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EU State Aid Rules and WTO Subsidies Agreement

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Contents:

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



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
World Trade Organisation Agreement on Subsidies and Countervailing Measures	5
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 Special rules for public services	11
There is no state aid if the following conditions are met:	12
1.4 Notifying the European Commission	14
1.5 How are state aids controls organised in the UK	14
Devolved administrations	14
1.6 Statistics	15
2. WTO Agreement on Subsidies and Countervailing Measures	17
2.1 Comparing EU state aid and WTO rules	19
Statistics	20
3. Implications of Brexit	22
Summary	22
3.1 Will state aid be part of the new relationship with the EU?	22
3.2 The outlines of an independent regime	24
The CMA becomes the new state aid authority	24
Domestic reform	26
3.3 The role of devolved administrations	27
3.4 Opposition views on state aid	28
4. Scenarios for state aid	29
4.1 Transition period	29
After the Transition period (<i>Common rulebook</i> on state aid)	29
4.2 Protocol on Ireland and Northern Ireland	30
Commentary	32
4.3 Leaving without a deal	33
4.4 Future models for the UK-EU cooperation on state aid	34
European Economic Area (EEA)	34
EU-Ukraine Association agreement	34
Comprehensive Economic and Trade Agreement (CETA)	35

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

The government is setting up an independent UK-wide state aid regime. 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 legislation. The substance of state aid regulations will not change. The *State Aid (EU Exit) Regulations 2019* will make the Competition and Markets Authority (CMA) the UK's independent state aid enforcement authority, in place of the EC. Public organisations will have to notify their state aid measures to the CMA.

No-deal scenario

If the UK leaves the EU without an agreement, the government intends to have the new UK-wide state aid regime functioning by the exit day.

Transition period

If the UK and the EU agree on a transition period, the EU state aid regulations will continue to apply during that time. The EC will continue to assess and approve UK state aid and will scrutinise allegedly unlawful UK aid, which was granted during the transition, for up to four years after its end date.

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

Northern Ireland “backstop”

The Protocol on Ireland and Northern Ireland foresees that the UK regulator will enforce EU state aid law in the UK, but the EC will monitor state aid which affects trade between the EU and Northern Ireland. The UK regulator will consult the EC on its state aid decisions and the EC will have standing in UK court cases in matters of state aid.

Future relationship

The extent to which EU state aid rules will apply in relations between the UK and the EU will be determined by the deal both agree. It is very likely that state aid provisions will be part of the agreement, not least because both sides are keen on preserving a level playing field for their businesses. Also, 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.

For example, 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.

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.

Separate state aid regulations apply to the financing of public services (so-called “Services of General Economic Interest”).

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 2017, the UK spent 0.38% of GDP on state aid (excluding railways), while France spent 0.76% 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 on [this page of the European Commission's website](#).

The full text of the WTO's Agreement on Subsidies and Countervailing Measures can be found on [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).

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

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

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.

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.

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

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.

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

***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.

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

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)

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

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, and their advisory 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. Aid is allowed if it "enhances economic cohesion" by helping the development of less developed areas (see box 1 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

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

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](#).

Box 1 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 the [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.

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

Export-related aid is never allowed.

1.3 Special rules for public services

In the EU legal framework public services are referred to as Services of General Interest. These include non-commercial services provided by the government, such as defence and public education, but also services which governments contract out to businesses but financially support their provision. The latter are called Services of General Economic Interest (SGEIs).

Under the EU law, SGEIs are economic activities which deliver outcomes in the overall public good that, in absence of public intervention, would not be available at all or would not live up to the desired standard in terms of quality, safety, affordability, equal treatment or universal access. Such services for example can include public utilities such as gas and electricity supply, postal services, public service broadcasting, rural transport, provision of social housing and more.

Public authorities can choose to define what they consider a service of general, public interest. Thus, SGEIs may refer to different services across the EU, depending on the market situation and policy choices in that particular Member State. However, the Commission and the Union's courts can determine whether a Member State has made a "manifest error" in defining something as an SGEI and giving it financial support which distorts the level playing field for businesses. The Court and Commission have found manifest errors in several cases, including:

- support to broadcasting organisations for activities related to advertising and e-commerce;⁹
- broadband networks limited to business parks and not benefiting the population at large,¹⁰ and
- port operations, i.e. the loading, unloading, transshipment, storage and movement which do not differ from other, commercial activities in ports.¹¹

These activities, although earmarked as SGEI, were not found to be different from purely commercial services and did not warrant financial support.

State aid rules and compensation for SGEI

In general, **state aid principles apply** to the [financing of SGEIs](#) in the same way as they apply to any other economic activity: public authorities should not excessively subsidise such services. This is because an undertaking which provides the service might use an overly generous compensation to cross-subsidise its other, commercial activities to the detriment of fair competition.

EU law refers to public services as "Services of General (Economic) Interest".

Member States are free to define what they consider a SGEI. The Commission guards against "manifest errors".

⁹ CJEU, C-195/06, Kommunikationsbehörde Austria (KommAustria)/ Österreichischer Rundfunk (ORF), 18 October 2007

¹⁰ Commission decisions on state aid [N 890/2006, France, SICOVAL](#), 8 March 2005 and [N 284/2005, Ireland, Metropolitan Area Networks](#), 10 July 2007

¹¹ CJEU, C-34/01 to C-38/01, Enirisorse, 27 November 2003

However, **a separate set of state aid rules** exists for SGEIs.¹²

There is **no state aid** if the following conditions are met:

- Public service obligations are clearly defined and explicitly entrusted to an undertaking which will provide the service;
- The amount of compensation is calculated using objective and transparent methodology and does not exceed the costs incurred.
- Finally, a provider is selected in a public tender. Alternatively, the level of compensation can be determined based on a bench-mark analysis of the costs of a typical well-run business.¹³

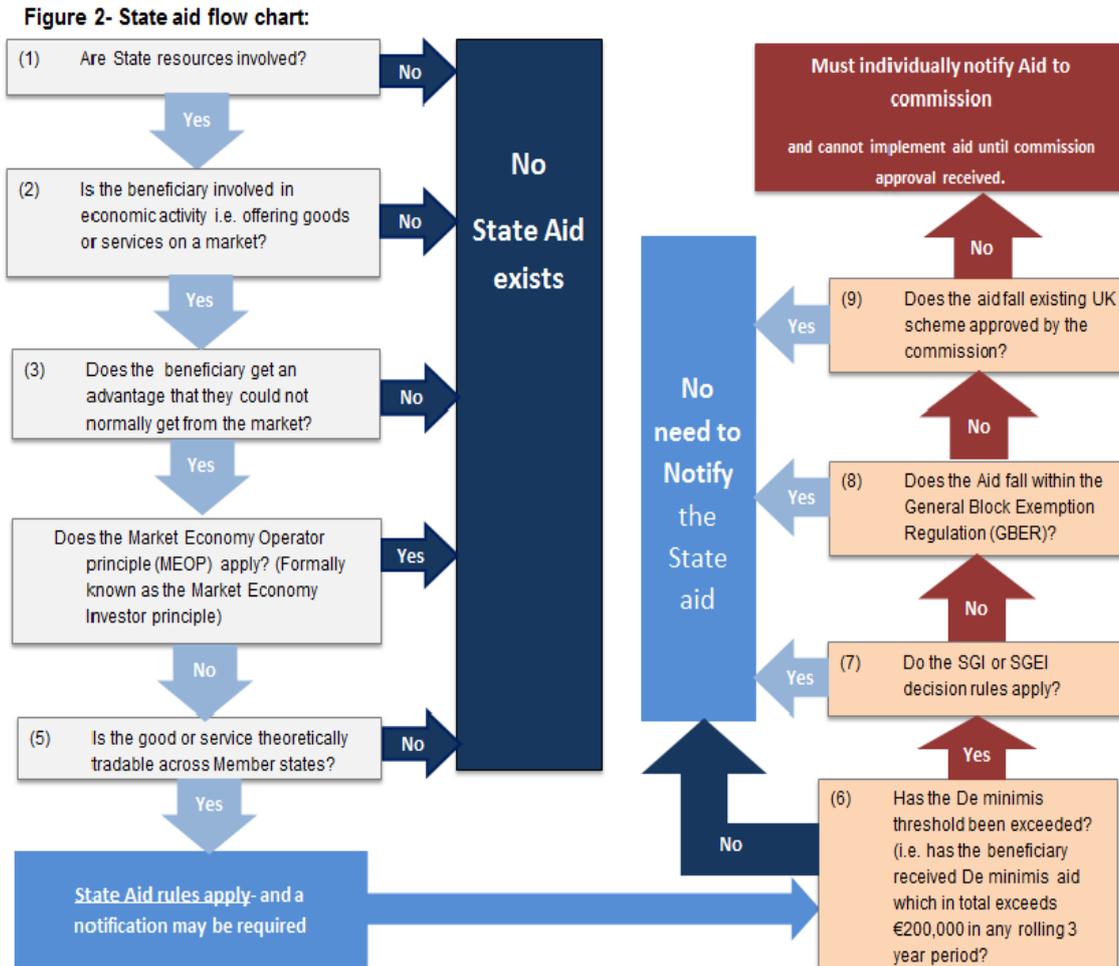
If one of the conditions above is not met, a compensation for an SGEI is considered state aid and has to comply to [SGEI state aid regulations](#); the higher the amount of support the more thorough the scrutiny by the Commission. State aid rules for SGEIs can be found on [this website of the Commission](#). These rules are also explained in more detail in chapter 7 of the [State Aid Manual](#) of the Department for Business, Energy and Industrial Strategy (BEIS).

A separate set of state aid rules applies to SGEIs.

¹² European Commission, [Guide to the application of the European Union rules on state aid, public procurement and the internal market to services of general economic interest, and in particular to social services of general interest](#), 29 April 2013

¹³ The Court of Justice of the EU set out these conditions in its [Altmark](#) judgement - Case C-280/00, 24 July 2003.

The flow chart below summarises all that has been laid out so far:¹⁴



¹⁴ Department for Business, Energy and Industrial Strategy, [State Aid: the Basics Guide](#), July 2015

1.4 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:¹⁵

- 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)

1.5 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.¹⁶

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 to state aid grantors, liaise with BEIS and represent devolved perspectives in state aid cases in Brussels.¹⁷

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

¹⁵ Department for Business, Energy and Industrial Strategy, [State Aid: the Basics Guide](#), July 2015, p8

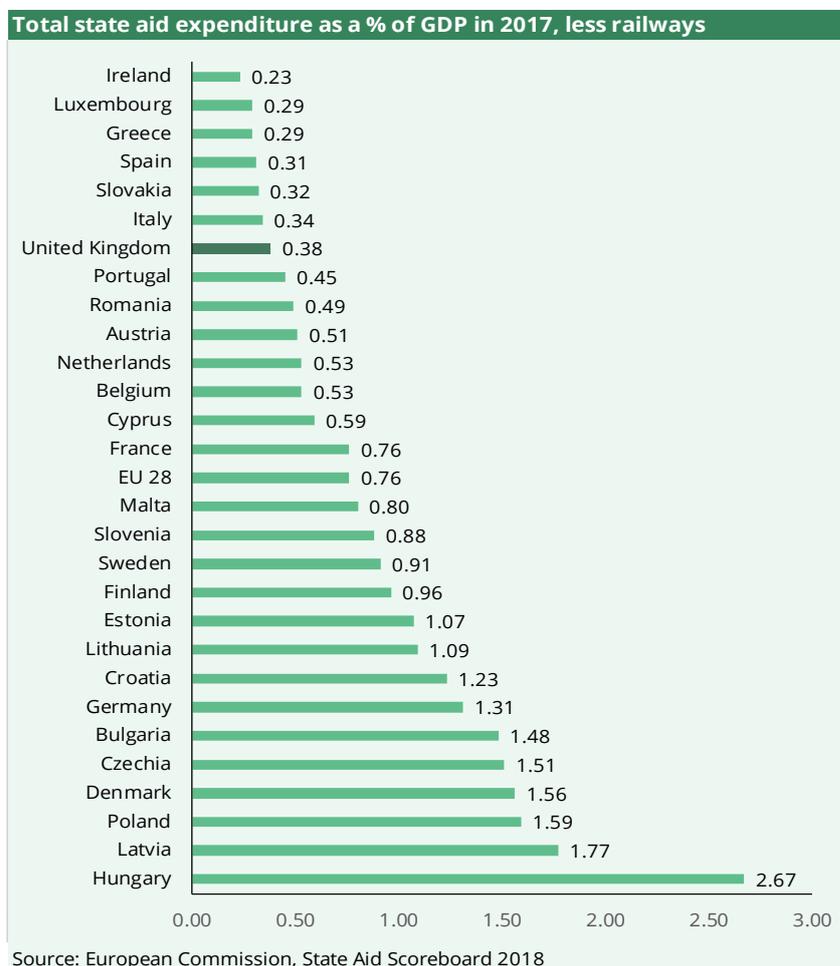
¹⁶ Department for Business, Energy and Industrial Strategy, [State Aid Team](#) website (accessed on 10 June 2019)

¹⁷ [Department for the Economy State Aid Unit Northern Ireland](#), [Scottish Government State Aid Team](#), [Welsh Government State Aid Unit](#) (accessed on 31 May 2019)

1.6 Statistics

Statistics on approved state aid expenditure are collected in an annual [State Aid Scoreboard](#) by the European Commission.¹⁸ 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 2017 the UK spent 0.38% of GDP on state aid schemes (excluding railways), while France spent 0.76% and Germany 1.31%.

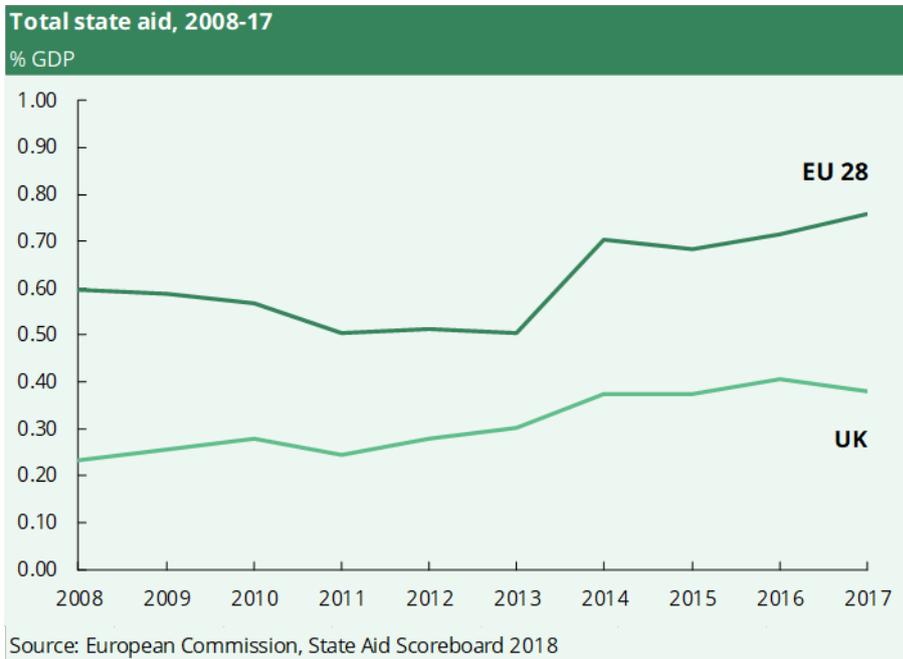
Data covers all existing state aid measures to industries, services, agriculture, fisheries and transport for which the EC adopted a formal decision. It also includes state aid which falls within the scope of the General Block Exemption Regulation (GBER). *De minimis* aid, aid to railways, measures in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



¹⁸ European Commission, [State Aid Scoreboard 2018 website](#) (accessed on 7 June 2019)

16 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 2008-2017 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, 2019



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 subsidised products.¹⁹

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

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.

¹⁹ World Trade Organisation, [Understanding the Agreements website](#) and [SCM Agreement website](#) (accessed on 31 October 2018)

that these subsidies are hurting a domestic industry. Countervailing duties can usually be imposed for five years.²⁰

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.²¹

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 trade, while EU state aid rules apply to any economic activity, including services and capital movements.
- 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

²⁰ World Trade Organisation, [SCM Agreement website](#), (accessed on 7 June 2019)

²¹ WTO, [Legal texts: Agreement on Agriculture website](#), (accessed on 7 June 2019)

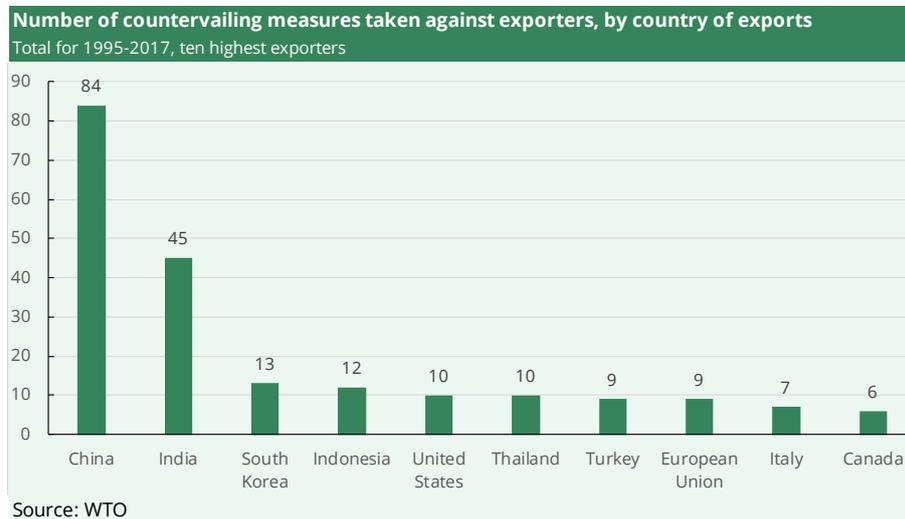
examines the differences between the WTO rules on subsidies and the EU state aid regime in greater detail.²²

Statistics

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

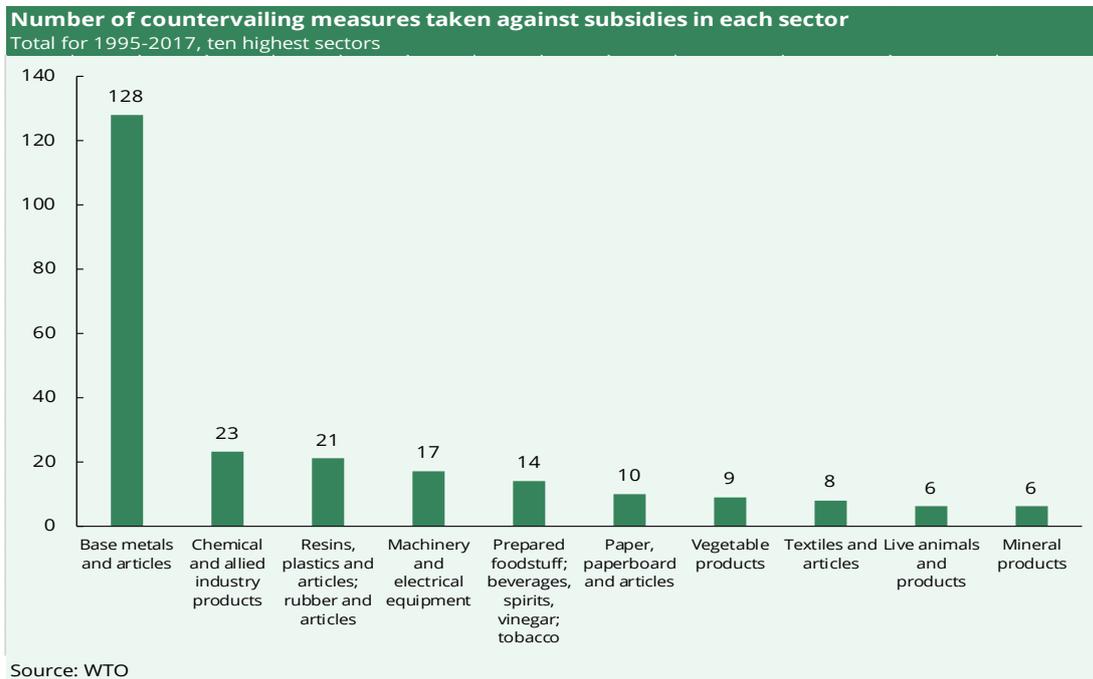
The data presented in the charts below cover the period from January 1995 to December 2017. The data comes from WTO members submitting reports for the relevant periods and may underrepresent the actual number of measures. Each measure reported covers one product imported from one country or customs territory.

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.



²² European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, pp47-48; a comprehensive comparison is given in L. Rubini, *The Definition of Subsidy and State Aid: WTO and EC Law in Comparative Perspective*, Oxford University Press, 2009

The 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 section discusses changes to the state aid framework in the UK, after it 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 1.6 of this briefing. However, pressure on the government to intervene might become more intense in the absence of the EU framework.

The government is working on an independent UK state aid regime. It is introducing UK regulations to replace EU law and setting up an independent body to police the system. Currently the EC assesses cases of state aid, 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, it will have its own state aid regime. The UK rules will largely preserve the EU state aid regulations as they were on the exit day. The WTO rules will still apply.

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 and a customs union with Turkey to Free Trade Agreements with South Korea and Canada. The question is how deep the alignment will be.

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.²³

Theresa May's Government has repeatedly confirmed its willingness to maintain a rigorous state aid system after leaving the EU. It has argued

²³ European Commission, [State aid scoreboard 2018 website](#) (accessed on 7 June 2019)

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.²⁴
- 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.²⁵

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. Also, the UK-Turkey customs union agreement contains state aid commitments.²⁶ 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.²⁷

State aid law experts Verouden and Ibanez Colomo emphasize that the question is not whether state aid controls will be part of the new UK-EU relationship but how deep this relationship will be with regard to policy coordination and enforcement, and what the institutional framework will look like.²⁸

²⁴ Department for Exiting the European Union, [David Davis' Foundations of the Future Economic Partnership Speech](#), 20 February 2018

²⁵ Prime Minister's Office, Prime Minister's Mansion House speech [On our future economic partnership with the European Union](#), 2 March 2018

²⁶ F. Hakura, [EU-Turkey Customs Union Prospects for Modernization and Lessons for Brexit](#), Chatham House briefings, December 2018, p2

²⁷ European Council, [Guidelines following the United Kingdom's notification under Article 50 TEU](#), 23 March 2018, p3,5

²⁸ V.Verouden, P. Ibáñez-Colomo, "[Ensuring a level playing field post-Brexit: State aid control](#)", 11 January 2019

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 Commission. The government is working to establish a full, UK-wide subsidy control framework after leaving the EU.

The *EU (Withdrawal) Act 2018* will preserve a general prohibition of state aid from “exit day” by transposing the existing EU law into UK legislative framework.²⁹ The rules will apply to all sectors, including agriculture, fisheries and transport and will mirror any existing exemptions from state aid rules.³⁰

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 and are instrumental to deciding what kind of state aid is allowed. 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. EU ‘soft law’ measures will not be retained by the *Withdrawal Act*³¹ and have to be transposed by secondary legislation.

The government has confirmed that its own guidance will remain consistent with the EU’s, including the ‘soft law’. For this purpose it has laid a new statutory instrument: the [State Aid \(EU Exit\) Regulations 2019](#) before [Parliament](#). Under this statutory instrument, a UK body, which the government has confirmed to be the Competition and Markets Authority (CMA), will receive powers to enforce state aid rules (see box 2 below).

The CMA becomes the new state aid authority

The Competition and Markets Authority (CMA) is set to take on the role of independent state aid regulator in the UK after Brexit.³² The government has argued that the CMA being the UK’s competition regulator has the necessary experience and understanding of markets and is independent from government in its decision-making.³³

Since its establishment in 2014, the CMA - an independent non-ministerial department - is the UK’s primary competition and consumer rights authority. It enforces business merger and anti-competition rules as well as consumer protection legislation.

The issue of the state aid authority’s independence has attracted considerable attention. Although the CMA is used to independent

The UK will preserve existing state aid rules in UK domestic law from exit day.

The CMA is set to become an independent UK state aid authority.

²⁹ 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.

³⁰ 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

³¹ [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

³² This will be postponed till the end of the transition period, in case the Withdrawal Agreement comes into force.

³³ 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

rulings, given the political impact of some decisions to support specific sectors or companies, the CMA might come under unprecedented political pressure.³⁴

Box 2 The State Aid (EU Exit) Regulations 2019

In January 2018, the government laid a new statutory instrument (SI), *The State Aid (EU Exit) Regulations 2019*, before Parliament under the draft affirmative procedure. The Regulations aim to ensure that a **domestic state aid** regime is in place on the day the UK's leaves the EU.

The *EU Withdrawal Act 2018* preserves most EU state aid law in principle as it is on exit day and allows to replicate the existing EU regime in domestic law. The State Aid Regulations 2019 make some technical modifications to the retained EU law as well as give the CMA powers to regulate and enforce the regime instead of the European Commission. Most decisions of the CMA will be subject to judicial review in the High Court (or the Court of Session in Scotland).

The Regulations do not materially alter the EU state aid rules. They allow the CMA to adopt all of the Commission's existing state aid guidelines, frameworks, communications and notices (the 'soft law'), as well as replicate the exemptions from state aid law, such as *de minimis* rules.

Committees of both Houses of Parliament have considered and debated the Regulations, including the CMA's powers and the role of devolved administrations in the new regime, but the final approval by the Commons is pending.

The Regulations will come into force on the exit day if there is no Withdrawal Agreement with the EU. Under the Withdrawal Agreement, the current EU regime will stay in place during the transition.

Under the *State Aid (EU Exit) Regulations 2019*, the CMA has the power to decide whether state aid proposed by the government, devolved administrations and other public bodies is legal. At the same time, the Secretary of State has power to issue guidance to the CMA on the assessment of state aid. This potential risk to the independence of the CMA's rulings was raised in the House of Lords in May 2018, and on several subsequent occasions.³⁵ The government responded that the guidance described in the *State Aid Regulations 2019* will draw on the Commission's current policy and will not substantially alter the way state aid is assessed now.

The CMA's role under the *State Aid Regulations 2019* has also raised some constitutional questions. If an Act of Parliament involves unlawful state aid, the CMA will not have the power to set this act aside. Only Parliament itself will have this power. (The Commission is currently able to rule Acts of Parliament illegal state aid).

At the same time, the CMA will have powers to declare an Act of a Scottish, Welsh or Northern-Irish parliament unlawful state aid and order its termination. State aid lawyer Peretz has pointed out:

³⁴ Osborne Clarke, law firm, "[Post-Brexit regulation of State aid rules: UK government set out a framework for the future](#)", 19 April 2018 (accessed on 30 May 2019); M.Holehouse, [Comment: State aid stand-off exposes UK regulator to heat](#), MLex, 30 April 2019

³⁵ HL Deb [24 May 2018](#) [Brexit: Competition and State Aid (EUC Report)], c1089; HL Deb [14 March 2019](#) [State Aid (EU Exit) Regulations 2019], c1161

The grant to what is, at the end of the day, an organ of the UK Government of such a power to set aside Acts of the devolved Parliaments may well be controversial.³⁶

The role of devolved administrations in the new state aid regime is discussed further in section 3.3.

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.³⁷

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."³⁸

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 (see section 3.4). Doing so however, the UK would have to weigh carefully the costs of potential retaliatory measures from other countries if they were to suffer from more subsidies in the UK.³⁹ 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.⁴⁰

³⁶ G.Peretz, [The State Aid \(EU Exit\) Regulations 2019: some initial comments](#), UKSALA website, 19 February 2019

³⁷ 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

³⁸ *ibid*, paras 37-42, paras 89-193, para 219

³⁹ CMS, law firm, "[Brexit and State aid – can the WTO fill the gap?](#)", [online], 6 November 2017 (accessed on 29 October 2018)

⁴⁰ 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 government and devolved administrations disagree as to whether state aid is a reserved matter.⁴¹

The UK government considers state aid regulation to be reserved and favours a single framework for 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.⁴²

The devolved administrations argue that state aid is an area where the division of competences with the UK government is disputed.⁴³ It has been argued that state aid policy might be seen as a natural extension of the devolved executives' existing powers in relation to economic development and local government.⁴⁴

Scottish and Welsh governments have emphasized that any new state aid regime should be designed "in close partnership" with devolved administrations.⁴⁵ Considering the statutory instruments for state aid, Welsh Brexit Minister has said that it was "not acceptable for UK government ministers to take unilateral decisions on matters which have a direct effect upon areas of devolved competency."⁴⁶ However the Minister said later that there is no disagreement on the substance of state aid policy and "that there is still scope to resolve the ongoing dispute between our administrations to reflect devolution in the medium to longer term..."⁴⁷

The UK government said on 10 April 2019 that the UK, Scottish and Welsh governments broadly agree to the development of a UK-wide post-Brexit regime that mirrors the EU regulations. It reiterated the commitment to working closely with the devolved administrations. It has been agreed that devolved administrations will be responsible for managing the communication between their respective aid givers and the CMA. The government has also proposed a memorandum of

⁴¹ HC [Delegated Legislation Committee, Draft State Aid \(EU Exit\) Regulations 2019](#), 10 April 2019, c19

⁴² *Ibid*, c1

⁴³ [Intergovernmental Agreement on the European Union \(Withdrawal\)](#), Memorandum, Annex A, 25 April 2018; for the context see [Implications for Scotland of leaving the EU](#), Commons Debate Pack CDP-2018-0166, 28 June 2018, p17

⁴⁴ Slaughter and May, law firm, "[As State Aid Regime in the UK post-Brexit – a familiar regime or a step into the unknown](#)", June 2018 (accessed on 31 May 2019)

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 [A letter from Counsel General and Brexit Minister Jeremy Miles, to Mick Antoniw AM Chair of the Constitutional and Legislative Affairs Committee 25 January 2019](#); see also a [letter from Mick Antoniw AM](#), Chair of the Constitutional and Legislative Affairs Committee of the National Assembly, to Lord Trefgarne, Chair of the Secondary Legislation Scrutiny Committee, 6 February 2019

⁴⁷ PQ 244064, [Government Assistance: Wales](#), 11 April 2019

understanding about the devolved administrations' role in the operation of the new regime.⁴⁸

Talks between the government and the devolved administrations of Wales and Scotland on this matter are ongoing. In absence of the Northern Ireland Executive, the government is engaged in technical consultations with the Northern Ireland civil service.

3.4 Opposition views on state aid

Jeremy Corbyn, the Leader of the Opposition, has said that Labour Party wants to see more government spending in the UK:

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.⁴⁹

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

In December 2018, Corbyn reiterated that in his view state aid rules need to be revisited:

I think the state aid rules do need to be looked at again, because quite clearly, if you want to regenerate an economy, as we would want to do in government, then I don't want to be told by somebody else that we can't use state aid in order to be able to develop industry in this country.⁵⁰

EU law is generally neutral with respect to property ownership.⁵¹ 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).

Certain types of state aid to any 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 mostly be structured to be cleared.⁵²

⁴⁸ HC [Delegated Legislation Committee. Draft State Aid \(EU Exit\) Regulations 2019](#), 10 April 2019, c7

⁴⁹ ["Build it in Britain again" – Corbyn's full speech](#), LabourList.org [online] 24 July 2018

⁵⁰ The Guardian, 'Corbyn: Brexit would go ahead even if Labour won snap elections', 21 December 2018

⁵¹ 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

⁵² A. Tarrant, A. Biondi, ["EU law is no barrier to Labour's economic programme"](#), Renewal [online], 22 September 2017; G. Peretz, ["Calls for EU "commitments" on state aid are a fantastical solution to an imaginary problem"](#), *New Statesman* [online], 15 May 2018

4. Scenarios for state aid

The state aid regime in the UK will be different depending on the future developments in the UK-EU relationship:

- a departure under the Withdrawal Agreement and a **transition period**, followed by a new treaty on future relationship;
- a **protocol on Ireland and Northern Ireland** (the so-called “backstop” arrangement) enters into force in case a new relationship is not agreed by the end of the transition; or
- a departure without an agreement (a ***no-deal scenario***).

The following sections discuss what these three scenarios will mean for state aid controls.

4.1 Transition period

If Parliament approves the [draft Withdrawal Agreement](#) (WA), a transition period will begin. Under the WA, state aid assessment will remain unchanged in the UK during the transition period. EU law will be applicable in the United Kingdom during the transition period and the UK will be treated as if it were a Member State for state aid purposes.⁵³

The Commission shall continue to be competent for **ongoing** state aid **procedures** which were initiated before the end of the transition period. Retaining the authority of the Commission during the transition is in line with the government’s position during the withdrawal negotiations with the EU.⁵⁴ This would allow the CMA to prepare for its future state aid role after the end of the transition.⁵⁵

Regarding UK aid granted before the end of the transition period, the Commission will be able to **initiate new procedures** that relate to alleged illegal state aid for a period of four years after the end of the transition and follow up on those procedures thereafter. The Commons Briefing Paper [The UK’s EU Withdrawal Agreement](#) gives more detail on this.⁵⁶

After the Transition period (*Common rulebook on state aid*)

Currently, there is less clarity about the future after a potential transition. The Government’s [White Paper on The Future Relationship between the United Kingdom and the European Union](#) of 12 July 2018

⁵³ V. Verouden, P. Ibáñez-Colomo, “Ensuring a level playing field post-Brexit: State aid control”, 11 January 2019, p21

⁵⁴ 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

⁵⁵ Competition and Markets Authority, a speech by Michael Grenfell, Executive Director, [“A view from the CMA: Brexit and beyond”](#), 16 May 2018

⁵⁶ Commons Briefing Paper [The UK’s EU Withdrawal Agreement](#), 4 December 2018, CBP 08453, Chapter 4.11

(also referred to as the ‘Chequers’ proposal) outlines how the EU-UK relationship regarding state aid could operate.⁵⁷

The Government has proposed “an upfront commitment to maintain a common rulebook on state aid, enforced by the CMA”. That entails continuous, dynamic 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.⁵⁸

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

Committing to a common rulebook on state aid would require the UK courts “to pay due regard to [Court of Justice of the EU] 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.⁵⁹

At this point, it is unknown how much of this government proposal on “dynamic alignment” could return 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.

Therefore, some way of adhering to common rules is plausible. Section 4.4 of this briefing discusses possible options.

4.2 Protocol on Ireland and Northern Ireland

Under the Withdrawal Agreement, if there is no agreement on the future relationship between the EU and the UK by the end of the transition period, the Protocol on Ireland and Northern Ireland (the so-called “backstop”) comes into effect.

Strong controls on state aid are included in the Protocol as part of the ‘level playing field’ commitments. In order to prevent undue distortion of competition and trade, the UK as a whole will continue to apply EU state aid regulations “in a way that is dynamically aligned to the development of those rules in the EU.”⁶⁰ This is roughly in line with the Government’s proposal of the *Common Rulebook*, as set out in the July 2018 White Paper (see section 4.1 above).

EU state aid law will continue to apply under the “backstop”. It will be policed by the Commission in Northern Ireland and by the CMA in the rest of the UK.

⁵⁷ HM Government, [White Paper on The Future Relationship between the United Kingdom and the European Union](#), Cm 9593, 12 July 2018

⁵⁸ *ibid*, para 1.6.1, paras 111-112

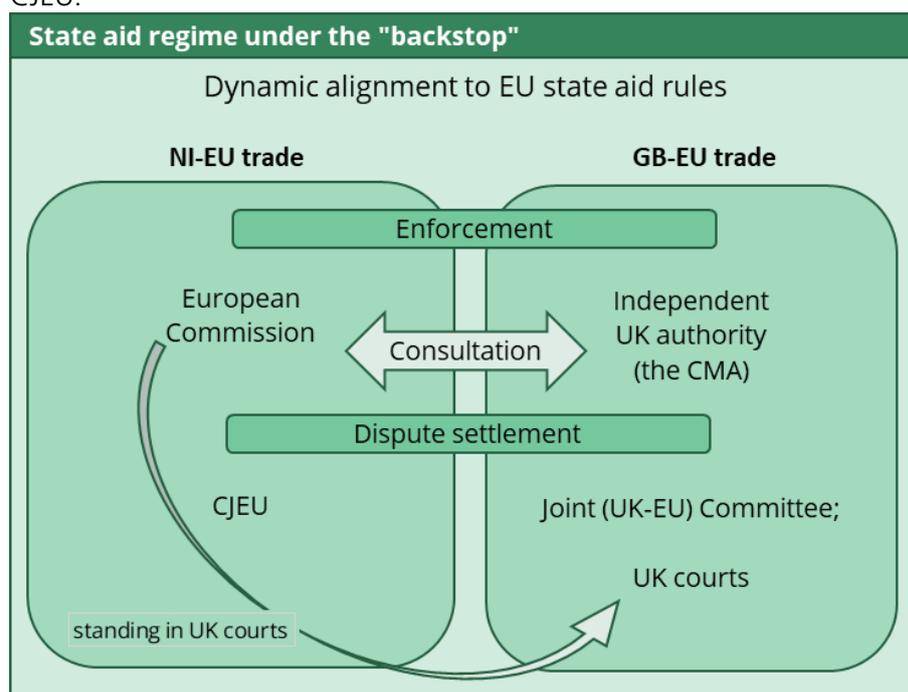
⁵⁹ *ibid*, para 4.4.2

⁶⁰ European Commission, [Fact Sheet Protocol on Ireland and Northern Ireland](#), 14 November 2018

However, state aid provisions will be enforced differently in Northern Ireland and Great Britain (see diagram below). The Commission will retain its authority over state aid measures which affect trade between the EU and Northern Ireland.

In Great Britain, EU state aid law provisions will also apply, but specifically to aid measures affecting trade between the EU and Great Britain. They will be enforced by an operationally independent UK authority which is “free from political or other external influences”. This role would presumably be fulfilled by the CMA. The Commission would have no jurisdiction over such measures. However, the Protocol requires that the UK authority works in close alignment with the European Commission, consults it before taking any formal decisions and “takes utmost account of [the Commission’s] opinion”.⁶¹

Under the Protocol, UK courts will supervise the CMA and the Commission will have standing before UK courts and right to intervene in cases. The Court of Justice of the EU (CJEU) will maintain its jurisdiction, particularly over the interpretation of EU state aid law and decisions of the European Commission. UK courts will be able to refer questions regarding the interpretation of EU state aid rules to the CJEU.⁶²



The Protocol contains a carve-out for state aid to agricultural sector. The maximum exempted annual level of support will have to be agreed in the UK-EU Joint Committee established under the Withdrawal Agreement.⁶³

⁶¹ The Northern Ireland and Ireland Protocol, 25 November 2018, Annex 4, Article 10.

⁶² *Ibid.*, Annex 4, Article 11. Global Competition Review writes though that UK courts seldom refer pre-judicial questions to the CJEU, as they generally consider themselves capable of resolving state aid issues directly. This is due to the available volume of national and EU case law and direct legislation. See Global Competition Review, an antitrust and competition law news service, '[Global Competition Review on State aid](#)', September 2018 [accessed on 31 May 2019].

⁶³ The Northern Ireland and Ireland Protocol, 25 November 2018, Article 12(2)

The provisions under the Protocol are described in more detail in the Commons Briefing Paper [The UK's EU Withdrawal Agreement](#) (sections 8.7 and 8.9).⁶⁴

Commentary

The Institute for Government has said that the powers the UK has given to the Commission in the field of state aid under the Protocol are particularly strong, which is an unusual feature in international agreements:

The UK has conceded a strong role for the Commission and the ECJ in Northern Ireland and given the Commission wide-ranging rights to ask for information and intervene in the way UK enforcement bodies are acting. Most notably in the area of state aid, the Commission can bring legal cases to UK courts – which is not usually a feature of international agreements.⁶⁵

State aid experts note that the provisions of the Protocol are at times ambiguous and could lead to legal disputes if ever applied. The Protocol creates a *de facto* customs union and covers trade in goods between the UK and the EU, but not trade in services. Therefore, it can be interpreted in a way that state aid regulations under the Protocol should only apply to trade in goods between the UK and the EU.⁶⁶ The Parliamentary Under-Secretary of State for the Department for Business, Energy and Industrial Strategy Lord Henley used this interpretation in a Lords debate on 14 March 2019.⁶⁷

Nevertheless, the European Commission has not referred to different application of state aid rules for goods or services trade under the Protocol, which implies that the Commission does not intend to differentiate. Moreover, the state aid in the EU refers to “any economic activity” (related to goods, services or capital) capable of affecting trade between Member States.

In practice, it would be very difficult to make a distinction between goods or services trade, or movements of capital. As a result, for example, UK aid to banks could affect manufacturers’ access to credit across the UK, including Northern Ireland, and might thus fall under the jurisdiction of the Commission and not only under the jurisdiction of the CMA.⁶⁸ Also, a UK government grant scheme which would be open to all UK businesses, including ones based in Northern Ireland, might as well fall under both regimes.

Further, it is not entirely clear to what extent the Protocol will protect UK-based businesses from the remaining EU Member States granting

⁶⁴ Commons Briefing Paper [The UK's EU Withdrawal Agreement](#), 4 December 2018, CBP 08453, Chapter 8.7

⁶⁵ Institute for Government, explainers, [The Northern Ireland and Ireland Protocol](#), [accessed on 31 May 2019]

⁶⁶ G. Peretz, [State aid and the withdrawal agreement: key points](#), UK State Aid Law Association (UKSALA) website, 3 December 2018

⁶⁷ HL Deb [State Aid \(EU Exit\) Regulations 2019](#), 14 March 2019, c1611

⁶⁸ M. Holehouse, [Comment: State-aid questions in Brexit backstop merit clarification](#), MLex, 8 February 2019

state aid to their own competing industries when the UK has left the bloc.⁶⁹ Others argue, that the Withdrawal Agreement provisions grant such protection to UK businesses.⁷⁰

The above issues could lead to complex legal disputes if the backstop was ever activated.

4.3 Leaving without a deal

For the eventuality of a no-deal Brexit, the government is preparing to have a UK-wide state aid framework in place. This new regime will preserve most EU state aid regulations as they were on the exit day. See the Department's for Business, Energy & Industrial Strategy [guidance on State aid if there's no Brexit deal](#) of 23 August 2018.

The *EU (Withdrawal) Act 2018* preserves EU state aid law in the UK. The [State Aid \(EU Exit\) Regulations 2019](#) will make the necessary procedural changes (see box 2 above).

The CMA will become the UK's state aid regulator. A new [CMA's guidance](#) explains what will change. For example, UK public organisations will have to notify their state aid measures to the CMA, instead of the European Commission. However, procedures are intended to be as similar to the current ones as possible.

Any previously approved state aid measures will retain their status. Any pending notifications to the Commission will need to start a new approvals process with the CMA. Businesses will also be able to submit their complaints about allegedly unlawful cases of state aid to the CMA.

In March, the CMA held a consultation on its [draft guidance](#) on state aid procedures and is currently analysing the feedback.

Although the *State Aid Regulations 2019* will apply if no withdrawal terms are agreed, they give an indication as to how the government envisages the setup of the UK domestic regime and the CMA's future role.

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

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

⁶⁹ *Ibid*

⁷⁰ Pursuant to Article 4(1). V. Verouden, P. Ibáñez-Colomo, "[Ensuring a level playing field post-Brexit: State aid control](#)", 11 January 2019, p22

4.4 Future 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 and whether the UK will to a certain extent follow the dynamic alignment with EU state aid law.

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.⁷¹

One can distinguish between ‘parallel systems’ substantially equivalent to EU state aid regulation and ‘WTO-plus’ systems.⁷² Examples of parallel application are the European Economic Area (EEA) agreement 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.⁷³ 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.⁷⁴

⁷¹ M. Schonberg, “[Continuity or change? State aid control in a post-Brexit United Kingdom](#)”, *Competition Law Journal* 47, 2017, p54; on comparison

⁷² European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, [Ev CMP0029](#)

⁷³ EEA website, [State aid](#) (accessed on 12 June 2019)

⁷⁴ European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, para 178

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 as such and would fall within the WTO-plus category. Instead, it mainly reaffirms the partners’ rights and obligations under the WTO Subsidies and Countervailing Measures agreement for goods, with a voluntary extension for services.⁷⁵

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.⁷⁶

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

If such a model is chosen for the future UK-EU state aid relationship, it is possible that both sides will seek extra guarantees that a similar degree of protection will be available to businesses in the UK and the EU. Verouden and others argue that such extra guarantees might resemble the template of the Protocol on Ireland and Northern Ireland, which includes such features as the Commission having standing in UK proceedings, requiring the UK authority to communicate its draft decisions or be transparent about its state aid.⁷⁷

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.⁷⁸

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

⁷⁵ European Commission, [CETA chapter by chapter](#), December 2016, Chapter 3

⁷⁶ *ibid*, Chapter 7

⁷⁷ V. Verouden, P. Ibáñez-Colomo, “[Ensuring a level playing field post-Brexit: State aid control](#)”, 11 January 2019, p23-24

⁷⁸ European Union Committee, Internal Market Sub-Committee, [Brexit: competition and State aid](#), 2 February 2018, HL 67 2017-19, para 215

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