



BRIEFING PAPER

Number 06775, 7 November 2018

EU State Aid Rules and WTO Subsidies Agreement

By Ilze Jozepa

Contents:

1. EU state aid rules
2. WTO Agreement on Subsidies and Countervailing Measures
3. Implications of Brexit



Contents

Summary	3
What is state aid?	3
Implications of Brexit	3
What does the EU state aid framework look like?	4
Is there much state aid in the UK?	4
1. EU state aid rules	6
1.1 Is it state aid?	6
1.2 Exemptions	8
<i>De minimis</i> rule	8
Aid under an approved scheme	9
General Block Exemption Regulation	9
1.3 Notifying the European Commission	12
1.4 How are state aids controls organised in the UK	12
Devolved administrations	12
1.5 Statistics	13
2. WTO Agreement on Subsidies and Countervailing Measures	15
2.1 Comparing EU state aid and WTO rules	17
Statistics	18
3. Implications of Brexit	20
Summary	20
3.1 Will state aid be part of the new relationship with the EU?	20
3.2 The outlines of an independent regime	21
A new state aid authority	22
Common rulebook on state aid	23
Transition period	24
Leaving without a deal	24
Domestic reform	25
3.3 The role of devolved administrations	26
3.4 Opposition views on state aid	26
3.5 Other models for the UK-EU cooperation on state aid	27
European Economic Area (EEA)	28
EU-Ukraine Association agreement	28
Comprehensive Economic and Trade Agreement (CETA)	28

Summary

What is state aid?

EU Member States sometimes use public resources to intervene in their national economies by assisting companies or industries. This can range from a government tax relief scheme for investors to a local authority giving a subsidy to a property developer.

This type of assistance is called 'state aid' and is normally prohibited because it can distort trade and competition between firms, discourage investment and increase costs to consumers. EU state aid rules aim to create a level playing field so that, for example, British firms can compete fairly with German ones.

But state aid can also be an important and effective policy tool. Exemptions to the EU state aid rules allow for certain beneficial interventions. For example, state aid might be necessary and justified to address a market failure, as when SMEs have difficulties finding investment capital. It may also be necessary to achieve policy goals such as regional economic development or environmental protection. Governments can, for instance, use state aid to stimulate businesses to invest in less developed areas or the development of advanced environmentally friendly technologies.

The European Commission (EC) has strong powers to assess cases of state aid, approve them and enforce stringent 'claw-back' mechanisms when state aid is deemed unlawful. The UK has no specific legislation for state aid, as the EU rules apply directly.

Implications of Brexit

Leaving the European Union will alter the state aid regime in the UK.

The absence of the EU state framework is not expected to translate into higher levels of direct support to businesses in the UK as successive governments have preferred rigorous state aid controls and have avoided subsidising particular industries or companies. However, pressure on the government to intervene might become more intense.

The extent to which EU state aid rules will apply in relations between the UK and the EU will be determined by the deal the UK and the EU agree. It is very likely that state aid provisions will be part of the agreement, not least because the EU has insisted on including some sort of controls on state assistance in almost every free trade agreement it has signed with other countries in the past.

While the European Economic Area (EEA) Agreement and Association Agreements with aspirational Member States like Ukraine tend to replicate the EU state aid rules, Free Trade Agreements with South Korea and Canada build upon the less stringent World Trade Organisation commitments on restricting harmful subsidies. In general, the closer the market integration with the EU, the more state aid rules form part of the agreement.

State aid is when public organisations support certain enterprises or industries, financially or by other means.

4 EU State Aid Rules and WTO Subsidies Agreement

The Government is in favour of an independent UK state aid regime and is already working to create one. The EU Withdrawal Act 2018 will preserve a general prohibition of state aid from “exit day” by transposing the existing EU law into the UK legislative framework. The Competition and Markets Authority (CMA) will become the UK’s independent state aid authority to take over the current role of the EC.

The UK has proposed the EU to follow a common rulebook on state aid whereby the UK continues to apply the existing EU state aid law. At this point, it is unknown how much of this Government proposal will be included in the future EU-UK Agreement, but state aid appears to be one of the less contentious aspects of cooperation, as both sides are keen on preserving a level playing field for their businesses.

Transition period

If the UK and the EU agree on a transition period, the Government will continue to apply the EU state aid regulations during that time. The EC will continue to assess and approve UK state aid. The jurisdiction over pending cases is still under negotiation.

No-deal scenario

If the UK exits the EU without a formal agreement, the Government plans to have a functioning UK-wide state aid regime in place by the exit day. The UK public organisations would have to notify their state aid measures to the CMA, instead of the EC. Any previously approved state aid measures would retain their status and any pending notifications to the EC would need to start a new notification with the CMA.

What does the EU state aid framework look like?

There is a general prohibition of state aid in the EU, but there are some exemptions. If a measure involves state aid, policymakers need to ensure that it is legal. This can be done, for example, by demonstrating that the measure is covered by an exemption in the rules, or by seeking the approval of the EC.

There are three categories of standard exemptions to the state aid rules. If any exemption applies to a state aid measure, then the assistance is normally permitted without the need to seek the EC’s approval. These categories are:

- the *de minimis* rule under which assistance that is worth less than €200,000 per business over three years is allowed;
- the exemptions for aid under schemes that have already been approved by the EC; and
- general exemptions for aid that serves certain policy aims such as regional development, environmental protection and innovation.

Is there much state aid in the UK?

The UK public sector spends less directly and selectively supporting businesses than most other EU countries. In 2016, the UK spent 0.36% of GDP on state aid (excluding railways), while France spent 0.65% and Germany 1.31%.

World Trade Organisation Agreement on Subsidies and Countervailing Measures

In addition to EU state aid rules, the UK is party to the WTO Agreement on Subsidies and Countervailing Measures. Under the Agreement, some subsidies are prohibited outright while the rest are 'actionable' – meaning that the subsidy is allowed, but other countries can take certain actions if the subsidy harms them. Countries can protect their industries by taxing imports of the subsidised good – this is known as imposing a 'countervailing duty'.

Although the definition of a 'subsidy' under the WTO regime is broadly similar to 'state aid' in EU law, the EU rules are a lot more stringent than the WTO rules on subsidies. The key differences are:

- The default position in WTO rules is that subsidies are generally allowed, while EU rules consider subsidies to be generally illegal.
- WTO rules apply to goods, but EU rules include services too.
- EU rules are applied prospectively (i.e. legality must be proved *before* awarding any support), while WTO rules are only reactive, and are only triggered if a member country lodges a complaint.
- WTO rules rely on state-to-state enforcement while under EU rules there are remedies available to businesses and individuals.
- Under EU rules, a business has to repay illegal state aid. There is no such mechanism to remove anti-competitive effects under the WTO rules.

In case the UK exits the EU without a formal agreement, the WTO rules on subsidies would still apply.

Disclaimer

This information is provided to Members of Parliament in support of their parliamentary duties. It is a general briefing only and should not be relied on as a substitute for specific advice.

The EU state aid legislation currently in force can be found in [this page of the European Commission's website](#).

The full text of the WTO's Agreement on Subsidies and Countervailing Measures can be found in [this page of the WTO's website](#).

1. EU state aid rules

EU Member States sometimes intervene in their national economies by providing assistance to companies or industries using public resources. This can range from a government tax relief scheme for investors to a local authority giving a subsidy to a property developer.

This type of assistance is called 'state aid' and is normally prohibited by EU rules, unless it is covered by one or more of the exemptions outlined later.

State aid is generally prohibited in the EU because it can distort competition between firms, discourage investment and cost consumers. State aid rules aim to create a level playing field so that, for example, British firms can compete fairly with German ones. The arguments in favour of state aid rules also apply to domestic competition.

The UK Government supports strong state aid rules:

The ineffective use of State aid in the long run can ... lead to a persistence of inefficient and unproductive industries, preventing the emergence of new and more innovative, high growth firms ... and so damaging the country's long term prosperity. And of course, if taxpayers' money is not being used to subsidise inefficient enterprises, taxes can be lower or public spending can be increased in other areas.¹

But state aid can also be an important and effective policy tool. Exemptions to the state aid rules allow for certain beneficial interventions. For example, state aid might be necessary and justified to address a market failure, as when SMEs have difficulties finding investment capital or companies are reluctant to invest in employee training. State aid may also be necessary to achieve policy goals such as regional economic development or environmental protection. Governments can, for instance, use state aid to stimulate businesses to invest in poorer regions or to purchase advanced environmentally friendly technologies.

1.1 Is it state aid?

There are four key questions to determine whether an aid measure involves state aid (i.e. whether state aid rules apply). Note however that **the presence of state aid does not automatically mean that a measure is prohibited**. Rather, the authorities need to ensure that the proposed measure is legal. This can be done, for example, by demonstrating that the aid measure is covered by an exemption to the rules, or by seeking the approval of the European Commission (EC).

State aid is when public organisations support certain enterprises or industries, financially or by other means.

State aid can be legal or illegal.

¹ Department for Business, Energy and Industrial Strategy, [The state aid manual](#), July 2015, p6

For any assistance provided by EU Member States, if the answer to all of the following questions is 'yes', then the measure involves state aid. Conversely, if 'no' is the answer to at least one of these questions, then the measure does not involve state aid (i.e. state aid rules do not apply).²

1. Does the aid **favour certain undertakings** (such as companies) or the production of certain goods?
2. Is aid **provided through state resources**?
3. Does the aid distort or threaten to **distort competition**?
4. Could the aid **affect trade between Member States**?

These four questions are explained in more detail below:

1. Does the aid give an **advantage to certain undertakings** (such as companies) or the production of certain goods?

The state aid rules apply if the aid provides financial assistance to an organisation or group of organisations. Normally the rules apply to assistance provided to companies, but assistance to third sector organisation (such as charities) can also be considered state aid.

Assistance to individuals is not considered state aid. Assistance such as tax measures which apply to all businesses equally, are not considered state aid. However, if the assistance applies to a specifically defined type of businesses (for example, businesses in a certain area, or businesses of a certain size) then it will count as state aid. Indirect financial assistance (such as exemption from a certain charge or fee) will also count as state aid.

There is no state aid advantage to a particular company if a public body behaves (purchases, sells, invests, lends etc.) like a private business would do, in similar circumstances (this is called the [Market Economy Operator \(MEO\)](#) principle).³ For example, a local authority can inject capital in a business expecting the same returns as a commercial investor. It can also provide a loan to a company at an interest rate that would be acceptable to a commercial lender. If the local authority can demonstrate that the MEO is met, there is no state aid.

2. Is aid **provided through state resources**?

The rules apply if the assistance is provided by any organisation that is controlled by a Member State. This includes non-departmental public bodies, executive bodies, as well as government departments and local authorities.

² Department for Business, Energy and Industrial Strategy, [The state aid manual](#), July 2015, p6. Article 107(1) of the [Treaty on the Functioning of the European Union \(TFEU\)](#) contains the definition on state aid.

³ European Commission, [Commission Notice on the notion of State aid as referred to in Article 107\(1\) of the TFEU](#), 19 July 2016, OJ C 262, p17

The form of state support is not decisive. It can be a grant to a company, a loan or a guarantee below market rates, a tax relief scheme, sale of public property at a discounted rate or free consultancy advice and more.

3. Does the aid distort or threaten to **distort competition**?

If the assistance strengthens the position of a company within a particular market, relative to other companies operating in that market, then the assistance distorts or could distort competition in that market.

Since the EU operates a free trade area involving other Member States, assistance which strengthens the position of all companies in a particular sector within one country would be considered state aid since these companies may operate in a market involving companies in other Member States.

4. Could the aid **affect trade** between Members States?

This condition is interpreted broadly. If the good or service benefitting from the aid could possibly be traded between Member States, then the assistance is considered to affect trade.⁴

To reiterate, if the answer to all of the above questions is 'yes', then the assistance would be considered a state aid measure by the EC. For the aid measure to be legal, the EC's approval would have to be sought, unless it can be demonstrated that the policy is covered by at least one of the exemptions outlined below. If an exemption applies, then there is no need to seek the EC's approval.

1.2 Exemptions

There are three categories of exemptions to state aid rules. If any exemption applies to a state aid measure, then the assistance is normally permitted without the need to seek the EC's formal approval, although some requirements regarding transparency and reporting apply. These categories are the *de minimis* rule; individual aid under schemes that have already been approved by the EC; and the General Block Exemption Regulation.

De minimis rule

According to the *de minimis* rule small amounts of assistance are exempt from state aid rules. Any aid that is worth less than €200,000 per business over three years is allowed by the EC.⁵ The threshold is lower in two sectors: €100,000 in the road transport sector, and €15,000 for agriculture.

State aid that is covered by one of these 'exemptions' is legal...

⁴ Department for Business, Energy and Industrial Strategy, [The state aid manual](#), July 2015, pp7-8

⁵ European Commission website, [State aid procedures \(accessed on 5 November 2018\)](#)

In order to be covered by the *de minimis* rule, the value of the aid must be “transparent” – that is, precisely calculable in advance. This means that aid which requires any form of risk assessment in order to determine its monetary value is not exempt under the *de minimis* rules, regardless of how small the amount of assistance is.⁶

Aid under an approved scheme

The EC can approve state aid schemes by giving its consent to a policy framework, maximum amounts and conditions of aid, as well as types of beneficiaries of these schemes. When public organisations grant assistance to companies under such a pre-approved scheme they will normally be exempt from a prior notification.

Various UK state aid schemes fall into this category, for example the [Enterprise Management Incentive](#) scheme, which helps SMEs attract and retain skilled personnel, and the [Enterprise Investment Scheme](#), whereby state aid is used to promote investment in smaller knowledge-intensive companies.⁷

General Block Exemption Regulation

State aid with the following aims is included in the General Block Exemption Regulation (GBER) and is exempt from prior notification. Block exemptions exist for aid that promotes:⁸

- **Small and medium sized enterprises (SMEs).** Aid which overcomes market failures that prevent SMEs from starting and thriving is allowed. This aid often takes the form of assistance to invest, take on new workers or cover intellectual property costs.
- **Research, development and innovation.** Aid that allows the EU to move towards a ‘knowledge-based economy’ is allowed. This can include assistance with patent costs, technical feasibility studies or development projects.

Beyond traditional research and development, aid is also exempt from state aid rules if it assists in the creation of innovative enterprises, advisory services or support services.
- **Employment and training, especially for disadvantaged residents and workers with disabilities.** Aid for training workers is generally allowed. Aid which helps disadvantaged workers into employment is also allowed. This aid often takes the form of assistance to employ people with disabilities, provide training or establishing family friendly leave/pay systems. Aid for the transport of workers who live in remote regions is also allowed.
- **Regional aid.** One of the key objectives of the EU is to raise the quality of life of citizens in disadvantaged regions of the Union.

⁶ Department for Business, Energy and Industrial Strategy, [The state aid manual](#), July 2015, p20

⁷ Pre-approved UK state aid schemes are registered in the [EC State aid database](#).

⁸ [Council Regulation \(EU\) 2015/1588, OJ L 248, 13 July 2015](#), Article 1

Aid is allowed if it “enhances economic cohesion” by helping the development of less developed areas (see the box on Regional state aid).

- **Infrastructure aid.** Aid for investment in local infrastructure and broadband, sport and multifunctional recreational infrastructure is allowed.
- **Environmental protection.** Aid which favours environmental protection or measures to tackle climate change is exempt from state aid rules. In particular, investments in energy savings, investments in renewable energy and environmental tax reductions are allowed.
- **Aid for culture and heritage conservation.** It is for Member States to define what they consider cultural or natural heritage.
- **Aid to make good the damage caused by natural disasters.**

The detailed rules and limits on the aid that is allowed under each of the different block exemptions can be found in [Commission Regulation \(EU\) No 651/2014 of 17 June 2014](#).

Regional state aid

Authorities can give state aid to support investment and employment in less advanced regions of the EU, thereby contributing to more balanced economic development within and between EU Member States. Regional state aid is restricted to eligible geographical areas which Member States record in their regional aid maps. The most recent map for the UK is available on <http://www.ukassistedareamap.com/>.

According to the EC’s [Regional Aid Guidelines](#) Member States can grant state aid to companies in the designated areas to support investment in new production or modernisation of existing facilities. The guidelines limit how much state aid companies can receive as a percentage of their costs.

Schemes targeting sensitive sectors like steel are not eligible. For other sectoral schemes, Member States have to demonstrate how those would be more beneficial than horizontal policies available to all sectors. Smaller schemes under the GBER do not need prior approval of the EC.

Regional aid is not intended to encourage relocation of firms from one Member State to another.

Regional state aid may not be awarded to firms in difficulty, as state aid for rescuing and restructuring of businesses is strictly limited in the EU and [specific guidelines](#) apply.

The UK has received EC’s approval for a wide range of aid schemes targeting assisted areas, for example the [Regional Growth Fund](#) in England and [Welsh Local Government Property Development Grant Scheme](#). Examples of local initiatives are [SCR Jessica Urban Development Fund](#) and [Business Growth Programme](#) in Yorkshire.

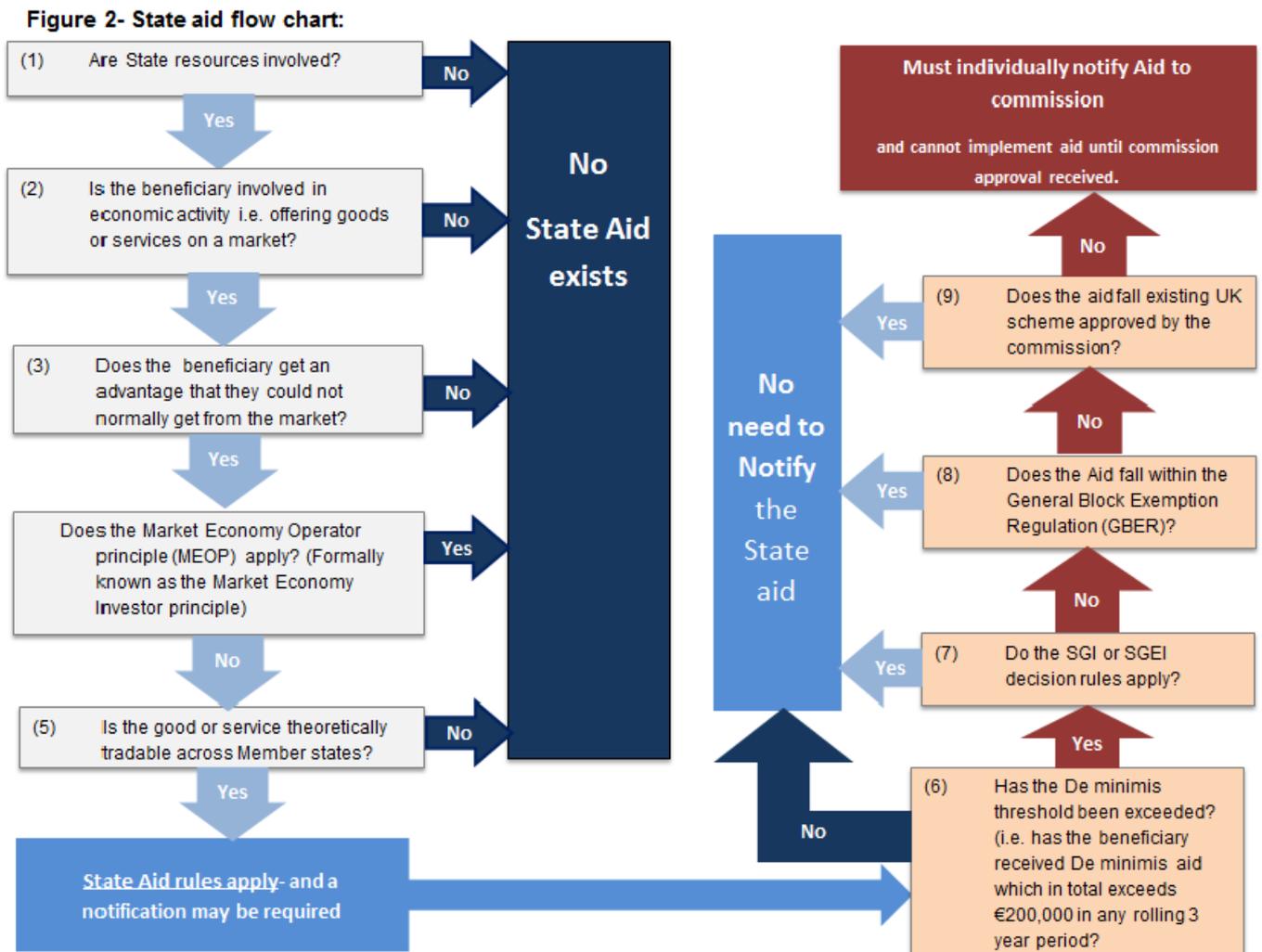
Export-related aid is not allowed

Aid for “export-related activities” is not allowed even if the assistance otherwise meets *de minimis* or GBER exemptions. Examples are aid directly linked to quantity of exported products or to setting up distribution networks. Support to attend trade fairs is allowed though.

Export-related aid is never allowed.

Further detail on GBER exemptions can be found in this EC publication, [General Block Exemption Regulation \(GBER\) Frequently Asked Questions](#).

The flow chart below summarises all that has been laid out so far:⁹



⁹ Department for Business, Energy and Industrial Strategy, [State aid: the basics](#), July 2015

1.3 Notifying the European Commission

If an instance of assistance is found to involve state aid, and none of the exemptions applies, then the EC must be formally notified to seek its approval for the aid measure.

Generally, the EC grants its approval based on whether the aid is:¹⁰

- The minimum necessary to remedy the failure (proportionate)
- Really changing the behaviour of the organisation that receives it (incentive effect)
- The best way to address the failure (appropriate)
- Beneficial enough to outweigh any negative effects on competition (balancing test)

1.4 How are state aids controls organised in the UK

Currently, the Department for Business, Energy and Industrial Strategy (BEIS) has the overall policy responsibility for state aid in the UK. It can advise local and regional authorities, as well as devolved administrations on their state aid measures. BEIS State Aid Team coordinates notifications to the EC submitted by other Government departments, agencies or authorities. The Department for Environment, Food and Rural Affairs (Defra) offers guidance on application of the rules to agriculture, fisheries and aquaculture. The Department for Transport (DfT) deals with matters related to state aid to transport.¹¹

Devolved administrations

Although state aid is not devolved, each of the devolved executives in Scotland, Wales and Northern Ireland have their own state aid units that offer advice and guidance, liaise with BEIS and represent devolved perspectives in state aid cases in Brussels.¹²

The ultimate authority to decide whether an aid measure involves state aid and when it can be permitted, rests with the European Commission.

¹⁰ Department for Business, Energy and Industrial Strategy, [State aid: the basics](#), July 2015, p8

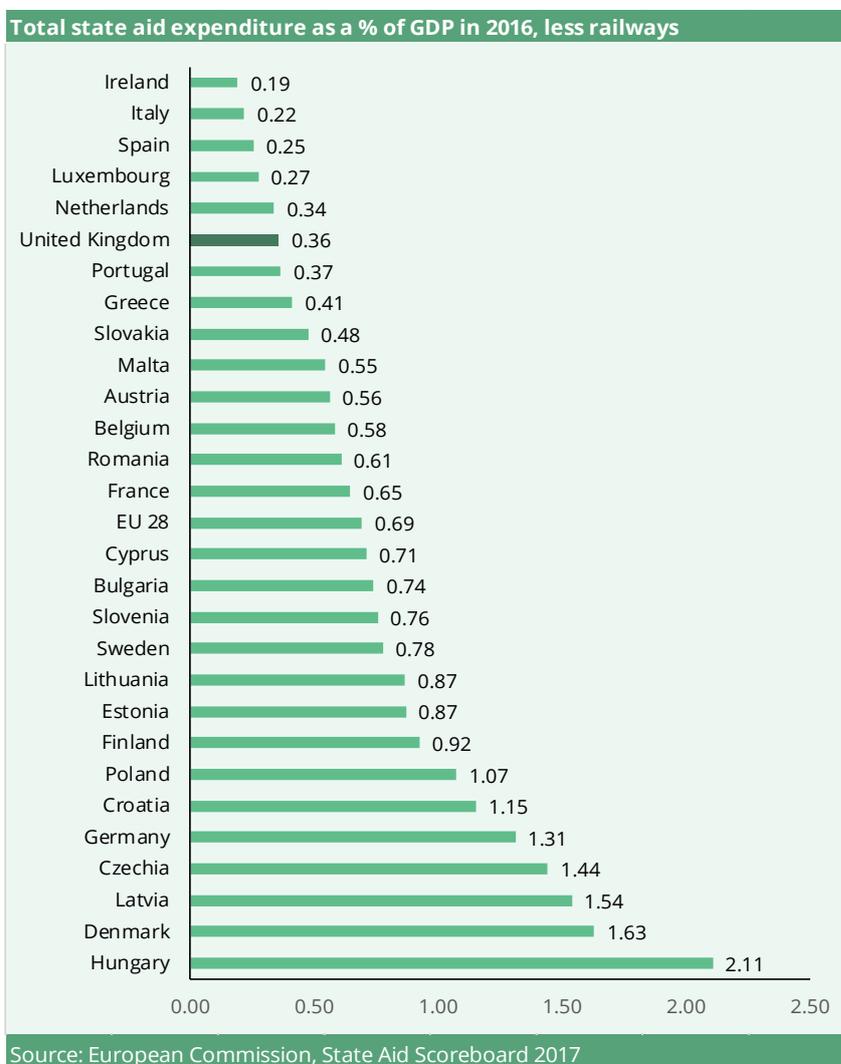
¹¹ Department for Business, Energy and Industrial Strategy, [State Aid Team website](#) (accessed on 5 October 2018)

¹² [Department for the Economy Northern Ireland](#), [State Aid Scotland](#), [Welsh Government State aid](#) (accessed on 5 October 2018)

1.5 Statistics

Statistics on approved state aid expenditure are collected in an annual [State Aid Scoreboard](#) by the European Commission.¹³ The latest Scoreboard shows that public organisations in the UK spend less directly and selectively supporting businesses than in most other EU countries. According to Member State expenditure reports, in 2016 the UK spent 0.36% of GDP on state aid schemes (excluding railways), while France spent 0.65% and Germany 1.31%.

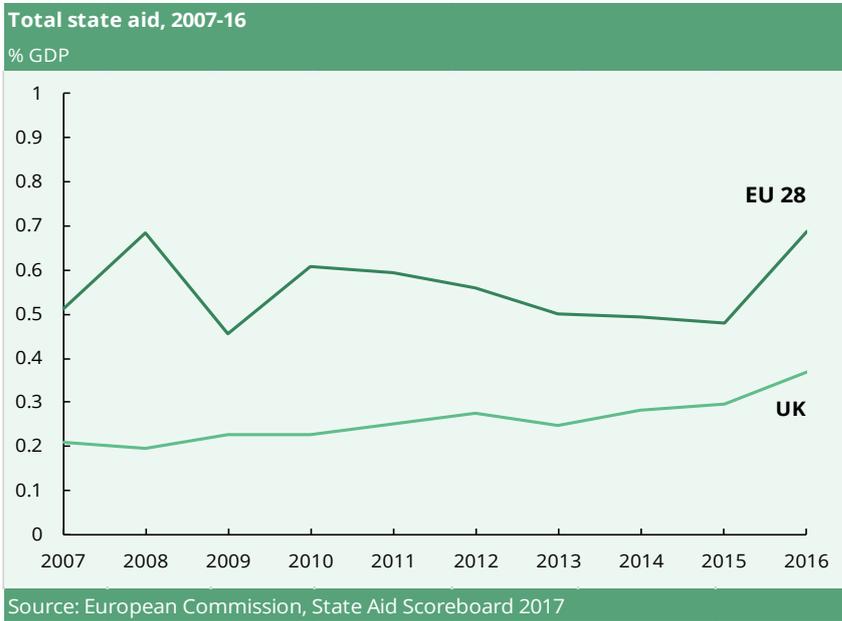
Data covers all existing state aid measures to industries, services, agriculture, fisheries and transport for which the EC adopted a formal decision. It also includes state aid which falls within the scope of the General Block Exemption Regulation (GBER). *De minimis* aid, aid to railways, measures in support of public services and crisis aid to the financial sector are not included.



¹³ European Commission, [State Aid Scoreboard 2017 website](#) (accessed on 5 November 2018)

14 EU State Aid Rules and WTO Subsidies Agreement

In the past, successive UK governments have spent less on state aid than most other EU countries. Over the 2007-2016 period, UK state aid as a percentage of GDP remained below the percentage of EU GDP as a whole.



2. WTO Agreement on Subsidies and Countervailing Measures

The vast majority of countries in the world are members of the [World Trade Organization \(WTO\)](#). The WTO is a forum where member countries agree on trade rules and resolve their trade disputes.

WTO member map, 2018



Source: www.wto.org

One of the key WTO agreements is the [Agreement on Subsidies and Countervailing Measures \(ASCM\)](#). This agreement lays out rules on the use of subsidies and on the actions countries can take to protect themselves from the effects of another country's subsidies.

[For the purpose of the ASCM, a subsidy is defined](#) as consisting of three elements:

- (i) A financial contribution (e.g., grants, loans, equity infusions, loan guarantees, fiscal incentives, the provision of goods or services, the purchase of goods, payments into funding mechanisms)
- (ii) by a government or any public body within the territory of a Member
- (iii) which confers a benefit.

To qualify, a subsidy must be 'specific', that is, it must be targeted at certain enterprises or industries.

All elements must apply for a subsidy to exist.

Under the Agreement, some subsidies are prohibited outright while the rest are 'actionable' – meaning that the subsidy is allowed, but other countries can take certain actions if the subsidy harms them. All subsidies fall into one or the other category.

- **Prohibited subsidies:** these are subsidies that require recipients to meet export targets, or to use domestic goods instead of imported goods. They are prohibited because they are specifically designed to distort international trade, and are therefore likely to hurt other countries' trade.

The WTO prioritises complaints about prohibited subsidies by handling them more quickly than procedures regarding actionable subsidies. If the dispute settlement procedure confirms that the subsidy is prohibited, the offending country must withdraw it immediately or face 'countermeasures' – a form of retaliation authorised at the WTO level. If the offending country does not withdraw the subsidy, the complaining country can impose a special tax on imports of the subsidised good to counteract the effect of the subsidy. This is called a 'countervailing duty'.

- **Actionable subsidies:** any subsidy that is not prohibited outright is allowed but 'actionable'. Most subsidies, such as production subsidies, fall into this category. Actionable subsidies can be challenged by other WTO countries if they hurt their domestic producers. The complaining country has to show that this is the case, otherwise the subsidy is permitted.

There are three types of harm that actionable subsidies can cause. First, one country's subsidies can hurt a domestic industry in an importing country. Second, they can hurt rival exporters from another country when the two compete in third markets. And third, domestic subsidies in one country can hurt exporters trying to compete in the subsidizing country's domestic market.

If the WTO's Dispute Settlement Body rules that the subsidy does indeed have harmful effects, the subsidy must either be withdrawn or its harmful effect removed. Again, countermeasures against the subsidy can be taken at the WTO level, and the complaining country can impose countervailing duties if its domestic producers are hurt by imports of the subsidized products.¹⁴

Countervailing duties are a tax on the imports of subsidised goods which makes these goods more expensive to buy. The principle behind these duties is to bring the market price of subsidised goods back up to what it would have been without subsidies. Doing so restores a level playing field between domestic producers and the imports they compete with.

To be allowed to impose countervailing duties, a country must carry out a detailed investigation to prove that certain imports are subsidised, and that these subsidies are hurting a domestic industry. Countervailing duties can usually be imposed for five years.¹⁵

Some subsidies are prohibited outright while the rest are 'actionable' – meaning that the subsidy is allowed, but other countries can take actions if the subsidy harms them.

Countervailing duties are a tax on the imports of subsidised goods which makes these goods more expensive to buy.

¹⁴ World Trade Organisation, [Understanding the Agreements website](#) and [SCM Agreement website](#) (accessed on 31 October 2018)

¹⁵ World Trade Organisation, [SCM Agreement website](#), (accessed on 29 October 2018)

There are **special rules for agricultural products**, which are more permissive of subsidies. The rules are set out in the [Agreement on Agriculture](#). The broad objective of the agreement is to secure reductions to the levels of support and protection in the agricultural sector.¹⁶

2.1 Comparing EU state aid and WTO rules

WTO rules on subsidies and EU state aid rules are two different frameworks. The EU rules are more stringent than the WTO's. Although the definition of a 'subsidy' under the ASCM is broadly similar to 'state aid' under the Treaty on the Functioning of the European Union (TFEU), the WTO rules are more limited in scope. The key differences are:

- 1 The default position in WTO rules is that subsidies not targeted at exports and/or import substitution are allowed, unless another country can demonstrate that these subsidies are hurting a domestic industry or trade in general; EU rules can apply domestically, as they consider state aid to be generally illegal, unless it falls within an exemption or has been approved.
- 2 The provisions of the ASCM only apply to goods, while EU state aid rules apply to any economic activity, including services.
- 3 EU rules are applied prospectively and do not need an official complaint from a Member State to be triggered. For instance, a public body planning to provide state aid must either satisfy itself that its scheme is exempted or seek the explicit approval of the European Commission *before* awarding any subsidy. WTO rules, on the other hand, are only reactive.
- 4 EU rules allow businesses and individuals to lodge a complaint to the Commission and to bring claims in national courts. The WTO rules rely on state-to-state enforcement. Private actors such as companies cannot complain to the WTO, so businesses who believe there has been a breach of the ASCM have to persuade their own government to take action.
- 5 The EU state aid rules are set up to remove anti-competitive effects through recovery of illegal state aid. The WTO offers dispute settlement mechanisms to terminate the subsidies or to offset them by allowing the importing country to introduce countervailing duties on subsidised imports.

EU state aid rules are a lot more stringent than WTO subsidies rules.

The report of the House of Lords EU Committee's Internal Market Sub-Committee [Brexit: competition and State aid](#) of 2 February 2018 examines the differences between the WTO rules on subsidies and the EU state aid regime in greater detail.¹⁷

¹⁶ World Trade Organisation, [Legal texts: Agreement on Agriculture website](#), (accessed on 29 October 2018)

¹⁷ European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, pp47-48

Statistics

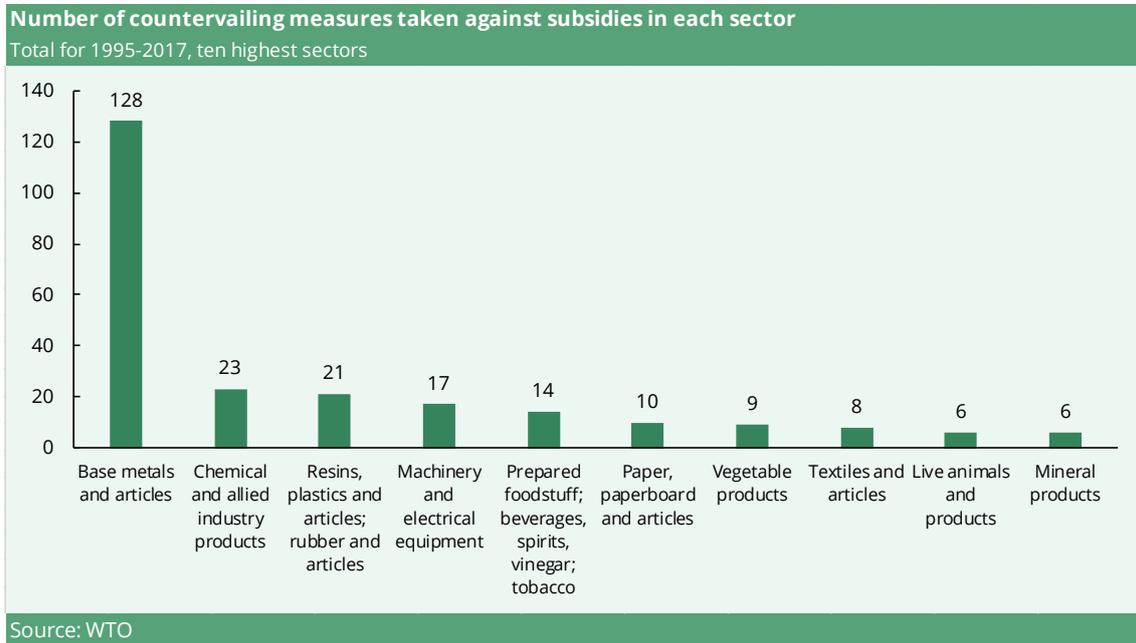
The [WTO publishes data](#) on the number of countervailing measures taken by countries (i.e. the imposition of countervailing duties on certain imports).

The data presented in the charts below cover the period from January 1995 to December 2017. The data comes from WTO members submitting reports for the relevant periods and may underrepresent the actual number of measures. Each measure reported covers one product imported from one country or customs territory.

Over the 1995-2017 period, the highest number of countervailing measures (84) was taken against China, which makes 33% of all measures taken during that period.



The second chart below shows countervailing measures by sector. Half of the total of 257 countervailing measures are taken against subsidies in the base metals and articles sector.



3. Implications of Brexit

This chapter discusses changes to the state aid framework in the UK, after the UK leaves the EU.

Summary

The absence of the EU state aid framework is not expected to translate into higher levels of direct support to businesses in the UK. Successive governments have favoured rigorous state aid controls. For statistical evidence that the UK gives less state aid than most other EU Member States see section 1.5 of this briefing.

However, pressure on the government to intervene might become more intense in the absence of the EU framework.

The extent to which EU state aid rules will apply in relations with the EU will be determined by the deal the UK and the EU agree. It is very likely that state aid provisions will be part of the agreement, not least because the EU has insisted on including some sort of controls on state assistance in almost every free trade agreement it has signed with other countries in the past, from association agreements with aspirational Member States like Ukraine to Free Trade Agreements with South Korea and Canada.

The Government is in favour of an independent UK state aid regime and is already working on creating one. It will introduce UK regulations to replace EU law and set up an independent body to police the system. Currently the EC assesses cases of state aid and may approve them, and has the power to enforce stringent 'claw-back' mechanisms. The Competition and Markets Authority (CMA) will become the UK's independent state aid authority to take over the role of the EC.

If the UK leaves the EU without a formal agreement on state aid rules, the WTO rules would still apply.

A future UK-EU trade deal is likely to include state aid rules.

3.1 Will state aid be part of the new relationship with the EU?

It is highly likely that state aid provisions will be part of the Brexit deal as both the UK and the EU have a mutual interest in restricting state support to businesses in order to ensure a level playing field.

The UK has long been a proponent of a rigorous state aid system and a leading advocate of the EU state aid framework development. The UK has been among the lowest granters of state aid as a proportion of Gross Domestic Product (GDP) in the EU. In 2016 the UK gave 0.36 per cent of GDP as state aid, half the EU average of 0.7 per cent.¹⁸

¹⁸ European Commission, [State aid scoreboard 2017 website](#) (accessed on 17 October 2018)

Theresa May's Government has repeatedly confirmed its willingness to maintain a rigorous state aid system after leaving the EU. It has argued that such a system is beneficial for taxpayers and consumers, and ensures an efficient allocation of resources:

- [The then Secretary of State for Exiting the EU](#) said in February 2018, that the rules of fair competition and restrictions on unfair subsidies would continue to underpin the UK-EU relationship.¹⁹
- The Prime Minister stated in her [Mansion House speech in March 2018](#): that the UK's and the EU's access to each other's markets should be on fair terms and to achieve this, commitments on state aid are inevitable:

"As with any trade agreement, we must accept the need for binding commitments – for example, we may choose to commit some areas of our regulations like state aid and competition to remaining in step with the EU's."²⁰

The EU has insisted on including some sort of controls on state aid in almost every free trade agreement it has signed, from association agreements with aspirational Member States like Ukraine to Free Trade Agreements (FTAs) with South Korea and Canada. The European Council's guidelines for negotiating UK's withdrawal from, and future relationship with the EU specify:

[..] Any agreement with the United Kingdom will have to be based on a balance of rights and obligations, and ensure a level playing field.

[..] The aim should be to prevent unfair competitive advantage that the UK could enjoy through undercutting of levels of protection with respect to, *inter alia*, competition and state aid, tax, social, environment and regulatory measures and practices. This will require a combination of substantive rules aligned with EU and international standards, adequate mechanisms to ensure effective implementation domestically, enforcement and dispute settlement mechanisms in the agreement as well as Union autonomous remedies, that are all commensurate with the depth and breadth of the EU-UK economic connectedness.²¹

3.2 The outlines of an independent regime

At present, the UK relies on the EU legal framework for state aid and enforcement by the EC. The government has considered several options for future regulation and has chosen to establish a full, UK-wide subsidy control framework after leaving the EU.

¹⁹ Department for Exiting the European Union, [David Davis' Foundations of the Future Economic Partnership Speech](#), 20 February 2018

²⁰ Prime Minister's Office, Prime Minister's Mansion House speech [On our future economic partnership with the European Union](#), 2 March 2018

²¹ European Council, [Guidelines following the United Kingdom's notification under Article 50 TEU](#), 23 March 2018, p3,5

The EU (Withdrawal) Act (EUWA) 2018 will preserve a general prohibition of state aid from “exit day” by transposing the existing EU law into UK legislative framework.²² The transposed rules will apply to all sectors, including agriculture, fisheries and transport and will mirror any existing exemptions from state aid rules. A UK body will get powers to maintain those rules.²³

However, EU state aid rules consist for a large part of the so called “soft EU law” – communications and guidelines, which explain how the EC interprets and applies EU state aid law. These are instrumental to deciding what kind of state aid is allowed. EU ‘soft law’ measures will not be retained by the EUWA 2018.²⁴ For example, the [Framework for state aid to research, development and innovation](#), and the [Guidelines on State aid for environmental protection and energy](#) fall within this category of ‘soft law’. Although the Government has said that its guidance will remain consistent with the EU’s, it is at the moment not clear how this part of EU state aid regulations will be mirrored.²⁵

A new state aid authority

The Competition and Markets Authority (CMA) will take on the new role of independent state aid regulator in the UK after Brexit. The Government argues that the CMA has the necessary experience and understanding of markets as the UK’s competition regulator and will be independent from government in its decision-making.²⁶

The CMA is set to become an independent state aid authority

An issue that has attracted attention is the state aid authority’s independence. Once the CMA has become the UK’s state aid regulator, it will have to decide on the legality of state aid proposed by the government and other public organisations. Although the CMA is used to independent rulings, given the political impact of a decision to give aid to specific sectors or companies, the CMA might experience unprecedented political pressure.²⁷

²² The EU (Withdrawal) Act 2018 of the Parliament repeals the European Communities Act 1972, preserves or transposes EU law into domestic law, and provides the UK government with certain powers to modify that law to ensure that it operates effectively on exit day.

²³ Letter from [Andrew Griffiths MP, Minister for Small Business, Consumers & Corporate Responsibility to the Chairman of the House of Lords EU Internal Market Sub-Committee](#), 28 March 2018

²⁴ [EU \(Withdrawal\) Bill: the Charter, general principles of EU law, and 'Francovich' damages](#), Commons Library Briefing Paper CBP-8140, 17 November 2017, para 4.3

²⁵ Slaughter and May, law firm, [“As State Aid Regime in the UK post-Brexit – a familiar regime or a step into the unknown”](#) [online], June 2018 (accessed on 10 October 2018)

²⁶ Letter from [Andrew Griffiths MP, Minister for Small Business, Consumers & Corporate Responsibility to the Chairman of the House of Lords EU Internal Market Sub-Committee](#), 28 March 2018

²⁷ Osborne Clarke, law firm, [“Post-Brexit regulation of State aid rules: UK government set out a framework for the future”](#) [online], 19 April 2018 (accessed on 16 October 2018)

The issue of the CMA's independence was debated in the House of Lords in May 2018, where Baroness Noakes noted that the Government appoint the board of the CMA and has issued a "strategic note" to the body potentially compromising its independence. The Government replied that the issue of independence is being considered.²⁸

Common rulebook on state aid

The Government's [White Paper on The Future Relationship between the United Kingdom and the European Union](#) of 12 July 2018 (also referred to as the 'Chequers' proposal) outlines how the EU-UK relationship regarding state aid could operate.²⁹

The Government proposes "an upfront commitment to maintain a common rulebook on state aid, enforced by the CMA". That entails continuous application of the existing EU state aid legal framework in the UK after Brexit. However, the UK reserves the right to seek some leeway with regard to state aid for farmers, and future changes in its procurement policy and tax regime:

This is without prejudice to the UK's intention to develop new tailored arrangements in relation to payments to farmers and other land managers for environmental benefits, and the UK's future public procurement policy.

The UK's proposal for its future economic partnership with the EU would not fetter its sovereign discretion on tax, including to set direct or indirect tax rates, and to set its own minimum tax rates.³⁰

The White Paper does not provide more detail on possible changes to tax or procurement policy.

The CMA would take over the European Commission's role of policing the implementation.

Committing to a common rulebook on state aid would require the UK courts "to pay due regard to CJEU case law, insofar as this was relevant to the matter before them." This would ensure that both the UK and the EU interpret rules consistently. But rights in the UK would be enforced by UK courts and in the EU by EU courts.³¹

At this point, it is unknown how much of this Government proposal will be included in the future EU-UK Agreement, but state aid appears to be one of the less contentious issues, as both sides are keen on preserving a level playing field for their businesses. Some way of adhering to common rules is possible. The section of this briefing "Other models for the UK-EU cooperation on state aid" discusses several options.

²⁸ HL Deb [24 May 2018](#), c1089

²⁹ HM Government, [White Paper on The Future Relationship between the United Kingdom and the European Union](#), Cm 9593, 12 July 2018

³⁰ *ibid*, para 1.6.1, paras 111-112

³¹ *ibid*, para 4.4.2

Transition period

If the UK and the EU agree the terms of the withdrawal, a transition period will begin. During this period, the Government intends to continue the application of the EU state aid rules and regulations. The EC would continue to assess and approve UK state aid.³²

The EC will continue to assess UK state aid during transition

The CMA would presumably acquire jurisdiction over UK's state aid cases from the end of the transition period. The status of pending cases which would be under the EC's assessment at that moment, is still subject to negotiation.³³ For example, the EC might finish pending assessments, UK authorities might be asked to start a new notification with the CMA or the CMA might take over pending investigations.

The sensitivity of such a settlement is illustrated by the fact that the EC is currently investigating several high profile cases with respect to a UK's tax exemption scheme for multinationals and a corporate tax regime in Gibraltar.³⁴

Leaving without a deal

For the eventuality of a no-deal Brexit on 29 March 2019, the Government is preparing to have a UK-wide state aid framework in place. It is planning to present secondary legislation under the Withdrawal Act in autumn 2018. This legislation would replicate the existing EU regime. In the beginning of 2019, the CMA is expected to publish its own guidance on the new state aid regulations.³⁵

In case of a no-deal, the Government plans to have a UK-wide state aid regime in place

After leaving the EU, UK public organisations would have to notify their state aid measures to the CMA, instead of the European Commission. Any previously approved state aid measures would retain their status. Any pending notifications to the EC would need to start a new approvals process with the CMA. Businesses would also be able to submit their complaints about allegedly unlawful cases of state aid to the CMA.³⁶

The timescale for this scenario is tight. The National Audit Office has noted that "any further compression of the legislative timetable will

³² Department for Business, Energy & Industrial Strategy, [Government response to the House of Lords EU Internal Market Sub-committee report on the impact of Brexit on UK competition and state aid](#), 29 March 2018, p2

³³ Competition and Markets Authority, a speech by Michael Grenfell, Executive Director, "[A view from the CMA: Brexit and beyond](#)", 16 May 2018

³⁴ Skadden, law firm, "[UK Plans to Maintain State Aid Regime Post-Brexit](#)", [online], 30 August 2018; See also European Commission, "[Potential state aid scheme regarding UK CFC Group Financing Exemption](#)", 26 October 2017, European Commission, "[State aid: Commission extends in-depth investigation into Gibraltar corporate tax regime to include tax rulings practice](#)", 1 October 2014.

³⁵ Department for Business, Energy & Industrial Strategy, guidance [State aid if there's no Brexit deal](#), 23 August 2018

³⁶ *ibid*

place pressure” on the plans of the CMA to be ready for the new regime.³⁷

In case the UK exits the EU without a formal agreement on state aid rules, the WTO rules on subsidies and countervailing measures would still apply.

Domestic reform

The working of the current EU state aid controls has attracted some criticism, notably more about the procedures and a strict interpretation of rules than the substance of the law. Designing a new regime, the UK might address some of these issues.

For example, the House of Lords EU Internal Market Sub-Committee report [Brexit: competition and state aid](#) mentions lengthy notification processes in Brussels, as it currently can take six months and more to get the Commission’s approval. Also, local governments often face disproportionately high costs of external legal advice in relatively small cases.³⁸

The House of Lords EU Internal Market Sub-Committee has recommended that “the Government should take into account calls from local authorities for a less complex and burdensome approval process than under the current EU regime.”³⁹

Time constraints may – at least in a short term – restrict any reform beyond integration of existing rules into the UK legislation, but adjustments are possible later.

In the long run, domestic pressure on the Government of the day for a more interventionist industrial strategy may increase, triggering greater use of state aid measures at all levels of government. Doing so however, the UK would have to weigh carefully the costs and/or potential retaliatory measures from other countries if they were to suffer from more subsidies in the UK.⁴⁰ The House of Lords EU Internal Market Sub-Committee said:

“Should the Government respond by significantly increasing state aid to UK businesses, this could undermine the UK’s ambition to become an open, global trading nation.”⁴¹

³⁷ National Audit Office, [Exiting the EU: Consumer protection, competition and state aid](#), 6 July 2018, HC 1384, p31

³⁸ European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, para37-42, paras 89-193, para 219

³⁹ *ibid*, paras 37-42, paras 89-193, para 219

⁴⁰ CMS, law firm, [“Brexit and State aid – can the WTO fill the gap?”](#), [online], 6 November 2017 (accessed on 29 October 2018)

⁴¹ European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, par217

3.3 The role of devolved administrations

The UK Government views state aid as a reserved matter⁴² and is in favour of a framework which would apply to the whole of the UK. A core argument is the need to prevent distortion of competition between various parts of the UK or a domestic subsidy race among the different authorities willing to attract relocating businesses from other parts of the UK.

It has been argued that, at the same time, state aid policy might be seen as a natural extension of the devolved executives' existing powers in relation to economic development and local government.⁴³

From the point of view of the devolved administrations, state aid is one of the areas where the division of competences with the central Government is disputed.⁴⁴ Scottish and Welsh governments have emphasized that any new state aid regime should be designed "in close partnership" with devolved administrations. They argue that to safeguard the interests of devolved administrations, the independence of a UK state aid authority would be essential.⁴⁵ The House of Lords EU Internal Market Sub-Committee, has concluded:

The Government should ... involve and secure the support of the devolved administrations in this process, including in agreeing the terms of reference, remit and priorities of any new UK State aid authority. It was made clear to us that any approach where the UK Government was perceived to be both 'rule maker' and 'rule taker' would probably be unacceptable to local and devolved governments.⁴⁶

Negotiations between the Government and the devolved administrations on this matter are ongoing.

3.4 Opposition views on state aid

Jeremy Corbyn, the leader of the Labour party has said that Labour wants to see more government spending in the UK:

⁴² HM Government, working document [Frameworks analysis: breakdown of areas of EU law that intersect with devolved competence in Scotland, Wales and Northern Ireland](#), 9 March 2018

⁴³ Slaughter and May, law firm, "[As State Aid Regime in the UK post-Brexit – a familiar regime or a step into the unknown](#)" [online], June 2018 (accessed on 10 October 2018)

⁴⁴ [Implications for Scotland of leaving the EU](#), Commons Debate Pack CDP-2018-0166, 28 June 2018, p14

⁴⁵ European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, [Ev CMP0043](#) and [Ev CMP0039](#); [Welsh Government Response to the Response from the UK Government to the House of Lords EU Internal Market Sub-Committee Report on Brexit: Competition and State Aid](#), 20 July 2018

⁴⁶ European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, paras 189-193, para 251

We have made clear we would seek exemptions or clarifications from EU **state aid** and procurement **rules** where necessary as part of the Brexit negotiations to take further steps to support cutting edge industries and local businesses.⁴⁷

The Labour party pledged in its [2017 Manifesto](#) to bring more public ownership into the railways, the utilities and the Royal Mail.

EU law is generally neutral with respect to property ownership.⁴⁸ State aid rules require though that all companies or utilities, regardless of their ownership structure, play by the same rules. It means for example that any rescue aid to failing state-owned companies must be backed by a sound restructuring plan designed with long-term viability in mind. See Library briefing paper on [Public ownership of utilities and services](#) (Section 7).

Aid in support of certain industries can be justified under the current regime, where there is evidence that the market fails to deliver on policy objectives, for instance investment in research and development falls short, or SMEs have difficulties accessing investment capital. (See section 1.2 of this briefing.) Several academics and lawyers have written that EU state aid rules do not need to be an obstacle to Labour's plans; with certain adjustments to the way state aid is given, it is likely that such measures could be structured to be cleared.⁴⁹

3.5 Other models for the UK-EU cooperation on state aid

Although both the EU and the UK have put forward proposals regarding future relationship with respect to state aid, it is not clear what the final agreement on this will be.

Trade agreements between the EU and third countries include varying degrees of controls on state aid. In general though, the closer the market integration, the more state aid rules form part of the agreement.⁵⁰

One can distinguish between 'parallel systems' substantially equivalent to EU state aid regulation and 'WTO-plus' systems.⁵¹ Examples of parallel application are the European Economic Area (EEA) agreement

⁴⁷ ["Build it in Britain again" – Corbyn's full speech](#), LabourList.org [online] 24 July 2018

⁴⁸ European Commission, Staff Working Document, [Guidance Paper on state aid-compliant financing, restructuring and privatisation of State-owned enterprises](#), 10 February 2012, SWD (2012) 14 final

⁴⁹ Tarrant, A. and Biondi, A., ["EU law is no barrier to Labour's economic programme"](#), Renewal [online], 22 September 2017; Peretz, G., ["Calls for EU "commitments" on state aid are a fantastical solution to an imaginary problem"](#), *New Statesman* [online], 15 May 2018

⁵⁰ Morris Schonberg, ["Continuity or change? State aid control in a post-Brexit United Kingdom"](#), *Competition Law Journal* 47, 2017, p54

⁵¹ European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, [Ev CMP0029](#)

and EU trade agreements with countries like Ukraine which aspire to become EU Member States. The WTO-plus approach of building on the WTO ASCM rules is found in the EU FTAs with South Korea and Canada.

European Economic Area (EEA)

Norway, Iceland and Liechtenstein are members of the European Economic Area. The EEA is a free trade area in which the free movement of people, capital, goods and services is guaranteed between EEA members and EU members. EEA members are bound by many of the EU's economic rules, including state aid. The [EEA Agreement](#) essentially replicates the state aid rules as they are incorporated into EU law.⁵² However, state aid measures are assessed by the EFTA Surveillance Authority and not the European Commission.

EEA members are bound by many of the EU's economic rules, including state aid.

EU-Ukraine Association agreement

The Ukraine-EU Association Agreement could be another model for the type of parallel state aid system the EU might seek for its future relationship with the UK. Under this agreement, Ukraine has its own state aid regime and an independent authority to control it, but it applies all EU state aid rules in full. Both parties report to each other annually on the state aid each has granted.⁵³

Comprehensive Economic and Trade Agreement (CETA)

The EU-Canada Comprehensive Economic and Trade Agreement (CETA), with "multiple pluses", is often cited as a template for the future trade relationship with the EU. CETA does not contain any state aid provisions and would fall within the WTO-plus category. Instead, it reaffirms the partners' rights and obligations under WTO agreements.⁵⁴

The CETA deal between the EU and Canada builds upon the WTO rules on subsidies

Beyond WTO rules, CETA introduces the obligation to be transparent about subsidies to producers of goods, and to service providers. In addition, there is a consultation mechanism for the parties to discuss subsidies that may negatively affect trade between them.⁵⁵

These provisions can be seen as an extension of WTO principles, rather than anything like EU state aid rules.

Given the level of access to the EU Single Market, which the UK is seeking, it is more likely than not that any deep and comprehensive UK-EU free trade agreement will address rules on state aid.⁵⁶

⁵² EEA website, [State aid](#) (accessed on 1 November 2018)

⁵³ European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, para 178

⁵⁴ European Commission, [CETA chapter by chapter](#), December 2016, Chapter 3

⁵⁵ *ibid*, Chapter 7

⁵⁶ European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, para 215

About the Library

The House of Commons Library research service provides MPs and their staff with the impartial briefing and evidence base they need to do their work in scrutinising Government, proposing legislation, and supporting constituents.

As well as providing MPs with a confidential service we publish open briefing papers, which are available on the Parliament website.

Every effort is made to ensure that the information contained in these publicly available research briefings is correct at the time of publication. Readers should be aware however that briefings are not necessarily updated or otherwise amended to reflect subsequent changes.

If you have any comments on our briefings please email papers@parliament.uk. Authors are available to discuss the content of this briefing only with Members and their staff.

If you have any general questions about the work of the House of Commons you can email hcenquiries@parliament.uk.

Disclaimer

This information is provided to Members of Parliament in support of their parliamentary duties. It is a general briefing only and should not be relied on as a substitute for specific advice. The House of Commons or the author(s) shall not be liable for any errors or omissions, or for any loss or damage of any kind arising from its use, and may remove, vary or amend any information at any time without prior notice.

The House of Commons accepts no responsibility for any references or links to, or the content of, information maintained by third parties. This information is provided subject to the [conditions of the Open Parliament Licence](#).