

The present document contains some observations by the European Competition Lawyers Forum ("ECLF") on the "Paper of the services of DG Competition containing draft guidelines on regional State aid for 2014-2020" (the "Draft Guidelines") which has been published by DG COMP on its website.

The ECLF would like first of all to congratulate the services of DG COMP for their effort in the preparation and drafting of the Draft Guidelines. This document addresses clearly the need to rationalize scarce public resources and to focus regional State aid on more efficient and effective projects. In general terms, the Draft Guidelines contribute to a more consistent approach of State aid, in line with the objectives of the State aid modernization initiative.

However there are certain aspects of the Draft Guidelines which in our view deserve a further reflection by the services of DG COMP, as we explain in the following sections.

## 1. NOTIFIABLE AID

The ECLF welcomes the approach of the Draft Guidelines to provide for a consistent and unified approach - together with the General Block Exemption Regulation (GBER) - on the notificability of regional aid. In accordance with this approach, Member States should not notify regional aid provided they fulfill the conditions laid down in the GBER to be adopted by the Commission.

The Draft Guidelines establish that the following categories of aid will be subject to the notification obligation and therefore covered by the Draft Guidelines, in particular: (i) investment aid schemes targeted at specific sectors of economic activity; (ii) certain forms of operating aid schemes; (iii) individual or ad hoc aid the amount of which is above a notification threshold laid down in paragraph 16(r) of the Draft Guidelines; and (iv) any

investment aid linked to a closure of the same or a similar activity in another territory of the EEA regardless of the aid amount.

In this regard, it would be advisable to ensure that the future GBER reproduces also these criteria (in particular, the notification thresholds of paragraph 16(r)) in order to ensure that all the thresholds for notification are included in one single and consolidated text. This would contribute to delivering a simpler, clear and more effective framework.

As regards regional operating aid, the Draft Guidelines provide that this type of aid will normally be prohibited but that, exceptionally, the following categories of aid could be granted, subject to prior notification: (i) aid to reduce certain specific difficulties faced by small and medium enterprises (SMEs) in 'a' areas; (ii) aid to compensate for certain additional costs (other than transport costs) in the outermost regions; (iii) aid to prevent or reduce depopulation in areas with a very low population density.

In view of the current economic situation, it might be advisable for the Commission to introduce a greater degree of flexibility in its approach towards operating aid. This could be done, for instance, by

> introducing new categories of operating aid which could be considered compatible, subject to a notification obligation (for instance, operating aid granted to SMEs in areas with exceptionally high unemployment rate or in regions undergoing particularly acute industrial restructuring process).

## 2. AID TO LARGE ENTERPRISES

The Draft Guidelines limit the possibility of granting investment aid to large enterprises in 'a' areas (although aid to large enterprises will still be available in 'c' areas for aid geared towards specific objectives).

The rationale of this approach is that regional aid does not change the behaviour of large enterprises, as opposed to SMEs. Large enterprises would more often have made the investment even in the absence of the aid measure. Additionally, the Commission services argue that access to finance is more often a problem for SMEs than it is for large enterprises.

Support to the latter would therefore be ineffective and costly with high distortive effects for the internal market.

In our view, these arguments are not entirely convincing and would deserve a further reflection by the Commission. Moreover, the maintaining of regional aid to large enterprises in ‘c’ areas could lead to some negative undesired effects.

First of all, investment projects undertaken by large enterprises are a key driver for growth and employment. While it is true that in many cases a large enterprise would carry out the project even in the absence of the aid, this is not a principle that can be extended universally to any and all investment projects undertaken by large enterprises. When confronted with projects with an uncertain prospect of profitability, a large enterprise will in many occasions base its investment decision also on the availability and of the external financing that it can obtain.

Also, it is well known that large investment projects are those which really make the difference in terms of development, employment and growth in less developed regions. Such projects are usually carried out by large enterprises, and the availability of support by public authorities plays a fundamental role in their decision to undertake the project in a given region. On the contrary, SMEs tend to focus their investments in regions where infrastructure is already present and these projects have much less impact on the economy of the region.

Moreover, while it is true that in normal circumstances SMEs have more serious difficulties to access external financing,. in the current economic situation, credit restrictions affect all players in the market (also large enterprises), in particular in certain Member States. Many companies which do not meet the thresholds to be considered an SME have serious difficulties to expand their activity due to the existing difficulties to access financing at a reasonable cost. Indeed, as the Commission is aware of, credit restriction (which affects individuals and companies across all sectors) is one of the main reasons of stagnant (or recessive) demand in many Member States. In these circumstances, a limitation to the possibility of granting investment aid to large enterprises in all ‘c’ territories could be counterproductive.

Second, the Commission should also consider that the thresholds for a company to be considered SME are considerably restrictive[1]. Indeed, a company with a turnover of just EUR 55 million could already be considered a “large enterprise”. Likewise, in many sectors which are labour-intensive, the threshold of 250 employees can be easily exceeded. Accordingly, assuming as a matter of principle that there will be no incentive effects in these situations is, in our view, reductive, and could lead to the loss of investment projects that can be very valuable in the present economic circumstances.

Third, the thresholds to define SMEs do not take into account the financial situation of the company, which means that they are not necessarily fit to measure the ability of a company to undertake a new project or to access external financing. Consequently, if the Commission wishes to maintain the prohibition of aid to large enterprises in ‘c’ regions, it should at least consider lowering the threshold for a company to be considered an SME.

Fourth, another relevant factor is that incentive effect is already one of the tests that the Commission will necessarily have to consider when assessing the compatibility of the aid[2]. Consequently, there is no need to exclude a priori the aid to large enterprises precisely on grounds of the lack of incentive effects. If, as the Commission states, it is true that this effect is often absent in aid to large enterprises, then the projects in question will fail to pass the incentive effect test. But a prohibition of all aid to large enterprises in ‘c’ regions[3] will only lead to excluding a priori investment projects (and the growth and employment related thereto) which otherwise might pass this effects test.

Fifth, the reasoning applied by the Commission does not seem completely consistent. If investment aid to large enterprises in ‘c’ regions lacks incentive effect and is ineffective, there would be no reason to allow aid to large enterprises geared towards specific objectives.

Lastly, the Commission should reflect on the fact that a prohibition of investment aid for projects in “c” regions could lead to undesired side-effects such as the risk of de-location of investments from these areas towards “a" regions. In fact, even in cases where the large

[1] Commission recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises (OJ L 124, 20.5.2003, p. 36).

[2] Draft Guidelines, paragraph 3.4.

[3] With the exception of aid geared towards specific objectives.

company would have made the investment without the aid, the aid instrument may be a relevant factor for the company in deciding the area where to make the investment. This would be particularly unfortunate, since the objective of the cohesion and regional policies cannot be to foster investments in poorer regions at the expense of other underdeveloped areas.

## 3. ECONOMIC APPROACH

The Draft Guidelines propose[4] that when all the criteria for compatibility are met, the Commission should conduct a balancing test of the positive effects in terms of contribution to the development of the area against the identified potential distortions of competition and trade. The Draft Guidelines therefore propose to maintain the refined economic approach which has become a standard feature of the Commission's analysis of state aid cases since the mid 2000s.

While a sophisticated economic approach may indeed be helpful in some aspects, for instance in identifying real market failures, the widespread use of these instruments may also have some undesired consequences for the efficacy of the system as a whole.

The use of sophisticated instruments and the application of economic analysis to measure the balance test of the effects of State aid implies the use of methods which are, by definition, debatable and to a certain extent uncertain as regards their outcome. This may sometimes undermine the legal certainty required for investors to undertake certain investment projects. In fact, in many occasions, the uncertainty as to the results of a certain economic test may act as a disincentive for a company to participate in projects. Moreover, the type of analysis applied is in many instances intensive in terms of data and time. This may delay the whole analysis and approval process which is another deterrent element for private investors.

In certain projects, the ability to rule out any regulatory concerns is essential for a company to decide whether to participate in a certain investment project. The inability to foresee the result of the analysis by the Commission in borderline cases will lead to the loss of many projects.

[4] Draft Guidelines paragraph 29.

For these reasons, we support that the Commission limits the sophisticated economic approach to more problematic cases and where possible, base its assessment on the compatibility on more objective and predictable grounds.

## 4. OTHER ISSUES

### 4.1 Incentive effects

We have two relevant observations as regards the method proposed to demonstrate the incentive effect of the aid.

First of all, we have some hesitations as to whether certain formalistic requirements are appropriate to measure the existence of the incentive effect of the aid. For instance, the fact that the act awarding the aid is made conditional up on the Commission decision approving the aid is irrelevant for these purposes. What is really relevant is that the beneficiary was informed that the Commission should approve the aid and that the granting of the aid was effectively suspended until this approval takes place. This is even more the case if we consider that other documentary evidence is in any case required to be submitted to demonstrate the incentive effect[5]. If a company is indeed able to produce convincing evidence of the incentive effect, then the fact that the act awarding the aid is made conditional on the approval decision by the Commission should not be a relevant factor.

Second, the Draft Guidelines propose that in cases where the project works started prior to the decision to award the aid, "the whole project" will not be eligible for aid. We believe this approach to be somewhat rigid and difficult to justify. If the documentary evidence submitted by the company pursuant to paragraphs 64 and following of the Draft Guidelines demonstrate unambiguously that at least a severable part of the project (the works of which did not start prior to the decision granting the aid) would not be made without financial support, or that such part of the project would not be profitable without the aid, then the Commission should consider the possibility of accepting that part of the project as eligible.

[5] Paragraphs 64, 65, 67 - 71.

### 4.2 Zoning criteria

The criteria to define the assisted areas should also include unemployment rate, as this is one of the most critical problems that regions across all the EU are currently facing. Also, the possibility that the macroeconomic scenario changes in the mid-term should be taken into account. In this line, the following considerations are relevant:

(i) currently, unemployment rate is only considered as an optional factor for Member States to define 'c' regions. However, Article 107(3)(a) TFEU expressly allows the possibility to make use of this exception "*to promote the economic development of areas where the standard of living is abnormally low <u>or where there is serious underemployment</u>*". In this respect, we believe that considering only gross domestic product as a factor to define 'a' regions may not adequately reflect the specific circumstances of certain collectives or regions suffering of considerable acute underemployment problems. For this reason, and in view of the current economic situation, we invite the Commission to reflect on the possibility of considering abnormally high rates of underemployment in specific collectives (for instance for women or young workers) as a further factor to define 'a' regions;

(ii) the Commission might also consider the possibility of introducing a flexibility mechanism in the zoning criteria in case a substantial change in the macroeconomic scenario takes place in the EU or in certain Member States in the following seven years. This mechanism would be aimed at allowing a redefinition of certain 'a' and 'c' regions or at permitting the elimination of certain areas or the inclusion of new assisted regions in case the economic circumstances so require.

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