Draft GBER - EXPLANATORY MEMORANDUM

I. OBJECTIVE AND CONTEXT OF THE PROPOSAL

The Commission launched, with its Communication on State aid Modernisation ("SAM"), of 8 May 2012, a broad review of State aid rules. State aid enforcement should contribute to sustainable, smart and inclusive growth, focus on cases with the biggest impact on the single market and streamline the rules and provide for faster, better informed and more robust decisions.

The review of the General block exemption Regulation ("GBER") is at the centre of the SAM reform and shall contribute to all objectives, with particular focus on simplification. With about 2000 measures introduced since its entry into force, the current GBER has been extensively used by Member States. In 2011 aid under GBER amounted to EUR 17.2 billion, which represents 32.5% of aid granted to industry and services.

The GBER review will ensure that Member States and stakeholders have a clear set of rules as of 2014 as a reference point for the development of their policies and aid interventions.

The GBER has made it possible to both broaden and simplify State aid enforcement but it has highlighted two main shortcomings of the current regime: (i) the rules are complex and they do not provide sufficient incentives to comply; (ii) there is a lack of consideration of the cumulative impact of aid. These shortcomings call for a double response: On the one hand, the GBER can be clarified and simplified to facilitate its correct application. In parallel, evaluation of large schemes, publication obligations and ex post monitoring should contribute to a better compliance, preventing deadweight losses as well as excessive and distortive aid. On the other hand, schemes which provide funding in fields where market failures may be presumed, but which are unlikely to raise serious competition concerns, should be covered by the GBER on the basis of clearer ex-ante rules and better evaluation of their impact.

II. PROPOSED MODIFICATIONS

The reform of the GBER can contribute to the SAM objective of simplification by extending its scope to include new measures and increase of the notification thresholds for individual cases. The review of the Regulation is a long process, as it requires twice a formal consultation of Member states (2 Advisory Committees) and a publication on the Official Journal of draft Commission proposal in between. On certain issues work is on-going within the Commission services and several Options are presented or are left open for the 1st public consultation of Member States to seek stakeholders' views. The Commission will take a final view a later stage.

- **Increased flexibility with regard to notification thresholds**

With regard to aid for **R&D projects**, it is proposed that for projects consisting predominantly in fundamental or industrial research activities, current notification thresholds to be doubled - without the need of ex ante scrutiny by the Commission – provided the compatibility conditions are respected. This modification reflects the Europe 2020 emphasis on research and development and the limited potential for distortion of competition stemming from activities that remain comparatively far from market application. For aid for experimental development projects, it is proposed to only slightly increase the notification threshold to EUR [10] million, as it has a higher distortion potential through the increasing proximity to market application of the research results. DG Competition encourage Member States to provide feedback on the proposal. The draft GBER recognises the importance of repayable advances as a risk sharing mechanism less distortive that traditional grants and with strong incentive effect and incentivises their use through increased notification threshold by [50]% and aid intensities. The proposed increase of the notification thresholds is open for discussion. EUREKA projects and projects implemented under Joint Undertakings on the basis of Article 187 of the Treaty will also benefit from higher notification thresholds.

In addition and for the first time, support for the construction or upgrade of **research infrastructures** which perform economic activities and are thus (fully or partially) subject to State aid rules does not need to be notified to the Commission for aid up to EUR [15] million. DG Competition encourages stakeholders to provide feedback in this respect. Such aid can be granted only to the extent that access to the infrastructure is granted on a transparent and non-discriminatory basis and on market terms. Any deviation from these conditions (for example, the use of the infrastructure is not charged at market prices) should be notified to the Commission for clearance.

Risk finance aid for SMEs shall better reflect actual market failures (in particular funding gaps) and allow more flexibility for timely investments; therefore the maximum annual investment tranche of EUR 1.5 million will be replaced by an overall investment cap of EUR 10 million. Thus risk finance will support the needs of SMEs more efficiently at each stage of their development, rather than imposing constraining annual investment limits. In addition, new simplified thresholds are proposed for aid for start-ups available throughout the EU: EUR 2 million for loans, EUR 3 million for guarantees (both nominal amounts) and EUR 0.4 million for grants with bonuses for enterprises established in assisted regions. For small and innovative enterprises these amounts will be doubled. Nominal amounts will significantly reduce administrative burden of aid granting authorities and serves the simplification objective for small enterprises.

With respect to aid for **environmental protection**, the current notification threshold of EUR [7.5] million for investment aid is open for discussion. A simplified calculation method of eligible costs is introduced, on which the DG Competition seeks the views of the stakeholders. In view of this change, the aid intensities are left open at this stage of the consultation.

- **Increased safeguards to ensure compliance**

The increased flexibility resulting from the above increase of the scope will be balanced by new provisions requiring the notification of **very large schemes** whose annual public expenditure cumulatively exceeds 0,01% of national GDP and EUR 100 million, including a clause to avoid circumvention by artificial splitting of schemes. DG Competition encourages Member States to provide feedback in this respect.

To increase efficiency and accountability of public spending in times of scarce resources and to increase the quality of controls and public awareness over aid granted, new **obligations with regard to transparency** are introduced. Member States have to publish, after the granting decision, key information on a single website, including the name of beneficiaries and the aid amounts. This information must be available to the general public without restrictions.

The introduction of these new transparency requirements will facilitate **enforcement** for national authorities and will lead to better control of aid granted, eventually reducing the need for reporting, thereby contributing to further reduction of the administrative burden.

Finally, the draft GBER introduces a more targeted and thus more deterrent sanction for failure to comply in the form of **withdrawal of the benefit of the block exemption**. In such a case, the Commission may require the notification of all or some of the future aid measures concerning certain beneficiaries or certain granting authorities.

- **<u>Simplified check of the incentive effect</u>**

One of the options proposed is a significant simplification as compared to the existing GBER, which will apply uniformly to all companies: before the project or activity has started, companies shall submit a standard application form. This would constitute a major reduction of the administrative burden for both aid granting authorities and aid beneficiaries. Since it is more difficult to establish the incentive effect with respect to ad hoc aid to large enterprises, these measures would have to be either notified or made subject to stricter conditions. DG Competition encourages Member States to provide feedback on the proposed Options for ad hoc aid to large companies.

Another option is to keep the existing rules and require large companies to submit additional documentation which aid granting authorities need to check. This would make it easier for the Member States to ensure that the aid is necessary and acts as an incentive for further activities, but would maintain the administrative burden involved.

In any case, the main principle will remain that no aid shall be available for activities in which the beneficiary would already engage under market conditions alone.

- **<u>Regional aid [articles 14-16]</u>**

This aid can be granted in areas eligible for regional aid as determined in the approved regional aid maps for the period 2014-2020.

Regional aid may be granted in 'c' regions for an initial investment to SMEs, whereas aid to large enterprises may only be granted for initial investments in favour of ***new activities*** in the area concerned, since large enterprises are less affected by regional handicaps when choosing a location to invest. Regional investment schemes outside an operational programme must now contribute to a regional development strategy with clearly identified objectives. Certain regional aid schemes targeted at particular sectors of the economy are excluded from regional block exemption, as structural sector deficits outweigh potential positive cohesion effects: steel and synthetic fibres. Regional aid to shipbuilding, coal and transport sectors and airport infrastructure shall not be block-exempted, but will need to be notified to the Commission for clearance to take into account their specificities.

To minimise the distortive impact on the internal energy market and to ensure an increased focus on cost efficiency, investments in assisted regions in favour of energy from renewable sources, co-generation and efficient district heating shall be allowed under the conditions laid down in the environmental section of the draft Regulation, possibly combined with regional bonuses to address the handicaps of assisted regions (Option on regional bonuses). On the other hand, state aid to electricity generation from non-renewable sources and to energy infrastructures shall not be exempt from the notification, in view of their high distortive potential impact on the internal energy market. Such investments shall be notified to the Commission to assess their compatibility with the internal market.

Given the importance of the European Territorial Cooperation under the EU cohesion policy and the handicaps these projects experience (variety of project partners located in different areas), a new provision has been introduced to transfer the aid intensity of the area in which (the biggest part of) an initial investment is located to all beneficiaries participating in the project.

Finally, for the first time, certain aid to outermost regions can be block exempted to reduce administrative burden: operating aid to compensate the transport costs of goods produced in outermost regions and sparsely populated areas and other additional costs faced by outermost regions.

- **<u>Aid for SMEs [articles 17-22]</u>**

Previously scattered provisions concerning aid to SMEs have been refined and regrouped under Section 2 of the draft GBER. Also, a new provision for the compensation of cooperation costs for SMEs participating in the European Territorial Cooperation (ETC) has been added to help SMEs cover the additional costs of the joint management of ETC projects.

SMEs often have difficulties in obtaining capital due to risk-averseness of financial markets. The reviewed block exemption rules on SMEs shall contribute to one of the key priorities of the Europe 2020 Strategy, i.e. ensuring access to debt and equity finance for SMEs while stimulating private investments.

The revision of risk capital rules shall extend its scope, simplify the rules and provide more flexibility. This extension shall be accompanied by well-designed compatibility rules to avert the risk of crowding out and distortion of competition. The increasing use of revolving aid instruments shall be promoted.

It is proposed to change the definition of SMEs eligible under risk finance rules and also include SMEs in their later growth stages, as well as follow-on investments and replacement capital, better reflecting the actual dimension of existing market failures. The new GBER will cover any form of risk finance, such as equity, quasi-equity and debt provided via financial intermediaries, to better reflect market practices, extending the ambit of the rules from 'risk capital' to 'risk finance' aid. This change will also bring many Financial Instruments for SMEs under the scope of the GBER and should thereby provide legal certainty in designing those instruments.

The scope of the new GBER will be extended to certain commonly used fiscal measures and guarantees to provide more legal certainty, considering the increasing use of these measures to support high growth SMEs. New provisions aim at block exempting aid to alternative trading platforms specialised in SMEs and aid for scouting costs.

Start-up aid: DG Competition proposes simplifying the above scattered provisions for start-up aid (regional aid, aid to female or young entrepreneurs and aid to innovative enterprises) into a broad category of start-up aid, targeting the market failure of access to finance for all start-ups. The measure will cover small enterprises up to five years following their registration.

- **Aid for research, development and innovation [articles 23-26]**

Experience shows that market failures prevent the RDI markets from reaching the optimal output and lead to inefficiencies. The reviewed GBER shall facilitate the granting of aid related to the Europe 2020 and in particular Horizon 2020 objectives.

The conditions for RDI aid under the GBER have been simplified and streamlined. Aid for demonstrators and pilots have been facilitated to bridge the gap between scientific research and market application and to remove the barriers for entrepreneurs to bring "ideas to market", priorities of the Communication on the Innovation Union flagship initiative and the Communication on Key Enabling Technologies. Also, improved definitions of industrial research and experimental development now allow for a more flexible coverage of some types of research activities, in particular of certain types of prototypes. These changes will usefully complement the increase in the scope and flexibility of the provisions addressing financing needs of SMEs not only for the start-up and early development phases, but also for demonstration and market introduction of the innovations developed.

Two categories of aid that previously were not covered by the GBER are now introduced:

i. **Research infrastructures:** in recognition of their key role in the advancement of knowledge and technology, a block exemption for aid for the construction or update of research infrastructures is introduced. Eligible infrastructures must be accessible on a transparent and non-discriminatory basis. The article only covers aid to the research infrastructure and not to the end users; the latter should be notified to the Commission for clearance.

ii. **Innovation aid**: In line with Europe 2020 and the Innovation Union, a wider range of innovation support measures for SMEs shall be covered in the new GBER. The proposal simplifies and streamlines conditions for innovation aid measures, grouping together all categories of innovation aid for SMEs. An important simplification is a single aid intensity.

In order to incentivise RDI investments in assisted areas, bonuses are introduced for large companies that choose to invest in "c" regions for investments with overlapping eligible costs for the purposes of regional and RDI aid.

- **Training and employment aid [Articles 27-29]**

For training aid, a single category is proposed, thus removing the distinction between general and specific training, responding to numerous difficulties highlighted by Member States and stakeholders. This implies a significant simplification of the rules and shall remove practical problems with the enforcement of the distinction and with the qualification of training as general. It will also simplify eligible costs.

The new GBER extends the scope of block exemption for aid for the recruitment and employment of disadvantaged and disabled workers. The eligibility for employment aid is enlarged so that the definition of disadvantaged worker applies to young people of 15-24 years old. The definition of "severely disadvantaged" is enlarged to include persons who accumulate 12-months unemployed and suffer from a specific disadvantage.

In view of the particular handicaps with which SMEs are confronted and their higher relative costs when they invest in training, the intensities of exempted aid should be increased for SMEs. Likewise the intensities shall be increased for training to disabled or disadvantaged workers.

- **Aid for environmental protection [Articles 30-38]**

The reviewed GBER shall contribute to a high level of environmental protection and thus to sustainable growth, one of the main pillars of the Europe 2020 strategy. Experience shows that environmental protection is confronted with market failures, in particular limited incentives for undertakings to reduce pollution levels, which may increase costs without corresponding benefits.

The reviewed GBER shall facilitate the granting of environmental aid in the areas of resource efficiency (energy saving and energy efficiency, cogeneration), climate change and energy measures, while a new category is added, support for district heating. It shall facilitate measures incentivising undertakings to achieve a higher level of environmental protection than required by EU standards and facilitate early adaptation to future EU standards for SMEs. New provisions are introduced on aid for the remediation of contaminated sites where the polluter cannot be identified.

In view of the difficulties in determining the extra cost resulting from the investment to improve environmental protection, the systematic identification of an alternative investment won't be required; if an alternative investment cannot be identified, the total costs of "green" investments may be taken into account.

Also, two alternative models to support to Renewables are presented. The first is an auctioning model on the basis of technology neutral, open and competitive bidding processes to ensure cost efficiency and to limit distortions of the internal energy market. The second is an investment model on the basis of total costs of the "green" investment; fixed aid intensities are not defined at this stage. DG Competition encourages Member States to provide feedback in this respect, in particular the inclusion of balancing responsibilities.

Conclusions

The GBER review faces the challenge to facilitate growth by promoting "good aid", while keeping focus on quality of public finance and promoting a more integrated, dynamic and competitive single market. The horizontal and vertical extension of the scope and the simplification of rules (with clearer rules that are applicable *per se*) are combined with safeguards (publication obligations, evaluation). This integrated approach shall incentivise Member States to undertake more efficient and pro-growth interventions, shall generate peer review and reduce competition distortions in the internal market.