EPRC

EUROPEAN POLICIES RESEARCH CENTRE

University of Strathclyde Glasgow

The final frontier, or just another staging post? The 2014-20 Regional Aid Guidelines

EoRPA Paper 13/5

This paper was prepared for the 34th meeting of the EoRPA Regional Policy Research Consortium at Ross Priory, Loch Lomondside on 6-8 October 2013. It should not be quoted without permission

EUROPEAN REGIONAL POLICY RESEARCH CONSORTIUM

September 2013

European Policies Research Centre
School of Government & Public Policy
University of Strathclyde
40 George Street
Glasgow G1 1QE
United Kingdom

Tel: +44 (0) 141 548 3061
Fax: +44 (0) 141 548 4898

e-mail:fiona.wishlade@strath.ac.uk

Preface

This report has been prepared by the European Policies Research Centre (EPRC) under the aegis of EoRPA (European Regional Policy Research Consortium), which is a grouping of national government authorities from countries across Europe. 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. Over the past year, EoRPA members have comprised the following partners:

Austria
- Bundeskanzleramt (Federal Chancellery), Vienna

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

France
- Délégation à l'aménagement du territoire et à l'attractivité régionale (DATAR), Paris

Germany
- Bundesministerium für Wirtschaft und Technologie (Federal Ministry for the Economy and Technology), Berlin
- Ministerium für Wirtschaft, Bau und Tourismus, Mecklenburg-Vorpommern (Ministry for the Economy, Construction and Tourism, Mecklenburg-Western Pomerania), Schwerin

Italy
- Ministero dello Sviluppo Economico (Ministry of Economic Development), Dipartimento per lo sviluppo e la coesione economica (Department for Development and Economic Cohesion), Rome

Netherlands
- Ministerie van Economische Zaken (Ministry of Economic Affairs), The Hague

Norway
- Kommunal-Og Regionaldepartementet (Ministry of Local Government and Regional Development), Oslo

Poland
- Ministerstwo Rozwoju Regionalnego (Ministry of Regional Development), Warsaw

Sweden
- Näringsdepartementet (Ministry of Enterprise, Energy and Communications), Stockholm

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

United Kingdom
- Department for Business, Innovation and Skills, London
- The Scottish Government, Enterprise, Transport and Lifelong Learning Department, Glasgow

The research for this report was undertaken by EPRC in consultation with EoRPA partners. It involved a programme of desk research and fieldwork visits among national and regional authorities in sponsoring countries during the first half of 2013. The EoRPA research programme is coordinated by Professor John Bachtler, Fiona Wishlade, Dr Sara Davies and Stefan Kah.

This report was drafted by Fiona Wishlade. The report draws on country-specific research contributed by the following research team:

Austria: Stefan Kah, EPRC

Finland: Heidi Vironen, EPRC

France: Frederike Gross, EPRC

Germany: Dr Sara Davies, EPRC

Italy: Dr Laura Polverari, EPRC

Netherlands: Dr Arno Van der Zwet and Prof John Bachtler, EPRC

Norway: Fiona Wishlade, EPRC

Poland: Dr Martin Ferry, EPRC

Sweden: Heidi Vironen, EPRC

United Kingdom: Rona Michie and Dr Martin Ferry, EPRC

Many thanks are due to everyone who participated in the research. Thanks also to Lynn Ogilvie and Alyson Ross for coordination and secretarial support respectively. In addition, the European Policies Research Centre gratefully acknowledges the financial support provided by the members of the EoRPA Consortium.

Disclaimer

It should be noted that the content and conclusions of this paper do not necessarily represent the views of individual members of the EoRPA Consortium.

TABLE OF CONTENTS

Executive Summary

On 19 June 2013 the European Commission adopted Regional Aid Guidelines (RAG) for 2014-20 in anticipation of the expiry of the current (2007-13) RAG on 31 December 2013. RAG 2014-20 represents both continuity and change in relation to its predecessors.

The ***architecture*** of regional aid control is unchanged insofar as it comprises the RAG and the GBER is unchanged, but given the residual character of assessments under the RAG 2014-20, the precise scope of what needs to be notified must await the finalisation of the GBER. RAG 2014-20 incorporates the common 'assessment of compatibility' criteria and these apply to both notifiable schemes and notifiable individual aid. The overall ***spatial coverage*** of policy increases, but not all countries gain from the increase in coverage. There is a significant reduction in the coverage of 'a' regions. The basic distinction between 'a' regions and 'c' areas is retained, but the scope to aid large firms in 'c' areas is restricted. The ***selection of 'c' areas*** remains the responsibility of domestic authorities, subject to the population ceilings and designation criteria in the RAG, and approval of the map by the Commission. There are some detailed changes to the designation criteria and a more rigid approach to the use of population coverage. There is a crucial change in the treatment of ***investment aid to large firms***: large firms in 'c' areas are only eligible for aid in respect of 'initial investment in favour of new activity'; aid to large firms in 'a' regions is unaffected. For the most part, ***aid intensities*** are lowered. As under RAG 2007-13, very large awards must be notified, but a significant change is that there is no explicit trigger for the Commission to open a formal investigation. For large firms, notified aid must be the minimum needed, based on the 'net extra cost' approach. There are some significant new ***other provisions***. In particular, there is considerable emphasis on transparency and reporting, including information on final beneficiaries. Also, there is scope for the Commission to require an evaluation of a measure to be conducted as a condition of approving the scheme.

Against this background, preparations for the new assisted area maps are well underway in most EoRPA partner countries. Arrangements for area designation differ widely. In some countries the exercise is largely devolved or decentralised, while in others the task falls principally to national government ministries or is shared between different tiers of government. The approaches taken also diverge, partly reflecting institutional structures and responsibilities, but also the degree of flexibility afforded by RAG 2014-20 and the scope to reconcile domestic priorities with these constraints.

RAG 2014-20 is a significant milestone in the evolution of regional aid control and gives rise to a number of practical as well as more philosophical issues and questions.

i. Notwithstanding the adoption of the regional aid guidelines, the current period is characterised by a degree of flux and uncertainty.
ii. RAG 2014-20 reflects a pronounced shift in the theories of competitive harm prioritised by the Commission.
iii. It is difficult to justify greater discrimination between 'a' and 'c' areas.
iv. NUTS and NACE, which provide the foundation for defining 'initial investment in favour of a new activity' offer only a veneer of comparability.
v. The very pursuit of incentive effect may diminish the prospect of achieving it.

1. INTRODUCTION

The recent reform of the Regional Aid Guidelines has taken place against the backdrop of a complex mix of interrelated economic and policy change. The fallout from the crisis has affected national and regional economies differently, but almost everywhere the policy response is also conditioned by the climate of austerity, with some governments increasing intervention to boost the economy and others cutting back due to public expenditure constraints. At EU level, the flagship Europe 2020 initiative,[1] focussed on developing a 'smart sustainable inclusive' economy sets out a strategic approach to reigniting growth. Recent developments in the control of State aids – as in other policies, notably EU Cohesion policy - have been cast in terms of the Europe 2020 agenda. Accordingly, the *substantive* objective[2] of the State aid modernisation initiative (SAM)[3] is "to foster sustainable, smart and inclusive growth in a competitive internal market."

SAM is essentially a successor to the State aid action plan (SAAP).[4] SAAP had provided a so-called 'road map' for State aid reform over the 2005-9 period, with a *leitmotif* of 'less, but better aid'. SAAP was set in the context of the Lisbon agenda and the perception that the State aid rules did not facilitate the design and implementation of measures to support innovation. It also aimed to respond to criticism 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."[5] At the same time, the implications of enlargement and a perceived need to reduce the bureaucracy associated with 'routine' aid schemes culminated in the adoption of the General Block Exemption Regulation (GBER) covering a range of policy areas, including regional aid.[6] While SAAP succeeded in putting some order into the State aid rules, there was limited progress in simplification and disproportionate Commission resources are still spent scrutinising cases of limited practical significance. SAM ostensibly provides for a re-focussing of State aid control against the backdrop of Europe 2020, but what is also noteworthy 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'. The shift in emphasis signalled by SAM is carried through into the State aid reforms currently underway, and regional aid control is no exception.

The adoption of the 2014-20 Regional Aid Guidelines follows a lengthy period of consultation and negotiation dating back to autumn 2010 and involving other European institutions, the Member States and the wider stakeholder community. The tortuous evolution of RAG 2014-20 has been documented elsewhere and is not rehearsed here.[7] Instead, the aim of this paper is to provide an overview and

[1] European Commission (2010) Europe 2020: a strategy for smart, sustainable, inclusive growth, COM(2010) 2020 final, 3 March.
[2] There are three stated objectives. The other two are: to focus Commission *ex ante* scrutiny on cases with the biggest impact on the internal market while reinforcing Member State cooperation in enforcement; and to streamline the rules and provide for faster decision-making.
[3] European Commission (2012) EU State aid modernisation – SAM, COM(2012) 209 final, 8 May.
[4] European Commission (2005) State aid action plan, COM(2005) 107 final, 7 June.
[5] 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.
[6] Commission Regulation (EC) No 800/2008 of 6 August 2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty [now Article 107 and 108], OJ 2008 L214/3.
[7] Wishlade, F. (2013) Draft Regional Aid Guidelines 2014-20 – Revised Data and Insights from the EP debate, EPRC Policy Briefing, April 2013, rev1: http://www.eprc.strath.ac.uk/news/Policy_Briefing_Apr_2013.pdf; Wishlade, F (2013) Draft Regional aid guidelines 2014-20: what are the proposals and how might they affect

assessment of the key provisions of RAG 2014-20 and the changes they entail, together with a review of the steps being taken in the EoRPA partner countries to adapt to the new regulatory framework, particularly regarding the revisions to the assisted area maps.

The remainder of this paper is structured as follows. Section 2 reviews the main changes introduced under RAG 2014-20. Section 3 provides a preliminary overview of Member State progress in devising assisted area maps. Last, Section 4 reflects on some of the key trends and issues arising from the reform as a basis for discussion.

regional policies in the Member States? EPRC Policy Briefing, March 2013: http://www.eprc.strath.ac.uk/news/Policy_Briefing_Mar_2013.pdf; Wishlade, F. (2012) 'Non-Paper: Non-Starter or Non-Negotiable? EU Competition Policy and Regional Aid Control Post-2013', European Policy Research Papers, No 83, University of Strathclyde: http://www.eprc.strath.ac.uk/eprc/documents/PDF_files/EPRP_83.pdf

2. REGIONAL AID GUIDELINES 2014-20

On 19 June 2013 the European Commission adopted Regional Aid Guidelines (RAG) for 2014-20[8] in anticipation of the expiry of the current (2007-13) RAG[9] on 31 December 2013. RAG 2014-20 represents both continuity and change in relation to its predecessors. This section considers the key features of RAG 2014-20 with respect to the overall **architecture** of regional aid control, **spatial coverage,** the parameters governing the **selection of 'c' areas**, the **treatment of investment aid to large firms**, the new maximum **aid intensities** and **other provisions**, notably those relating to *transparency* and *evaluation*.

2.1 The architecture of regional aid control

2.1.1 RAG 2014-20 and the new GBER

As with RAG 2007-13, RAG 2014-20 fulfils two main functions: first, it sets out the parameters for the regional aid maps and associated aid values; second, it sets out the criteria for assessing measures that are not exempted under the GBER and are therefore subject to notification.

At present, most regional aid measures fall within either the Regional Block Exemption Regulation or the General Block Exemption Regulation (GBER),[10] which superseded it. Like RAG 2007-13, the GBER was also set to expire on 31 December 2013. On 8 May 2013, the Commission published a Draft GBER for consultation.[11] The scope of notification will not be clear until the 2014-20 GBER is adopted; this is not now expected until spring 2014.

RAG 2014-20 extends RAG 2007-13 to 30 June 2014,[12] but it requires Member States to notify extensions of existing maps and notified aid schemes in order to take advantage of the prolongation of RAG 2007-13.[13] Extension of the regional aid maps also enables block-exempted schemes to benefit from the adjustment period of the GBER.[14] Both RAG 2014-20 and GBER 2014-20 are due to enter into force on 1 July 2014.

RAG 2014-20 sets out detailed provisions on the scope of aid that may be approved. Like RAG 2007-13, RAG 2014-20 excludes the possibility of regional aid to steel and synthetic fibres[15] and to firms in difficulty,[16] and does not apply where specific sectoral provisions are made under the Treaty.[17] RAG 2014-20 will not apply to airports or to the energy sector, which will be dealt with under specific

[8] Guidelines on regional State aid for 2014-20 [2013] OJ C209/1 (hereafter 'RAG 2014-20').

[9] Guidelines on National Regional Aid for 2007-13 [2006] OJ C54/13 (hereafter 'RAG 2007-13').

[10] Regulation (EC) 800/2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty [2008] OJ L214/3, hereafter, GBER.

[11] http://ec.europa.eu/competition/consultations/2013_gber/index_en.html

[12] RAG 2014-20, para 186.

[13] RAG 2014-20, para 187.

[14] The GBER includes an adjustment period for schemes, except regional aids, to remain compatible for 6 months – see GBER, Article 44(3). This currently appears to exclude the possibility of introducing new aid schemes between 31 December 2013 and 30 June 2014. An amendment to Article 45 of the GBER will address this: http://ec.europa.eu/competition/consultations/2013_second_gber/gber_prolongation_regulation_en.pdf

[15] RAG 2014-20, para 9.

[16] RAG 2014-20, para 18.

[17] Notably fisheries and aquaculture, agriculture and transport – RAG 2014-20, para 10.

guidelines.[18] On the other hand, regional aid can be used for the development of broadband networks, provided that the criteria under the Broadband Aid Guidelines are met, as well as research infrastructure, on condition that access to this infrastructure is transparent and non-discriminatory.[19] Aid to shipbuilding falls within the scope of RAG 2014-20,[20] following the expiry of sector-specific rules at the end of 2013.[21]

As now, most measures will be covered by the GBER so will not require notification. However, given the residual scope of the RAG,[22] the precise contours of those measures requiring notification – i.e. those *not* meeting the exemption criteria of the GBER – will only be known once the GBER is adopted. Nevertheless, some indications of the potential scope of notification can be gleaned from the Draft GBER and the RAG.

It can be expected that various types of aid *scheme* will be subject to notification. For instance:

- The Draft GBER does not extend to schemes where the planned expenditure exceeds 0.01 percent of national GDP and an annual budget of €100 million; on this basis, schemes with large budgets would be subject to scrutiny under RAG 2014-20.[23] If implemented, this would be the first time that compatibility of an aid scheme has been explicitly linked to the budget allocated.
- The Draft GBER extends the block exemption to cover certain types of operating aid which have been routinely approved under RAG 2007-13 for Outermost and sparsely populated regions.[24] However, not all operating aid schemes will fall within the GBER and those excluded will be assessed under RAG 2014-20.[25] As now, however, operating aid is generally prohibited and subject to specific conditions.
- Schemes with a sectoral focus[26] (including 'general' regional aid schemes under which shipbuilding is an eligible activity) will be subject to notification.[27]

Regarding *individual* aid, the Draft GBER specifically consults on whether *ad hoc* aid should be notified,[28] while RAG 2014-20 specifies three types of measure that *will* require notification and an assessment of compatibility on the basis of RAG 2014-20. These are: [29]

- Individual investment aid above the notification thresholds. This is unchanged from the RAG 2007-13 on large investment projects and concerns proposed aid amounts which exceed that for which a €100 million investment would qualify.
- Individual investment aid potentially linked to a closure of a similar activity in the EEA. This is new and is designed to address 'subsidy shopping' on the part of firms or poaching by inward

[18] RAG 2014-20, para 11.
[19] RAG 2014-20, para 12-13.
[20] RAG 2014-20, footnote 9.
[21] Framework on State Aid to Shipbuilding [2011] OJ C364/9.
[22] RAG 2014-20, para 21.
[23] Draft GBER, Article 1(2)(a).
[24] Draft GBER, Article 16.
[25] Draft GBER, Article 14(1)(c).
[26] With some exceptions eg tourism and agricultural products, which are not considered sectorally targeted.
[27] Draft GBER, Article 14(1)(a) and (b).
[28] Draft GBER, Article 15(1).
[29] RAG 2014-20, para 23-4.

investment agencies. It applies where the beneficiary has closed down a similar productive activity in the EEA in the two years preceding the award, or plans to do so in the two years after the investment is completed.

- Individual aid for large firms for diversification of existing activities in ‘c’ areas. This is a major change which severely curtails the use of aid to support expansion projects in ‘c’ areas. The Commission had originally sought to outlaw all general investment aid to large firms in ‘c’ areas; this was contested by a large number of affected Member States. The compromise is that aid to large firms in ‘c’ areas is eligible if it involves ‘initial investment in favour of new economic activity’. This is basically defined as (i) the setting-up of a *new* establishment (‘greenfield’ projects); or (ii) the *diversification* of the activity of an existing establishment, provided that the new activity is not the same or similar to existing activities.[30] The first of these falls within the Draft GBER; the second requires notification.

2.1.2 Compatibility assessment

It can be anticipated that, as under RAG 2007-13, the vast majority of schemes will fall under the GBER. While the GBER is set to be widened in some respects, in others it may be more restrictive. At the same time, the assessment criteria under the RAG are toughened and tightened, creating a disincentive for policymakers to notify, and arguably contributing further to the homogenisation of aid policy.

The State aid modernisation initiative (SAM)[31] called for ’common principles’ for the compatibility of State aid with the Treaty. Reflecting this, aid is compatible only if it meets specified criteria.[32] The approach is consistent with the ‘balancing test’ in other areas of State aid and the Commission Guidance on aid to large investments (LIPS guidance)[33] applicable under RAG 2007-13, though the ‘balancing’ is less explicit than in the LIPS guidance which it effectively replaces. In considering a notified measure, the Commission essentially seeks to analyse whether the positive impact of the measure in addressing an objective of common interest outweighs its potential negative effects on trade and competition. In doing so, the Commission will consider a range of criteria.

The way in which these criteria are applied varies according to whether the notified measures are individual aids, investment aid schemes or operating aids. All must be met for the measure to be considered compatible under the balancing test:

a) **Contribution to a well-defined objective of common interest:[34]** investment aid schemes should form part of a regional development strategy (such as an EU Cohesion policy Operational Programme); individual aid may be justified on the basis of a variety of indicators (such as job creation, training, clustering effects, knowledge spillovers); Member States must demonstrate the existence of specific difficulties.

[30] RAG 2014-20, para 20(i)(a) – the takeover of an existing establishment is also eligible, but also on condition that the activity is not the same or similar.

[31] European Commission (2012) EU State aid modernisation – SAM, COM(2012) 209 final, 8 May.

[32] RAG 2014-20, para 26.

[33] Communication from the Commission concerning the criteria for an in-depth assessment of regional aid to large investment projects [2009] OJ C 223/3.

[34] RAG 2014-20, para 30-46.

b) Need for state intervention:[35] it is sufficient that projects are located within the assisted area map, this being a reflection of the fact that the market is not delivering the Cohesion objective.

c) Appropriateness:[36] a notified aid measure will not be considered compatible if less distortive instruments or aid types can achieve the same positive contribution to regional development. The onus is on Member States to demonstrate the appropriateness of the aid proposed, including a consideration of forms of aid considered to be less distortive.

d) Incentive effect:[37] aid is only compatible if it alters the behaviour of the beneficiary. Member States must use a standard application form and applicants must explain what would have happened in the absence of aid; large firms must provide documentary evidence in support of the counterfactual described. Aid will be considered to have an incentive effect if it results in additional activity that the beneficiary would not carry out without aid or would do so on a smaller scale or in a different location. For notifiable individual aid, incentive effect can be proven in two possible scenarios: (i) the investment would not take place at all without the aid (investment decision); or (ii) the investment would not take place in that location without aid (location decision).

e) Proportionality:[38] Member States must ensure that aid is limited to the minimum needed. For notified aid schemes available to large firms and individual aid to large firms this is based on the 'net extra cost approach' – meaning that aid must be limited to the additional cost of the project in the area concerned, compared to the counterfactual, in the absence of aid. For SMEs, the aid ceilings specified in RAG 2014-20 offer a 'safe harbour'.

f) Avoidance of undue negative effects on competition and trade:[39] the negative effects on trade and competition must be limited and outweighed by the contribution to the objective of common interest. Nevertheless, the RAG outlines three instances where the negative effects 'manifestly' outweigh the positive impact and notified individual aid cannot be found compatible: (i) where the project creates capacity in a market that is in structural decline; (ii) where, without the aid, the project would have located in a region where the aid maximum is the same or higher and (iii) where there is a link between aid and relocation.

g) Transparency:[40] Member States must publish on a single website the text of notified measures and specified information on beneficiaries.

2.2 Spatial coverage

The distinction between 'a' regions and 'c' areas is maintained, but the differentiation is heightened by the fact that aid to large firms in the 'c' areas is only compatible in respect of 'initial investment in favour of new economic activity'; this is discussed further below.

The initial population ceiling set in RAG 2014-20 is 46.53 percent of the EU27 population (equivalent to 47 percent of the EU28 population – i.e. following the accession of Croatia).[41] This is higher in absolute terms than the RAG 2007-13 initial ceiling (42 percent of EU25), and leads to higher final coverage once all the adjustments (safety net, minimum coverage, etc.) are made (see Table 1).

[35] RAG 2014-20, para 47-49.
[36] RAG 2014-20, para 50-59.
[37] RAG 2014-20, para 60-76.
[38] RAG 2014-20, para 77-111.
[39] RAG 2014-20, para 122-140.
[40] RAG 2014-20, para 141.
[41] RAG 2014-20, para 148.

Table 1: Assisted area coverage 2014-20

	'a' regions	'c' areas	*Of which, ex-'a'*	*Sparsely-popd*	*Non-predefd 'c'*	Total
EU28	25.82	21.85	*6.74*	*0.58*	*14.53*	**47.67**
EU27	25.17	22.04	*6.80*	*0.58*	*14.66*	**47.21**
BE	0.00	29.95	*12.06*		*17.89*	**29.95**
BG	100.00					**100.00**
CZ	88.10					**88.10**
DK		7.97			*7.97*	**7.97**
DE		25.85	*11.9*		*13.95*	**25.85**
EE	100.00					**100.00**
IE		51.28			*51.28*	**51.28**
EL	45.91	54.09	*10.08*	*0.17*	*43.84*	**100.00**
ES	6.90	61.76	*28.25*	*0.51*	*33.00*	**68.66**
FR	2.93	21.24			*21.24*	**24.17**
IT	29.04	5.03			*5.03*	**34.07**
CY		50.00			*50.00*	**50.00**
LV	100.00					**100.00**
LT	100.00					**100.00**
LU		8.00			*8*	**8.00**
HU	70.38	6.33			*6.33*	**76.71**
MT		100.00	*100*			**100.00**
NL		7.50			*7.5*	**7.50**
AT		25.87			*25.87*	**25.87**
PL	86.30	13.70	*13.7*			**100.00**
PT	69.25	15.77			*15.77*	**85.02**
RO	89.44	10.56	*10.56*			**100.00**
SI	52.92	47.08	*47.08*			**100.00**
SK	88.48					**88.48**
FI		26.10		*24.25*	*1.85*	**26.10**
SE		12.26		*12.26*		**12.26**
UK	3.91	23.14		*0.35*	*22.79*	**27.05**
HR	100.00					**100.00**
IS				*36.6/100?*		**36.6/100?**
NO				*25.6*		**25.6**

Note: As mentioned beow, the change in definition of sparsely-populated regions could, apparently, result in Iceland being designated in its entirety; the lower figure corresponds to the definition based on NUTS 3, as now.
Source: RAG 2014-20, Annex I and EPRC calculations for Iceland and Norway.

The basic definition of Article 107(3)(a) regions[42] - ***'a' regions*** - as NUTS 2 regions with GDP(PPS) per head below 75 percent of the EU average is unchanged,[43] but eligibility is determined with reference to EU27, rather than EU25. In addition, and irrespective of their level of GDP per head, the Outermost regions (OMR) referred to in Article 349 TFEU also retain 'a' status.

The coverage of Article 107(3)(c) areas - ***'c' areas*** - comprises two elements that are now referred to as 'predefined' areas and 'non-predefined' areas.[44] This is broadly as now, but importantly the resulting population cannot be transferred to other areas – ie. it must be used to designate areas that fulfil the predefined criteria.[45]

[42] RAG 2014-20, para 150.

[43] Based on Eurostat data for 2008-10.

[44] RAG 2014-20, para 155.

[45] RAG 2014-20, para 159.

There are two categories of ***predefined 'c' area***, as now: (i) regions with 'a' status in 2011-13 that are now over the 75 percent threshold;[46] and (ii) sparsely populated areas.[47]

Former 'a' regions cover almost 7 percent of the EU population, and a very significant proportion of some countries (see Table 1). The statistical effect category in RAG 2007-13 is not retained.[48]

Sparsely-populated areas are defined as: NUTS 2 regions with fewer than 8 inhabitants per km^2 or NUTS 3 regions with fewer than 12.5 inhabitants per km^2.[49] This differs from the RAG 2007-13 definition, which refers only to the NUTS 3 based element of the definition.[50] This change does not alter the outcomes for Sweden or Norway.[51] However, it is significant for Finland since it results in the inclusion of a single NUTS 2 region as a predefined area, although the component NUTS 3 areas do not all meet the 12.5 inhabitants per km^2 threshold (so the coverage of the sparsely-populated areas is higher than it would otherwise be). Also noteworthy, it would appear that this change could result in the inclusion of Iceland in its entirety since Iceland constitutes a single NUTS 2 region, with population density of 3.2 per km^2.[52]

As now, the population of ***non-predefined 'c' areas*** is calculated by subtracting the 'a' regions and the predefined 'c' areas from the initial ceiling. The population is distributed between countries on the basis of both national *and* EU disparities in GDP per head and unemployment rate.[53] There are significant detailed changes to the methodology for the distribution of the population compared to RAG 2007-13 and 2000-6,[54] which both followed the same approach. For some countries the new method has a significant impact, as reflected in

A series of further ***adjustments*** is made to 'c' area coverage. A 'safety net' applies so that no Member State loses more than 50 percent of existing coverage[55] (as in RAG 2007-13); Cyprus and Luxembourg benefit from this. Each Member State has minimum coverage of 7.5 percent of the population.[56] This is a new provision, but finds a precedent in RAG 2000-6 which set a floor of 15 percent of coverage. The Netherlands benefits from this. Last, special provisions are made for Member States subject to various 'bailout' mechanisms, such that those countries affected do not see a reduction in coverage.[57] Greece, Cyprus and Portugal benefit from this.

The actual selection of 'c' areas continues to be undertaken by domestic authorities, based on parameters set in RAG 2014-20;[58] these criteria are discussed below.

[46] RAG 2014-20, para 158(a).

[47] RAG 2014-20, para 158(b).

[48] RAG 2007-13, para 18-20.

[49] Based on Eurostat population density data for 2010.

[50] RAG 2007-13, para 26, footnote 29 and para 30(b).

[51] Coverage is reduced but this is because of higher population density in Aust Agder county, not because of the change in definition.

[52] Importantly, however, the EFTA Surveillance authority, which is responsible for State aid control in Iceland and Norway, has not yet published any information on the application of RAG 2014-20 to the non-EU EEA countries.

[53] RAG 2014-20, Annex II; the 2007-13 approach is principally based on national disparities.

[54] Guidelines on national regional aid [1998] OJ C74/9 (RAG 2000-6)

[55] RAG 2014-20, para 165(b).

[56] RAG 2014-20, para 165(c).

[57] RAG 2014-20, para 163.

[58] RAG 2014-20, para 167-170.

The Commission will review coverage of the 'a' regions in 2016 to establish whether the list of such regions should be extended (there is no implication that it would be reduced); this would entail changes to 'c' area coverage in the countries concerned.[59]

illustrates the impact of RAG 2014-20 on spatial coverage. At the EU level, the most striking point to note is that, while overall coverage increases by around one percentage point, there is a pronounced shift in the *composition* of this coverage – with 'a' region coverage falling from around 33 percent to some 25 percent of the EU27 population and 'c' areas rising from under 14 percent to over 22 percent.

At country level, patterns of change vary widely. In *relative* terms, the biggest 'loser' is Luxembourg, where coverage is halved. In *absolute* terms, the biggest loser is Hungary, which loses over 23 percent of existing coverage (down from 100 percent to under 77 percent). Finland and Sweden each lose around 20 percent of current coverage. Germany will see a reduction of almost four percentage points, but also significant is that no German region will have 'a' status from July 2014. In Denmark and Italy there are more modest reductions in coverage.

Some countries will see no change in overall coverage: Bulgaria and the three Baltic states retain 100 percent 'a' region coverage; and Malta has 100 percent coverage, but with 'c' area rather than 'a' region status. Overall coverage is also unchanged in Poland, Romania and Slovenia but the capital regions now have 'c' area rather than 'a' region status. In the Czech Republic and Slovakia coverage is essentially unchanged; the differences shown in

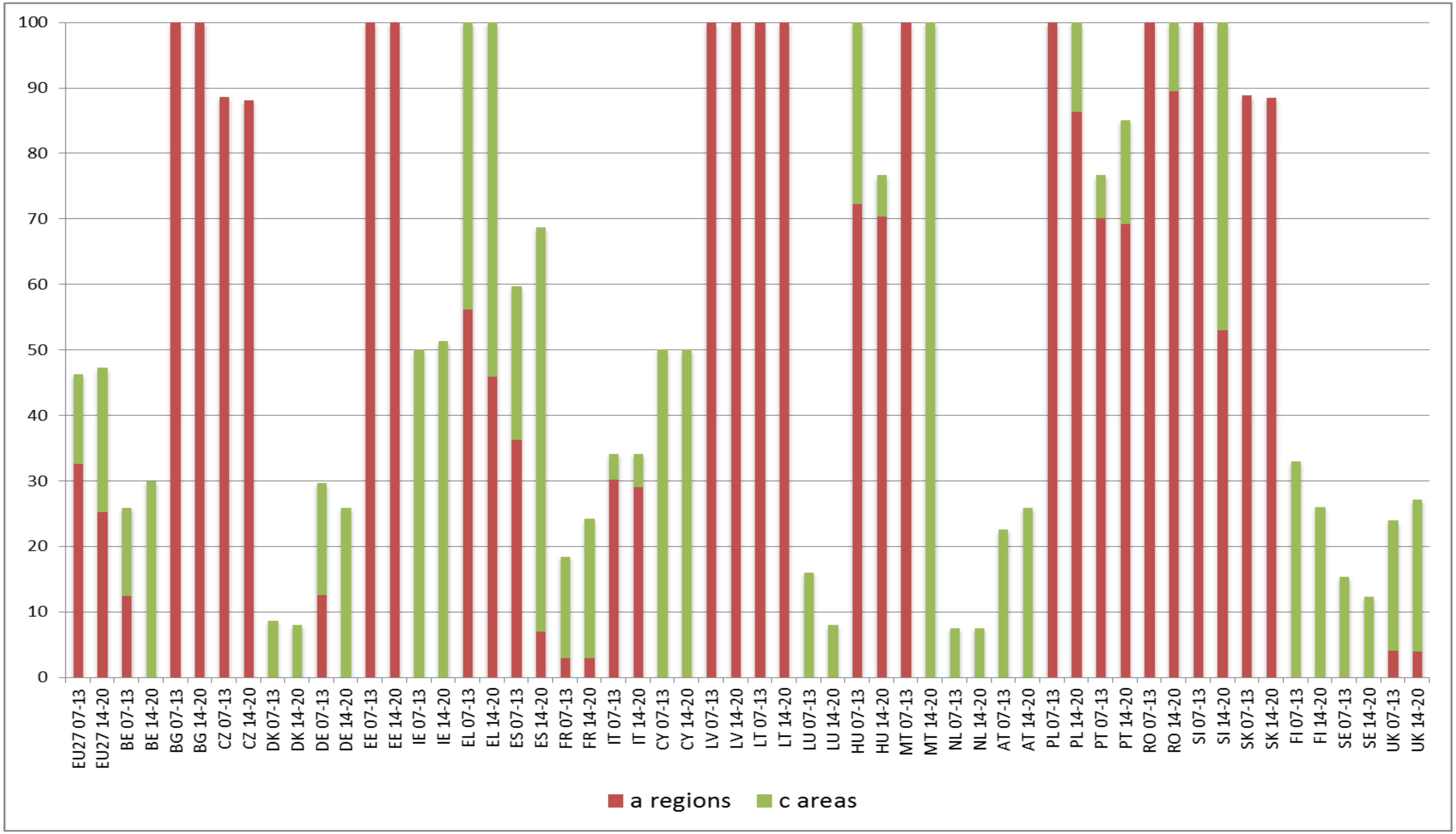
are the result of demographic change. Greece and Cyprus benefit from the special provisions for countries in receipt of 'bail out' mechanisms and retain coverage at existing levels. Coverage remains unchanged in the Netherlands which relies on the minimum 7.5 percent coverage, (the same as current coverage). Coverage of Croatia is not mentioned in RAG 2014-20 but, on the basis of the relevant GDP data, would qualify as an 'a' region in its entirety.

At the opposite end of the spectrum, the biggest 'winner' in *relative* terms is France, which sees an increase in existing coverage of over 30 percent. In *absolute* terms, the main gains are in Portugal and Spain – where coverage increases by 8.3 and 9 percentage points respectively. Austria, Belgium and the United Kingdom see coverage increase by around three to four percentage points, and there would be more modest gains in Ireland.

Though it is striking that some of the more prosperous Member States see an increase in coverage, it should also be recalled that RAG 2014-20 is much more restrictive in its treatment of large firms in 'c' areas than in 'a' regions. As such, the 'c' area maps may, in practice, serve mainly to determine eligibility for greenfield investment and those areas in which the SME 'bonus' applies.

[59] RAG 2014-20, para 183-185.

Figure 1: Population coverage 2007-13 and 2014-20 (% of total)



Note: 2007-13 figures in fact relate to 2011-13, i.e. following the 2010 review when Statistical effect areas were re-designated as 'full' 'a' regions or 'c' areas.
Source: RAG 2007-13, RAG 2014-20 and own calculations from Eurostat data,

2.3 The selection of eligible areas

Under RAG 2014-20, as under RAG 2007-13, ‘a’ region coverage is predetermined by the Commission. An important change under RAG 2014-20 is that the population allocation determined by the predefined areas former ‘a’ areas (broadly analogous to the economic development areas in RAG 2007-13) may only be used to designate those areas.[60] In the current period, some countries (for example the United Kingdom and Italy) used this population to designate areas other than in the qualifying regions; this is no longer possible. [61]

There is slightly more flexibility in the designation of sparsely-populated areas (as under RAG 2007-13). Whilst in principle these should concern NUTS 2 regions with fewer than 8 inhabitants per km^2[62] or NUTS 3 areas with fewer than 12.5 inhabitants per km^2, parts of adjacent NUTS 3 areas may also be designated, provided that those parts also have population density below the 12.5 inhabitant per km^2 threshold.

Proposals for the designation of the non-predefined areas are the responsibility of domestic authorities, subject to the parameters set out in RAG 2014-20[63] and Commission approval of the resulting map. The parameters set by the Commission concern both designation criteria and geographical units of analysis – ‘building blocks’.

2.3.1 Area designation criteria for investment aid (non-predefined ‘c’ areas)

The key *designation criteria* are set out in Figure 2. At first sight this appears as a rather complex matrix of options. In practice, however, the criteria are similar to those for RAG 2007-13: in general, areas must have GDP(PPS) below the EU average or an unemployment rate 15 percent higher than the national average. It is probable that the vast majority of non-predefined ‘c’ areas will be designated on the basis of Criterion 1,[64] as in 2007-13. The key differences between RAG 2014-20 and its predecessor are that there is now greater flexibility on minimum population coverage for countries with relatively low coverage and that the ‘structural change’ criterion, which requires a minimum population of 50,000 cannot be used to designate areas that could qualify under Criterion 1, or Criterion 2. Also, the capacity to target very localised problems for areas with a minimum coverage of 20,000 through support for SMEs has been dropped. While the minimum population criteria show more flexibility, at least for some countries, as will be seen below, the building block requirements introduce new constraints.

[60] RAG 2014-20, para 159.

[61] Though Member States could opt not to include all the predefined areas in the proposed map; the corresponding population quota would however, be ‘lost’.

[62] As noted earlier, the reference to NUTS 2 areas as the basis for predefined sparsely-populated areas is new, but the flexibility to designate parts of NUTS 3 areas is not.

[63] RAG 2014-20, para 168-70.

[64] Equivalent to RAG 2007-13, para 30(c).

Figure 2: Key area designation criteria for non-predefined 'c' areas

<table>
<tr><th>Criterion</th><th>Conditions</th><th>Minimum population</th></tr>
<tr><td>1. Contiguous areas</td><td>Within NUTS 2 or NUTS 3 regions with either:
• GDP(PPS) per head ≤ EU27 or
• Unemployment rate ≥ 115% of national average</td><td>• General case: 100,000
• For MS with 'c' coverage <1million: 50,000
• For MS with national pop <1million: 10,000</td></tr>
<tr><td>2. NUTS 3 regions with pop < 100,000</td><td>• GDP(PPS) per head ≤ EU27 or
• Unemployment rate ≥ 115% of national average</td><td>Not applicable</td></tr>
<tr><td>3. Islands and other contiguous areas characterised by geographical isolation</td><td>• GDP(PPS) per head ≤ EU27 or
• Unemployment rate ≥ 115% of national average or
• <5000 population</td><td>None</td></tr>
<tr><td>4. Border areas</td><td>• Contiguous areas
• NUTS 3 or parts of
• Adjacent to 'a' region, or
• Land border with non-EEA country</td><td>None</td></tr>
<tr><td>5. Structural change or serious decline</td><td>• Must not be within areas that fulfil criteria 1-4 above
• Contiguous areas</td><td>• General case: 50,000
• For MS with 'c' coverage <1million: 25,000
• For MS with national pop <1million: 10,000
• Isolated areas (cf criterion 3): 5,000</td></tr>
</table>

Source: Summarised from RAG 2014-20, para 168.

The national populations and the coverage of non-predefined 'c areas are given in Figure 3. This suggests that only Cyprus and Luxembourg qualify for the 10,000 population minimum under Criteria 1 and 5; and that Denmark, Hungary, Portugal and Finland qualify for the 50,000 and 25,000 population minima under Criteria 1 and 5 respectively.

Figure 3: Non-predefined 'c' areas and national population

	Non predefined 'c' population(' 000s)	National population (000s)
DK	460	5546
DE	11774	81766
IE	2386	4475
EL	4959	11312
ES	14670	46074
FR	14086	64823
IT	2873	60477
CY	415	831
LU	41	508
HU	658	9994
NL	1245	16603
AT	2258	8392
PT	793	10639
FI	103	5362
UK	14027	62257

Source: Eurostat and EPRC calculations from RAG 2014-20.

2.3.2 Building blocks for investment aid (non-predefined 'c' areas)

The geographic unit of analysis – or building block - is specified as local administrative unit 2 (LAU2) – see Figure 4.[65]

Figure 4: Geographical units – EU definitions

	NUTS 2		NUTS 3		LAU 1		LAU 2	
BE	Provincies / Provinces	11	Arrondissementen / Arrondissements	44	-		Gemeenten / Communes	589
DK	Regioner	5	Landsdeler	11	Kommuner	99	Sogne	2143
DE	Regierungs-bezirke	38	Kreise	412	Verwaltungsge-meinschaften	1481	Gemeinden	12066
IE	Regions	2	Regional Authority Regions	8	Counties, Cities	34	Electoral Districts	3441
ES	Comunidades y ciudades Autonomas	19	Provincias + islas + Ceuta, Melilla	59	-		Municipios	8116
FR	Régions + DOM	26	Départements + DOM	100	Cantons de rattachement	3785	Communes	36680
IT	Regioni	21	Provincie	110	-		Comuni	8094
CY	-	1	-	1	Επαρχίες (Eparchies)	6	Dimoi, koinotites	615
LU	-	1	-	1	Cantons	13	Communes	116
HU	Tervezési-statisztikai régiók	7	Megyék + Budapest	20	Statisztikai kistérségek	174	Települések	3154
NL	Provincies	12	COROP regio's	40	-		Gemeenten	418
AT	Bundesländer	9	Gruppen von politischen Bezirken	35	-		Gemeinden	2357
PT	Comissaoes de Coordenaçao regional + Regioes auto.	7	Grupos de Con-celhos	30	Concelhos - Munícipios	308	Freguesias	4260
FI	Suuralueet / Storområden	5	Maakunnat / Landskap	19	Seutukunnat / Ekonomiska regioner	70	Kunnat / Kommuner	336
SE	Riksområden	8	Län	21	-		Kommuner	290
UK	Counties (some grouped); Inner and Outer London; Groups of unitary authorities	37	Upper tier authorities or groups of lower tier authorities (unitary authorities or districts)	139	Lower tier auths individual unitary auths; Individual unitary auths or LECs (or parts); Districts	380	Wards (or parts thereof)	10310

Source: Eurostat

An important issue is the notion of 'contiguity', which is an explicit requirement of Criteria 1 and 3-5, and implicit in Criterion 2. The notion of contiguous areas refers to whole LAU2 areas or to a group of whole LAU2 areas. A group of LAU2 areas is considered to be contiguous if each of those areas in the group shares an administrative border with another area in the group. However, *parts* of LAU2 may be designated, provided that the population is at least 50 percent of the minimum population required under the criterion applicable. Under Criterion 1, for example, in the general case, this appears designed to preclude the inclusion of an area comprising a population of 150,000 of which 120,000 in one LAU2 and the remaining 30,000 in parts of adjoining LAU2. In contrast with the provisions on population minima outlined in Figure 2, this 'anti leopard skin' clause represents a significant tightening of existing provisions. For 2007-13 a number of countries designated areas on

[65] RAG 2014-20, para 169.

the basis of units below LAU2, and while these maps were accepted, it is also known that such approaches were not always considered by the Commission to be 'within the spirit' of RAG 2007-13.

2.3.3 Assisted areas for operating aid

It is important to note that the above discussion relates to area designation for investment aid. In practice, this will account for the vast majority of aid schemes. However, RAG 2014-20 also alludes to the possibility of operating aid being compatible:

> …."if it aims to reduce certain specific difficulties faced by SMEs in particularly disadvantaged areas falling within the scope of Article 107(3)(a) of the Treaty, or to compensate for additional costs to pursue an economic activity in an outermost region or to prevent or reduce depopulation in very sparsely populated areas".[66]

Apart from the Outermost regions, which are defined in the TFEU, the targeting of operating aid schemes would be determined on the basis of separate maps from that for investment aid; it is not linked to the population ceilings. RAG 2014-20 makes specific reference to the eligibility of 'very sparsely populated' regions for operating aid. These are defined as

> "NUTS 2 regions with less than 8 inhabitants per km^2 or parts of such NUTS 2 regions designated by the Member States concerned in accordance with paragraph 162 of these guidelines"[67]

The basic definition is unchanged from RAG 2007-13.[68] However, there would appear to be a typographical error regarding flexibility in this provision since paragraph 162 is not really relevant to the coverage of sparsely-populated areas. It may be that the reference is intended to be to paragraph 161, which would entail a material change to the definition of very sparsely populated areas that has not been signalled elsewhere in the reform discussions.

2.4 Investment aid for large firms

The treatment of investment aid to large firms in 'c' areas has been a major issue since DG Competition first floated proposals for RAG reform in its 2011 'non-paper'.[69] These proposals involved a complete ban on aid to large firms in the 'c' areas. This was arguably the most contentious aspect of the reform proposals and two joint letters to Commissioner Almunia attracted support from the majority of countries with a least some 'c' area coverage. In addition, the Commission's initial proposals were the subject of intensive bilateral lobbying from a number of quarters.

The RAG and the Draft GBER pull back from the complete ban on investment aid to large firms in 'c' areas, but nonetheless impose some very significant constraints on aiding such investment, reflecting the Commission's concern to focus aid on cases where it is perceived to have an incentive effect. However, it would appear that some further 'dovetailing' of the two documents is required.

[66] RAG 2014-20, para 16.

[67] RAG 2014-20, para 20(y).

[68] RAG 2007-13, para 80.

[69] This has never been published, but see: Wishlade, F. (2012) 'Non-Paper: Non-Starter or Non-Negotiable? EU Competition Policy and Regional Aid Control Post-2013', European Policy Research Papers, No 83, University of Strathclyde: http://www.eprc.strath.ac.uk/eprc/documents/PDF_files/EPRP_83.pdf

Under the Draft GBER, 'aid to large enterprises shall only be granted for "initial investment in favour of new activity", within the meaning of this Regulation, in the area concerned'.[70] In the Draft GBER this is defined as either (i) setting up a new establishment in a different NUTS 3 region from any existing operations of the firm; or (ii) diversifying the activity of an establishment to one that is 'not the same or similar' to that previously performed.[71] The 'same or similar activity' means one falling within the same four-digit NACE code of economic activities.[72] Broadly, this appears to mean that in order to escape notification, aid to large firms must either involve a new investment in a different region or a different activity in the same region.

Under RAG 2014-20, regional aid for large undertakings in 'c' areas may only be granted for 'initial investments that create new economic activities' or 'for the diversification of existing establishments into new products or new process innovations.'[73] Initial investment in new economic activity is defined as related to: (i) the setting-up of a new establishment; or (ii) the diversification of the activity of an establishment, under the condition that the new activity is not the same or a similar activity to the activity previously performed in the establishment.[74] However, while the Draft GBER exempts from notification aid for the 'diversification of the activity of an establishment', RAG 2014-20 explicitly requires the notification of aid 'to diversify an existing establishment in a 'c' area into new products'.[75] In short, is there a lack of clarity surrounding the notions of 'activity' and 'product' and whether the two are in fact interchangeable. Nevertheless, it would appear that RAG 2014-20 tightens the Draft GBER proposals by requiring the notification of aid to investments by large firms, other than those involving new establishments. On the other hand, the scope of potentially-compatible aid to large firms in 'c' areas is apparently widened to include 'new process innovations'. New process innovations are not defined in RAG 2014-20, though it does specify that eligible costs 'for a fundamental change in the production process', must exceed the depreciation of the assets linked to the activity to be modernised in the course of the preceding three years.[76]

As matters stand, it seems that any proposal for aid to large firms in 'c' areas to invest in *existing* establishments (whether changing products or processes) will require notification and approval on the basis of the RAG 2014-20.

2.5 Award values

2.5.1 Rates of award

RAG 2014-20 reduces aid intensities across the board, except for the very poorest regions and the sparsely-populated areas. The main maximum aid intensities are shown in Figure 5 along with rates under RAG 2007-13 (Figure 6). Note, however, that the rate 'bands' are adjusted to reflect enlargement to EU27, so direct comparisons cannot be made.

[70] Draft GBER, Article 15(4).
[71] Draft GBER, Annex I, para 34.
[72] Draft GBER, Annex I, para 35.
[73] RAG, para 15.
[74] 'Same or similar activity' is defined as in the Draft GBER.
[75] RAG 2014-20, para 24.
[76] RAG 2014-20, para 96.

Figure 5: RAG 2014-20 Maximum aid intensities ('standard' matrix) gross grant-equivalent

	Large firms	Medium-sized firms	Small firms
'a' regions GDP per head <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: As discussed in 2.4 above, aid to large firms in 'c' areas is restricted to certain types of investment, so that in practice a zero rate will often apply. Rates for OMRs and other specific cases are omitted.
Source: RAG 2014-20, para 171-177.

Figure 6: RAG 2007-13 Maximum aid intensities ('standard' matrix) gross grat-equivalent

	Large firms	Medium-sized firms	Small firms
'a' regions GDP per head <45% EU25 av	50%	60%	70%
'a' regions GDP per head <60% EU25 av	40%	50%	60%
'a' regions GDP per head <75% EU25 av	30%	40%	50%
'c' areas – sparsely populated/border	15%	25%	35%
'c' areas	15%/10%	25%/20%	35%/30%

Note: Rates for OMRs and other specific cases are omitted.
Source: RAG 2007-13, para 44-48.

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 in Figure 5 (as adjusted by Figure 7 if required) act as a cap on the minimum necessary. For SME aid under notified schemes, the rates in Figure 5 act as 'safe harbours' – at or below these levels, the proportionality criterion is deemed to be fulfilled.

2.5.2 Aid to large investments

As under RAG 2007-13, regional aid for large investments, defined as projects with eligible expenditure exceeding €50m, is subject to an adjusted aid amount. This is set out in Figure 7; SME bonuses do not apply to large investment projects irrespective of firm size.

Figure 7: Adjusted aid amounts for eligible investment exceeding €50m

Eligible expenditure	Aid ceiling
Up to €50 m	100% of applicable aid ceiling
For the part between €50m and €100m	50% of applicable aid ceiling
For the part exceeding €100m	34% of applicable aid ceiling

Source: RAG 2014-20, para 20(a).

Also as under RAG 2007-13, proposed aid must be notified for prior approval if it exceeds the adjusted aid amount which an eligible investment of €100m could obtain; this corresponds to the notification thresholds set out in Figure 8.

Figure 8: Notification thresholds expressed as amounts of aid against prevailing aid ceilings

Prevailing ceiling	**10%**	**15%**	**25%**	**35%**	**50%**
Notification threshold	€7.5m	€11.25m	€18.75m	€26.25m	€37.5

Source: RAG 2014-20, para 20(n).

These provisions (the adjusted ceilings and the notification thresholds) are unchanged. However, the RAG 2007-13 market share and production capacity 'screens'[77] beyond which aid is subject to a formal investment are dropped in RAG 2014-20. These screens concerned beneficiaries that had, or would have had, more than 25 percent market share of the product concerned or projects which resulted in an increase in capacity of more than 5 percent (except in rapidly expanding markets). By end 2012, 39 individual cases had been notified. In ten of these the Commission had proceeded to an Article 108(2) investigation.[78] The decision to abolish the screens partly reflects the implications of the *Smurfit Kappa* judgment,[79] but also doubts about the effectiveness and utility of the screens.[80] As a result, from 1 July 2014, *all* notified aids are subject to the compatibility assessment set out in RAG 2014-20, and there is no explicit trigger for the opening of a formal investigation. Although this affects relatively few cases, the scale of the aid concerned is significant and it reflects an important underlying shift in philosophy. It remains to be seen what impact this will have on the likelihood of notification by domestic authorities and on the workload of DG Competition, particularly in the context of the exclusion from the GBER of aid to diversification projects undertaken by large firms.

2.6 Other new developments in RAG 2014-20

2.6.1 Relations between regional aid control and EU cohesion policy

Since the 1988 reform of the Structural Funds relations between Cohesion policy and Competition control of regional aid have often been strained. Historically, this has been particularly so in context of assisted area coverage, and the lack of coincidence between the EU Cohesion policy and national assisted area maps. However, this has been less controversial since 2000, when Member States gained greater flexibility in choosing both sets of areas, and especially since 2007, when Cohesion policy ceased to be spatially restricted. In this context, the interface between Cohesion policy and the GBER is now of more relevance than relations with the RAG. Nevertheless, it is interesting to note a greater degree of coordination between RAG 2014-20 and the objectives of Cohesion policy. This is reflected in the explicit use of Cohesion policy criteria in State aid compatibility assessments and in the specific provisions made for territorial cooperation.

[77] RAG 2007-13, para 68.

[78] In practice, most of these investigations were opened because the Commission had doubts about whether the screens were exceeded.

[79] In this case, the Court found that the Commission is not precluded from opening the formal procedure if the market share or capacity criteria are not exceeded and that, by inferring that the aid complied with the guidelines because the market screens were not exceeded without assessing the importance of the project for regional development, the Commission had both misconstrued the scope of the guidelines and failed to exercise its discretion – see Case T-304/08 *Smurfit Kappa v Commission* (judgment of 10 July 2012)

[80] Kai-Uwe Kühn (2012) *Making State Aid Rules More Effective: the Reform of the Regional Aid Guidelines,* 10th annual Experts' forum on European State Aid Law, Brussels, 7 June; Friederiszick, H. and Tosini, N. (2013) *Implications of the State aid Modernisation for the Assessment of Large Investment Projects,* European State Aid Law Quarterly, 1, pp. 46-60.

Regarding the *contribution to a common objective*, schemes implemented within the context of Cohesion policy programmes are deemed to meet this criterion, whereas for purely national or regional measures Member States must demonstrate how they contribute to a regional development strategy[81] and schemes must include selection criteria that are in line with that strategy. In other words, there is a presumption of compatibility for Cohesion policy based measures that is not extended to domestic regimes. Similarly, where a scheme is introduced outwith a Cohesion policy programme, Member States must indicate why regional aid is an *appropriate instrument* and why, where applicable, a sectoral focus might be justified.[82] By contrast, for aid schemes implementing Cohesion policy programmes, the instrument proposed is considered to be appropriate without the need for further justification.

The Draft GBER makes specific provision to accommodate investments in Cohesion policy European Territorial Cooperation projects. This enables the participation of firms in cooperation projects with the higher rate of award to apply for an entire project where the major part of the project takes place in a higher rate area. This represents a clear attempt to address an issue that has hitherto proved an obstacle to the implementation of some territorial cooperation programmes. The standard RAG 2014-20 restrictions on aid to large firms in ‘c’ areas still apply.

Notwithstanding these modest elements of *rapprochement,* the implementation of State aid measures in the 2014-20 Operational Programmes may, in practice, be stalled by delays in adopting the new GBER and new substantive rules such as those relating to risk capital, which are also under preparation, especially given the emphasis on financial instruments in Cohesion policy post-2013.

2.6.2 Transparency

As mentioned above, transparency obligations are included in the common assessment criteria for notified aid.[83] These include online publication of the full text of the aid scheme, its implementing provisions and award data, notably names of beneficiaries, aid amounts and intensities. In principle, Member States are already required to provide online information on aid *schemes* approved under the GBER, though in practice the links to such information are often poorly maintained and the information limited in detail; it remains to be seen whether and how this requirement will be enforced under RAG 2014-20 and the new GBER. Reporting is required under RAG 2007-13 for aid to all *large* projects (those involving investment exceeding €50 million, irrespective of the amount of aid). RAG 2014-20 extends this to *all* projects and requires aid awards exceeding €3 million to be reported to the Commission within 20 days of the award.

2.6.3 Evaluation

A further innovation is the emphasis on evaluation. 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.[84] The precise terms of any requirement to undertake an evaluation[85] would be defined in the approval of the aid measure. However, evaluations must by undertaken by experts independent from

[81] RAG 2014-20, para 33 and Draft GBER, Article 15(3).

[82] RAG 2014-20, para 52-3.

[83] RAG 2014-20, para 141.

[84] RAG 2014-20, para 27.

[85] See also: http://ec.europa.eu/competition/state_aid/modernisation/evaluation_issues_paper_en.pdf

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 will be limited to those with large budgets, schemes with novel characteristics or in areas where significant market, technological or 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.[86]

[86] RAG 2014-20, para 144.

3. NATIONAL PERSPECTIVES ON AREA DESIGNATION

Following the adoption of RAG 2014-20, regional aid control moves into a new phase. Although a number of issues remain to be resolved – notably the precise scope of the GBER – the main task outstanding is the design and approval of the regional aid maps. For a number of Member States, this will be little more than a formality. This will be so if the entire country is eligible for regional aid (Bulgaria, Latvia, Lithuania, Estonia, Greece, Poland, Slovenia, Romania, Malta), or if the eligible population is entirely composed of 'a' regions (the Czech and Slovak Republics). In these cases there is no significant scope for domestic discretion beyond proposing aid intensities, and the maximum rates are anyway determined by RAG 2014-20.

In contrast, for many countries – those with non-predefined 'c' area, the process of selecting those areas is a complex process that will involve reconciling competing domestic demands with the constraints of RAG 2014-20.

For *all* countries, the notification of a regional aid map is an essential prerequisite for providing investment aid to large firms, or taking advantage of the SME aid intensities under the GBER; importantly, the approved maps will form an integral part of RAG 2014-20, [87] as under RAG 2007-13.

The aim of this section is to outline, to the extent possible at this stage, the steps being taken by the EoRPA countries to prepare assisted area maps for the 2014-20 period. For some countries, this review is of necessity limited given the recent adoption of RAG 2014-20 and given the sensitivity of many of the issues under consideration. Nevertheless, it is hoped that it will provide the basis for an exchange of experiences at the EoRPA partners' meeting.

3.1 Arrangements for area designation

Historically, countries have differed widely in their approaches to designating assisted areas, reflecting institutional structures and responsibilities, administrative conventions relating to consultation on certain issues and the perceived sensitivity of the process.

For 2007-13 ***Austria*** and ***France***, to some extent, adopted a similar approach. In both countries the 'c' area population quota was divided *ex ante* between the regions and the task of selecting the eligible areas delegated to that level. However, in *France* the process was essentially *deconcentrated* rather than *devolved.* The main responsibility for the task lay with the *Préfets*, the government representative in the region, which were charged with consulting with Regional Councils and local partners as they saw fit. By contrast, in *Austria* the process was led by *Land* level governments which produced draft maps, which were later subject to negotiation at a political level. The population quota was divided between the *Länder* in proportion to their shares of previous coverage.

Looking forward, the indications for both countries are of continuity rather than change in this process. In *Austria* the main responsibility for defining the assisted areas will remain with the *Länder*, though ÖROK administers a common database of indicators. It is not yet clear how population might be distributed between the *Länder,* but this task may be made easier by the overall increase in coverage. In *France* there are also signs of continuity. DATAR is the lead organisation at the national level and

[87] RAG 2014-20, para 175.

will propose a population coverage quota for each region based on a quantitative method for dividing up the national coverage. Formally, these regional population quotas are decided by the Prime Minister. The key difference in the current period is that, reflecting trends towards further decentralisation, the role of the elected Regional Councils will increase: in 2006, the regional *préfets* (the government representative in the region) took the lead in organising working groups with different local authorities, whereas this time maps will be drawn up jointly by the *préfets* and the regional councils. As in Austria, the process is likely to be eased by the increase in population coverage; on the other hand, the ‘anti leopard skin’ clause on area designation may prove to be a constraint in the French context. In terms of the timeframe, a decision on the criteria for population distribution was expected in summer, to be followed by a ‘circulaire’ from DATAR or the Prime Minister indicating the regional population ceilings and the provisions to apply. Based on these instructions, the regional maps are to be developed. While this is expected to be a time-consuming process, involving, for example, joint approaches by adjacent regions to reach the threshold of 100,000 inhabitants, it is also expected to be completed within two months. The regional maps will then be ‘aggregated’ into a national map by DATAR. The map is expected to be notified by the end of November.

In ***Germany***, as in previous periods, area designation is led by the Federal Ministry of Economy and Technology which coordinates proposals and secures domestic agreement. The main domestic forums where the proposals are discussed are the GRW (‘Regional Joint Task’) Coordination Committee at political level, and the GRW Sub-Committee at technical level. Overall the process is largely technocratic but the most sensitive decisions are taken at a political level. In both cases, the process is lengthy and involves extensive discussions, negotiations and trade-offs between the federal authorities and representatives of all the *Länder*. Technical decisions are made by the GRW Sub-Committee which is composed of federal and *Land* civil servants and chaired by a senior civil servant from the Federal Ministry for the Economy and Technology. Political decisions are either taken by the GRW Coordination Committee (made up of federal and *Land* Economics Ministers, and chaired by the Federal Minister for the Economy and Technology) or by the domestic Group of Ministers for the Economy (*Wirtschaftsministerkonferenz*) – which is made up of the relevant ministers of each *Land* and the relevant federal minister – sometimes separated into ministers for the eastern and western *Länder* respectively. In practice, preparations for the 2014-20 assisted areas map have been underway for some time, and were essentially awaiting the adoption of RAG 2014-20, which would determine the parameters relating to spatial coverage and areas designation criteria. Domestic preparations and the pre-existence of ‘well-oiled’ machinery for area designation enabled the German authorities to adopt an assisted area map and notify it to the Commission by end September 2013, though clearly this still requires Commission approval.

In ***Italy*** the designation of the ‘c’ areas for 2007-13 was extremely complex and controversial, leading to the Italian map being one of the last to be approved. The source of the difficulty was essentially two-fold. First, constitutional reforms had devolved economic development responsibilities to the regions; as a result, the emphasis was on reaching agreement between the regions. This was extremely difficult, largely owing to the very small ‘c’ area population quota accorded to Italy – just 3.9 percent of the national population. Moreover, of this quota, most (2.9 percent) was accounted for by Sardegna which, as an economic development area, had an *a priori* claim on ‘c’ status. In the first instance, the objective was to reach agreement on the division of the population quota. However, this was difficult to achieve and negotiations took a political rather than a technical turn. Moreover, discussions about the Structural Funds and regional aid were sometimes merged as regions sought

to exchange ‘c’ area coverage for Structural Fund receipts. Ultimately, some of the Sardegna coverage was ceded to other areas and the regions defined their own assisted areas, which were then assembled into a national map with, in effect, an *ex post* justification for the choices made. For 2014-20, as before, the process will involve a mix of ‘technocratic’ and political discussions within the CINSEDO (the Conference of Regions and Autonomous Provinces), within the working group chaired by the Ministry for Territorial Cohesion, which also led and oversaw the negotiations of RAG 2014-20. In the first instance, and based on a list of areas fulfilling the GDP and unemployment criteria (see 2.3.1 above) the Italian authorities (the national Ministry for economic development, DPS) will draw up a preliminary list on a ‘technical’ basis for discussion with the Commission. This preliminary list will then be discussed with the regions, to achieve political agreement. It is not anticipated that the map will be ready for notification in the autumn. The Italian authorities will seek the six-month extension of the current map (which has the additional advantage of higher aid intensities). Moreover, if agreement on the ‘c’ areas proves particularly difficult to achieve, the Italian authorities may notify only the map of the ‘a’ regions in spring 2014, in order for it to become operational by 1 July 2014, and notify the map for the ‘c’ areas separately.

In the ***United Kingdom***, as in the past, there is an extensive public consultation process underway.[88] The Department for Business Innovation and Skills (BIS), acting on behalf of the UK Government, is coordinating the consultation exercise with the devolved administrations for Scotland and Wales and will ultimately submit the UK 2014-20 assisted areas map to the Commission for approval. Northern Ireland is not included in this process and it has been agreed that Northern Ireland will retain 100 percent assisted area status ‘for at least the medium term’.[89] The first stage consultation document outlines the requirements of RAG 2014-20 and seeks responses on two issues: a set of proposed ‘common principles’ for drawing up the 2014-20 assisted areas map; and so-called ‘local intelligence’ that can be considered alongside economic data and policy considerations. The main targets of the process are: the Local Enterprise Partnerships in England; and local authorities in England, Scotland and Wales, all of whom have been alerted to the consultation. These bodies are encouraged to collaborate to identify cross boundary issues. In addition, the consultation document has been sent to a number of national stakeholders (eg. business organisations and planning associations), but is also open to the general public. The first stage closes on 30 September 2013. The second stage, which will seek views on a draft 2014-20 assisted areas map, will take place in winter 2013/14. The Welsh and Scottish governments are considered to have an important role to play in the gathering of local intelligence, coordinating the development of the draft maps to be presented at Stage 2 and refining the map in the light of the second round of consultation. However, the Stage 1 consultation document does not indicate whether this will be done on the basis of devolved population ceilings, similar to the process in France, for example.

The area designation process is far more centralised in the remaining EoRPA partner countries. In ***Finland***, ***Sweden, Norway,*** and ***the Netherlands,*** area designation is largely undertaken as a technocratic exercise within the ministries responsible for regional policy, though this is not to say that there is no external consultation or political input, but the mechanisms for this are less formal and the role of external input is lower key.

[88] Department for Business Innovation & Skills (2013) *2014-20 Assisted Areas Map: Consultation stage 1: Common Principles and Local Intelligence*.

[89] HM government and Northern Ireland Executive (2013) *Building a Prosperous and United Community* (https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/206979/Building_a_Prosperous_and_United_Community.pdf.

In the *Netherlands* there is no longer a regional aid scheme at the national level (the IPR was abolished in 2011), which diminishes the importance of an assisted areas map in general, though it can still be used as the basis for policies operated at the subnational level. Drafting the map is the responsibility for the Ministry of Economic Affairs (MEZ) and is expected to be a technocratic exercise focused on the same areas as at present (total coverage is unchanged), at least initially, but if a reallocation of the assisted area population is proposed, then it is possible that the proposals may be subject to lobbying from regional politicians. In *Finland*, *Sweden* and *Norway* the initial task of drawing up the map falls to policymakers in the relevant ministries, following which it is subject to political discussions. In Norway, for example, where the 2014-20 map has long been under discussion internally, policymakers drew up three alternative scenarios for each map (the investment aid map and the map of very sparsely populated areas where the social security concession applies). The different options use different indicators and approaches, but ultimately the choice will be a political one. Importantly, all three countries rely almost exclusively on the predefined sparsely populated areas for coverage; the new provisions on the non-transferability of this population to areas *not* meeting the population density criterion will be an additional constraint notably in Sweden and Finland.

In ***Poland***, area designation *per se* is not required as the whole country remains eligible either as 'a' regions or predefined 'c' areas. Nevertheless, as noted, a map will need to be formally submitted, though the parameters for this are effectively determined by RAG 2014-20, largely eliminating domestic discretion.

3.2 Approaches to assisted area maps

Member States adopt diverse area designation strategies to reconcile Commission constraints with domestic considerations. These considerations comprise a mix of policy options such as indigenous or inward investment, areas of need or opportunity – and political issues, such as the perceived equitable distribution of assisted areas between regions and the sensitivity of de-designating some areas, while according assisted area status to others for the first time. In the past, and rather more prosaically, an important factor was often the ease with which the map could be approved by the Commission, sometimes leading to rather pragmatic, as opposed to strictly policy-oriented, approaches to area designation.

At the time of writing, countries are at very different stages in the area designation process. On the one hand, the German authorities have already reached internal agreement on the map to be submitted for Commission approval; on the other hand, the Italian authorities already anticipate considerable challenges in designating 'c' areas and may, if necessary, simply submit a map comprising the 'a' regions and associated rates for approval to the Commission in the first instance.

In ***Germany*** the philosophy underpinning the map is based on national perceptions of economic disadvantage, but with some political adjustments a) to ensure that agreement can be reached among all *Länder* and the federal level and b) to maintain 'buy-in' to the GRW from as many *Länder* as possible (notably the western *Länder*). This rationale is unchanged compared to the past. The GRW Sub-Committee agreed the following principles for the regional aid map and process in 2014-20:

- The goal of the GRW is to strengthen growth in structurally weak areas, to create permanent competitive jobs and to support regions undergoing structural change.

- The GRW system benefits from ensuring that as wide as possible a number of *Länder* have designated areas.
- Area designation is on the basis of objective, consistent and economic criteria.
- GRW funding should be focused on structurally weak areas.
- Area designation should be transparent and comprehensible.

As in 2007-13, the map is based on 258 domestic 'labour market areas' (*Arbeitsmarktregionen*). In many cases, these areas are identical to NUTS 3 regions; there are also, however, numerous exceptions, particularly in urban areas (because the labour market areas are akin to travel-to-work-areas). Reflecting the principles outlined above, all German regions are ranked on the basis of a composite indicator, made up of four sub-indicators, the first two of which are significantly more important in terms of weighting, namely:

- the annual average unemployment rate in 2009-12 (45 percent weighting)
- the annual gross wage per employee paying social insurance in 2010 (40 percent weighting)
- the employment forecast for 2011-18 (7.5 percent weighting)
- an infrastructure indicator at 30 September 2012 (7.5 percent weighting)

In broad terms, these are the same indicators used for designating areas in 2007-13. In essence, areas are included in the map in order of the ranking until the population quota is exhausted, but further adjustments are made to deal with specific issues. Moreover, in addition to designating areas covered by the EU regional aid map, the same methods and ranking are used for designating domestic 'D' areas which are eligible for specific funding for SME aid. The German approach can be regarded as one of continuity, albeit within the context of a significant reduction in assisted area coverage.

In the ***United Kingdom*** the approach adopted for 2014-20 is more 'bottom up' and potentially less metrics-based than its predecessor. In particular, it seeks to make more use of locally provided economic intelligence than in the past; for 2007-13, the basis for the map was essentially the previous map, partly reflecting the cutbacks in coverage which had to be absorbed. The consultation document sets out a number of common principles on which it is intended to draw in drafting the assisted areas map. These are cast in term of both the need to assess economic *opportunity* and *need*. More specifically:

1. Assisted areas in the UK should reflect opportunities to support businesses with regional aid in locations that will support the economies of economically disadvantaged places.
2. A combination of quantitative and qualitative economic evidence and intelligence, and relevant economic policy considerations should be used.
3. In some circumstances, the primary purpose of designating some wards as assisted areas may be to link together other wards containing the characteristics sought for assisted area status – i.e. significant economic opportunities that could catalyse disadvantaged economies with a minimum contiguous population.

4. The 2007-13 assisted map should be a material consideration when developing its 2014-20 successor.
5. Providing eligibility to support large firms with regional aid should be a consideration of the 2014-20 assisted areas map given there are fewer constraints on government to support small and medium-sized enterprises with capital investment under other forms of state aid.
6. Offering UK public bodies the flexibility to invest regional aid in expanding and developing UK manufacturing should be a key goal when developing the assisted areas map.
7. The metrics of economic need that should be used to inform the map's development are:
    a. Low employment rate
    b. Low skills rate (level 2 and below)
    c. High working-age benefits claimant count rate
    d. Low population growth/et out-migration of working age population
    e. High rates of manufacturing
8. It is proposed that relative economic need will be considered at two spatial scales:
    a. At the LEP level in England, and the local authority level in Wales and Scotland
    b. At the potential assisted area level or its constituent parts.

The consultation asks respondents for their views on these principles, which are potentially subject to change, as well as seeking a better understanding of the geography of local economic opportunity by tapping into local knowledge and taking account of local priorities.

For ***Italy, France*** and ***Austria*** the approaches to areas designation are less explicit, at least at present, and this for a number of reasons.

In *Italy,* the principal focus of regional policy is on the south, the *Mezzogiorno.* Coverage of the 'c' areas is modest, at around 5 percent of the national population. This small quota, coupled with the need to reconcile regional priorities with the constraints on building blocks is likely to drive outcomes rather more than an overarching national strategic approach.

Austria has a more generous 'c' population quota than Italy (and higher than in 2014-20), but reflecting the federal structure and arrangements for area designation, outcomes will ultimately reflect *Land* level priorities coupled with political negotiations, rather than a national approach *per se*. Nevertheless, the national dimension is important in the context of the provision of common data and the political negotiations needed to achieve consensus, and there are some specific concerns relating to the definition and inclusion of mountain areas that are being addressed by national authorities with the Commission. The Austrian proposal is expected to be developed in the autumn, with a pre-notification meeting scheduled for late in 2013.

France also has a more generous 'c' population quota than before, which may ease the area designation process (though the building block criteria are a constraint). The first step in the process is for a decision to be taken on the distribution of the 'c' population between the regions. This will use a similar process as in 2007-13 taking into account income, the unemployment trends, the share of jobs in industry etc, depending on the precise scenario chosen. This forms the basis for a *circulaire* to the *préfets* containing the regional population ceilings and some indications as to how to proceed with the selection of areas. In this context, the existence of a national strategic approach to area designation will depend partly on the 'tightness' of the guidelines given to the *préfets* but also on the role of elected regional councils, which as noted earlier are set to play a bigger part.

For the ***Netherlands***, the approach to the map is arguably rather defensive, as opposed to reflecting a strategic intent: there is a specific concern with areas along part of the German border and particularly at the scale of cross-border differences in household income and unemployment. Moreover, Germany is perceived to have generous regional aid instruments that could potentially disadvantage Dutch firms. On the other hand, policy could be viewed as dormant in this regard as there is no national regional aid scheme, and apparently no pressure for one to be reintroduced.

In ***Finland*** and ***Sweden*** approaches to area designation are more tightly constrained than before owing to the 'non-transferability' of the population associated with pre-defined areas. In 2007-13 both Sweden and Finland had used the possibility of deploying this population elsewhere in order to address national priorities outside the strict limits of the sparsely-populated areas – although these areas remained the main focus of policy, not least because they qualify on a number of other indicators of disadvantage. For the 2014-20 map *Sweden* may only designate areas that fulfil the sparsely populated region criterion, a constraint that is somewhat at odds with recent regional economic developments in Sweden where the north has been performing comparatively well, largely due shifts in certain commodity markets, while there are pockets of difficulty in southern Sweden owing to the wider economic downturn. *Finland* has somewhat more flexibility, although the sparsely populated regions and Åland will remain the key focus of policy.

In ***Norway*** the basis for area designation proposals for the investment aid map is the peripherality index which takes account of a range of indicators grouped into geography, demography, economic development and living standards. Coverage for Norway is set to be slightly lower than in 2007-13 but the Norwegian authorities opted not to use all of the available population quota for the investment aid map in 2007-13, effectively trading this for some flexibility in the application of the social security concession for the very sparsely-populated areas. As noted earlier, a number of scenarios have been developed, but the ultimate decision about the focus of policy will be a political one.

4. DISCUSSION ISSUES

This paper has provided an overview of the key changes resulting from the adoption of the 2014-20 Regional Aid Guidelines and a preliminary review of EoRPA partners' progress in devising assisted area maps for the new period. RAG 2014-20 is a significant milestone in the evolution of regional aid control and gives rise to a number of practical and more philosophical issues and questions. The aim of this final section is to highlight some of these as a starting poit for further discussion.

i. Notwithstanding the adoption of the regional aid guidelines, the current period is characterised by a degree of flux and uncertainty.

This partly results from the state of play regarding the 2014-20 GBER, which means that the precise scope of the notification requirements are still uncertain. As would be expected, there remains opposition to the line taken by the Commission on aid to large firms; this is not universal - not all Member States were opposed to the exclusion from aid of large firms in 'c' areas. The compromise adopted by the Commission is welcomed by some, but it lacks clarity in some important respects. As matters stand, the compromise will involve greenfield investments by large firms in 'c' areas falling within the GBER, but any other proposed aid for general investment by large firms will require notification and assessment under RAG 2014-20. There is some ambiguity in the references to diversification investment and over where 'process innovations' fit regarding eligibility. There are also questions over the definition of single investment projects and the role of aid paid in the past. It remains to be seen what impact RAG 2014-20 will have on the scale of notifications and whether there is scope to design aid schemes including 'diversification aid' for large firms that could achieve compatibility.

Looking beyond RAG 2014-20 and the GBER, other aspects of State aid control will also affect the conduct of regional policies in the Member States to varying degrees. In particular, under SAM, the Commission committed itself to clarifying the notion of State aid. To date, no progress appears to have been made on this and the absence of concrete definitions remains a source of perplexity for many policymakers, especially those at the subnational level or involved in *ad hoc* interventions. Also, in some countries, regional aid has been an important instrument for the support the energy sector (for example in Poland and other Central and Eastern European countries); this is excluded from the scope of RAG 2014-20 and will, apparently, be included in future energy and environmental aid guidelines to replace the current environmental aid guidelines[90] which expire end 2014. However, no draft guidelines have yet been issued. Last, the decision in the *Leipzig-Halle* case[91] reflects a further evolution in the treatment of infrastructure funding under the State aid rules. Some types of infrastructure explicitly fall within the scope of RAG 2014-20, namely broadband and research infrastructures, while airports are excluded. In the wake of the *Leipzig-Halle* decision the Commission is scrutinising a number of cases (notably, but not only, concerning sports arenas), and in the absence of guidelines on aid to the relevant type of infrastructure, the compatibility assessment is based on the balancing test, heightening uncertainty for policymakers and beneficiaries and contributing to lengthy procedures.

[90] Community guidelines on State aid for environmental protection, [2008] OJ C82/1.

[91] Case C-288/11 P *Mitteldeutsche Flughafen AG and Flughafen Leipzig-Halle GmbH v European Commission,* judgment of 19 December 2012.

ii. RAG 2014-20 reflects a pronounced shift in the theories of competitive harm prioritised by the Commission

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.

The 1998 Multisectoral Framework (MSF 1998)[92] 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 the 2000 Multisectoral Framework (MSF 2000)[93] 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 LIPS Guidance[94] 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, curtailing 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 Draft GBER requirement to notify high budget schemes[95] and the scope to impose an external evaluation as a condition of scheme approval.[96]

The preoccupation with incentive effect and the manner in which this is prioritised raises a number of interrelated issues. There are some important questions of principle, as well as practical considerations. It has been argued that the reforms flowing from the SAAP promote “an essentially ideological agenda that aims to reduce the role of democratically elected public institutions on the market”. Importantly in the context of regional aid, the separation of equity and efficiency objectives and the presumption of negative trade-offs between the two limits the scope to justify aid measures with arguments about fair distribution.[97]

It is also questionable whether perceived ineffectiveness or inefficiency alone are sufficient grounds on which to prohibit a measure;[98] despite this, the policy turn in the latest reforms extends beyond

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

[93] Mulitsectoral framework on regional aid for large investment projects – Rescue and restructuring aid and closure aid for the steel sector, [2002] OJ C70/8, as amended, [2003] OJ C263/3.

[94] Communication from the Commission concerning the criteria for an in-depth assessment of regional aid to large investment projects OJ 2009 C223/3.

[95] Draft GBER, Article 1(2)(a).

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

[97] C. Kaupa, (2009) The More Economic Approach – a Reform Based on Ideology?, EStAL 8(3).

[98] See also D. Spector (2009) *State aids: Economic Analysis and Practice in the European Union*, in X. Vives (ed.) Competition Policy in the European Union, Oxford University Press.

concerns at competitive outbidding and market structures – competition effects – and, in the name of 'incentive effect' into the realms of efficiency, effectiveness and public spending choices that are arguably the domain of elected governments. Moreover, while it is clear that national authorities *are* quite genuinely concerned about the incentive effect of regional aid, particularly in a climate of budgetary constraint, opinion is divided about how and whether this can be ascertained in practice.

iii. Is greater discrimination between 'a' and 'c' areas really justified?

Explicit discrimination between 'a' regions and 'c' areas dates back to the 1988 Communication.[99] The criteria used to determine 'a' regions are rather questionable from a regional economic development point of view, as is the practice of 'sharing out' 'c' area population among the Member States. Arbitrary as these mechanisms are, they have nevertheless gained some degree of consensus in what is a highly contentious policy area. Importantly, however, there has never been significant discrimination between 'a' regions and 'c' areas, beyond maximum aid intensities (albeit arbitrarily set). By contrast, RAG 2014-20 restricts the scope of aid to large firms in 'c' areas drawing a very clear demarcation between the two categories of eligible area with respect to the availability of aid.

For several reasons, it is questionable whether this is justified. First, although as noted, the process of determining coverage and drawing maps has achieved some consensus, the underlying rationale is of rather dubious merit and does not provide a basis for such stark discrimination between eligible areas. Second, the coverage of 'a' regions is set for seven years, but on the basis of data that is not only four to six years out of date by the time the map comes into force,[100] but that is also highly sensitive to economic fluctuations and boundary changes.[101] Third, the studies cited by the Commission *do* indeed tend to doubt the incentive effect of regional aid for large firms,[102] but they do *not* provide an evidence base for discriminating between 'a' regions and 'c' areas – in other words they do not justify retaining aid to large firms in 'a' regions either!

iv. Of NUTS and NACE – a veneer of comparability

The compromise proposed in the Draft GBER – to enable regional aid for 'greenfield' investments seems ill-conceived. Under considerable political pressure, the objective of the provision is to enable some support for large firms in 'c' areas – namely "initial investment in favour of a new activity… …in the area concerned."[103] In this context, the 'same or a similar activity' means activities falling under the same class (four-digit NACE code); the area concerned refers to the NUTS 3 region. In other words, the provisions largely eliminate support for expansion projects in 'c' areas by requiring large firm investments to be either in a new activity or in a different NUTS 3 area from existing activities. The NUTS and NACE criteria ostensibly have the appeal of objectivity but in practice are likely to give rise to unintended consequences.

[99] Communication on the Method for the Application of Articles 92(3)(a) and (c) to Regional Aid, OJ 1988 C212/2.
[100] The 'a' areas for 2014-20 are based on GDP(PPS) data for 2008-10.

[101] For example, the splitting of Slovenia into two NUTS 2 regions has resulted in one having 'a' status; had Slovenia remained a NUTS 2 region, it would not have had 'a' status. Similarly, the merger of regions in Croatia has resulted in the entire country having 'a' region status; without this reconfiguration, only part of the country would have been covered. Last, and also important, an 'a' region map produced on the basis of 2007-9 data differs from that based on 2008-10 data.

[102] Though it is a rather limited list.

[103] Draft GBER, Article 15(4).

NUTS 3 regions differ widely in size and composition between (and even within) countries.[104] In mainland Europe, in physical size they range from just 35.7 km2 (Schweinfurt, Germany) to 106,012 km^2 (Norbotten, Sweden); in population terms they range from 19,300 (Evrytania, Greece) to 6.5 million inhabitants (Madrid). In short, the impact of the 'area' constraint would vary widely between locations.

The nature of the NACE codes varies considerably between activities.[105] For example, 'manufacture of workwear' and 'manufacture of other outerwear' are *different* activities under the NACE classification, but a much less fine-grained approach is taken to newer, often high technology service activities; for instance, 'data processing, web hosting and related activities' all fall within the *same* four-digit code. Significantly, however, in an apparent tightening of the Draft GBER proposals, RAG 2014-20 subjects *all* diversification projects to notification.

The NUTS and NACE criteria aside, the constraints do not sit easily with typical economic development promotion activities in many disadvantaged regions, which often depend on building long-term relationships between incoming investors, the sub-supplier network and development agencies. Perversely, these new constraints on 'c' areas might even encourage existing firms in weaker regions to consider relocation more actively when major investments are under consideration. On the other hand, the treatment of 'new process innovations' mentioned in RAG 2014-20, but not defined, seems likely to offer some scope for projects other than greenfield investments in 'c' areas, albeit subject to notification at scheme or individual aid levels. However, it remains to be seen how this is interpreted and, in particular, whether there is scope to introduce aid *schemes* that could provide support for 'diversification' under conditions that the Commission could accept or whether individual notification would always be required.

v. The very pursuit of incentive effect may diminish the prospect of achieving it

For the last decade or so policy developments in the control of State aid have been heavily influenced by the 'more economic approach'. However, in the field of regional aid, the reach of economics has arguably been rather partial. While there have been successive refinements to the handling of cases of large investment aid, many of the underlying parameters governing regional aid remain either unchanged or subject to seemingly arbitrary adjustment. For example, the aid intensities set out in successive guidelines are largely based on relative levels of regional GDP per head and have been steadily reduced over time. Regional GDP measured in national PPS is a questionable basis on which to determine what rates are appropriate. Moreover, whilst reducing aid rates is desirable on several levels, little consideration seems to have been given to the aid intensity actually required to produce an incentive effect. Indeed, it could be argued that the levels of aid available to large projects under the reduction formula may be too low to create an incentive effect and may, paradoxically, increase the likelihood of windfalls gains. In other words, low value aid may be discounted early on in investment decisions, but informational asymmetries enable firms to conceal the fact that aid is non-decisive. In this regard, one might also question the logic of requiring an incentive effect, but limiting

[104] The NUTS classification (Nomenclature of territorial units for statistics) is a hierarchical system which divides up the EU territory for statistical purposes. See http://epp.eurostat.ec.europa.eu/portal/page/portal/nuts_nomenclature/introduction

[105] The NACE classification is the nomenclature of economic activities in the EU. The current version is NACE Rev.2, available here: http://epp.eurostat.ec.europa.eu/cache/ITY_OFFPUB/KS-RA-07-015/EN/KS-RA-07-015-EN.PDF

aid to the amount necessary to compensate for additional costs in an assisted area location. Can mere compensation have an incentive effect?

Related, depending on the scope for aid schemes for large firms in 'c' areas, an important issue is the impact of the rules themselves on the incentive effect of regional aid. Notifiable large investments will have no 'safe harbour' in the market screens, though it remains to be seen what impact this might have on the number of notifications. However, the application process which preceded the notification may itself have been lengthy; the compatibility assessment will add to the delay. There is an inherent conflict in the requirement that aid be needed (incentive effect) for project to go ahead and the uncertainty created by Commission scrutiny. It can be argued that the incentives most likely to alter business behaviour are those that are predictable and can be factored into business decisions at the outset. The length and complexity of the notification and assessment procedures create considerable uncertainty and delays for applicants. This may actually lead to aid being discounted in the investment decision and treated as a bonus should aid ultimately be approved. In other words, the bureaucratic process may itself result in higher windfall gains – i.e. less incentive effect – because applicants are well-placed to exploit information asymmetries in order to meet the requirements of the compatibility assessment. The lessons from MSF 1998 – the need for predictability, reduction of the administrative burden and simplification[106] – may have been lost.

[106] 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.