Government Offices of Sweden
Ministry of Climate and Enterprise

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Regarding proposed changes to EU state aid rules

In a letter dated 13 January, 202[3], the Executive Vice-President of the European Commission, Margrethe Vestager, wrote to EU member states regarding revisions to state aid regulations.

In her speech at the World Economic Forum in Davos on 17 January, 2023, the President of the European Commission, Ursula von der Leyen, also spoke about proposed changes to state aid regulations.

The Confederation of Swedish Enterprise hereby presents its position on what was described and proposed by representatives of the Commission as mentioned above, in addition to [Swedish Enterprise's previous position paper regarding changes to state aid regulations dated 10 January 2023.]

Summary

- Swedish Enterprise continues to believe that the Commission's proposals, which are a response to the Inflation Reduction Act (IRA), are premature. It is imperative to analyse more carefully how the IRA will affect European businesses. This includes waiting for the guidelines that are expected to be published in March 2023.
- Another factor that points to the validity of waiting is that there is still no analysis of how the combined climate policies of the EU and the US distort competition.
- The proposals to further ease state aid rules are inappropriate. They risk increasing the already tangible distortions of competition that exist, where a small number of countries favour their businesses to a far greater extent than others. The proposals also risk increasing the complexity of the regulatory framework, administrative burdens, and in the long term, undermining Europe's competitiveness, dynamism and productivity.
- Proposed changes to the Temporary Crisis Framework (TCF) are inappropriate, as the Framework is temporary and unsuitable for forward-looking investment. The proposals risk overlapping with existing regulations and have an unclear legal basis in the Treaty on the Functioning of the EU (TFEU).
- Sensible proposals to make the regulatory framework simpler and processes faster are welcome if they do not in themselves result in a more watered-down regulatory framework and increased amounts of state aid. However, reviews of state aid notifications based on the TCF is already relatively fast. Swedish Enterprise is happy to take part in upcoming proposals on this point. Broadening state aid rules to cover all types of fossil-free energy seems reasonable in principle.
- The introduction of new support for green investment in strategic sectors where there is a risk of investment being taken out of the EU due to subsidies given in third countries is discouraged. There is a very real risk that this would lead to a state aid

race with the outside world. If such aid is introduced, it is vital that it is limited to investment aid, time limited, and that principles of proportionality, appropriateness and necessity are applied.

- IPCEI regulations should continue to be a limited complement to other state aid regulations. The regulation and effects of projects need to be evaluated to assess how regulations and processes can be improved.
- Pending more knowledge, the Commission should develop guidance/best practice based on its existing experience on how beneficiaries, authorities and member states should work with the IPCEI. Lengthy application processes are largely due to the fact that parties are unfamiliar with processes, that applications are substandard, and that other parts of the state aid rules would be more appropriate to use.
- It may also be worth considering the division of large integrated projects into smaller integrated sub-projects to a greater extent to reduce the need for co-ordination and administration.

Regarding the Inflation Reduction Act

It is clear that the main reason for the proposed amendments to state aid regulations is the US's IRA, and concern that it risks diverting investment from the EU to the US and will worsen opportunities for European businesses to export environmental technology to the US.

Swedish Enterprise would once again like to point out that there are discriminatory elements in the IRA, that these constitute barriers to trade, and that Swedish Enterprise opposes these. However, the proposals also have some clearly positive aspects and cannot be dismissed entirely.

The IRA is essentially a climate act. Its primary purpose is not to exclude European business. American authorities are working on guidelines for how the regulations are to be applied, and negotiations are ongoing between European and American representatives on whether certain terms in the regulations can be given a broad definition, which could include European businesses to a greater extent. There are already indications of success in these respects, and there are several other reasons why the IRA need not be so problematic as feared, and indeed, in several respects it could also offer opportunities for European businesses.

US and EU climate policy differs considerably. While both the US and the EU subsidise the green transition, the EU is also increasingly working with the polluter pays principle. In the next few years, EU businesses will increasingly be subject to the Emissions Trading System, (ETS), and prices for emission rights will increase as the number of emission rights decreases. In parallel to this, member states are entitled through existing state aid guidelines for ETS compensation to compensate sectors where there is a risk of carbon dioxide leakage. The overall picture of how conditions for competitiveness differ with regard to green investment and production between the US and the EU is difficult to assess and will also differ depending on which EU member states and US states are compared. As far as Swedish Enterprise is aware, there is a lack of a broad analysis that includes subsidies, taxes, and regulations on each side of the Atlantic.

This is why Swedish business as a whole does not believe that the IRA, based on what we currently know, justifies drastic measures. Rather, it demands thorough analysis of needs and consequences. The measures that have now been announced by the EU risk being counterproductive and threaten competition in the single market and long-term productivity gains.

Why the proposed changes to state aid rules are problematic

The proposals that have been announced are mainly aimed at opening up the regulatory framework further for certain types of state aid, thereby increasing the total amount of state aid from member states, (although this is described in different ways, often in terms of increased flexibility, speed, and simplifying calculations, procedures and rules). This is extremely problematic.

The increased amount of distorting state aid within the EU is in itself a problem. The amount of support has increased drastically in conjunction with the latest crises – Covid-19 and the war in Ukraine – but even excluding crisis aid, the amount of state aid is increasing significantly. For example, as Swedish Enterprise has shown, support for climate, environment and energy has increased by 10 per cent on average between 2015 and 2020. Should that trend continue, member states would grant 1 172 billion Euros in such support between 2023–2030, compared to the USD 369 billion included in the IRA.

The risk of competition distortion in the single market is obvious. The Commission proposes changes to the TCF, among other things, which has been used extensively during the current crisis. Of the 672 billion euros approved by the Commission, 53 per cent has been notified by Germany and 24 per cent by France. Further easing of regulations risks distorting competition even more in favour of those countries that have the resources and political will to use state aid as a tool to strengthen the short-term competitiveness of their respective countries' own businesses. This is a threat to the relative competitiveness of Swedish businesses and must be taken seriously.

Another major problem with state aid is the lack of evidence to suggest that such support has any long-term positive effects on the economy in terms of increased productivity, competitiveness, or employment. State aid also tends to favour large and established businesses over new and smaller ones. Businesses that benefit are therefore not necessarily businesses that improve productivity in the economy or that best meet environmental goals. This typically reduces competitive pressure on major players and results in a less dynamic economy. Therefore, state aid often leads to structural stagnation, which is particularly serious at a time when the EU needs faster structural transformation. Finally, support also needs to be financed, for example through increased taxes which in turn can result in distortions in the economy, reduced competitiveness, and reduced investment.

Swedish Enterprise therefore believes that the proposals in their current form risk harming European competitiveness more than benefiting it. Greater amounts of support, which are increasingly directed at politically designated sectors and technologies, threaten equal competition in the single market and a well-functioning and dynamic economy. It also risks undermining the important work that the Swedish presidency has begun on strengthening the EU's long-term competitiveness, which is what businesses are calling for, and where the European Council, for the same reasons, called on the Commission to present a strategy at EU level to strengthen competitiveness and productivity.

Regarding changes to the TCF

The Commission proposes a further revision of the TCF, this time also renaming it as the Temporary Crisis and Transition Framework (TCTF).

As Swedish Enterprise has previously described, the crisis framework is not a suitable legal basis to use for forward-looking support. Forward-looking support for long-term green investment specifically needs long-term and stable conditions, which are not created in a temporary crisis framework awaiting its fourth revision in less than a year.

The legal basis of the TFEU can also be questioned. Article 107.3 c of the TFEU is cited in relation to the option of granting forward-looking aid as per Articles 2.5 and 2.6 of the TCF. Swedish Enterprise has previously described how the balance test that the Commission must use to assess compatibility should not be affected by whether similar types of subsidies are granted in third countries. In addition, the introduction of forward-looking state aid opportunities under the TCF creates an overlap with state aid available under the framework of the General Block Exemption (GBER) and the Climate, Environment and Energy Guidelines (CEEAG). It is unclear on what basis the Commission can reach a different interpretation of what is compatible with the single market in the TCF than what is done in the GBER and CEEAG for the same type of aid.

Introducing additional support options in the TCF increases the risk that the regulatory framework is extended and is thus no longer temporary or related to the crisis as originally intended. The regulatory framework also becomes even more complicated, with the TCF overlapping in particular with the GBER and CEEAG. This does not contribute to simplification or improvement. In addition, the TCF is a communication rather than a block exemption – member states must notify approved aid to the Commission and await the Commission’s assessment. Use of the GBER is preferred, as there member states are able to implement support measures directly, without asking the Commission in advance, as long as certain conditions are met. An expansion of the TCF therefore risks counteracting the modernisation of the state aid regulations, increasing the administrative burden for member states and the Commission and making regulations more complex and difficult to manage.

The Commission proposes to primarily make two changes to the TCF. One seeks to make the calculation of aid easier, approving aid faster, and broadening the scope to cover aid for all renewable energy technologies. Swedish Enterprise is doubtful whether the Commission’s assessments can be conducted any faster than they already are, as aid is already approved much faster than was the case in the past, typically only in a few weeks. Simplified calculations of support are in themselves welcome, but not if this results in the granting of more and disproportionate amounts of state aid. Finally, it is positive if the Commission adopts a technology-neutral approach and does not discriminate between different types of fossil-free energy.

The second proposed change involves introducing new investment support for green investments in strategic sectors where there is a risk of investment being diverted from the EU due to subsidies given in third countries. It should be emphasized that the proposed new basis for aid is not limited to a comparison with the US, but subsidies in all third countries could call for corresponding state aid from an EU member state. It should also be possible to provide support in the form of tax breaks.

Swedish Enterprise advises against introducing such a basis for state aid. State aid should be used restrictively and in the event of market failure. The existence of state aid in third countries should not be a basis for approval of state aid within the EU. Such a development would make the granting of aid even less accurate and efficient and risks counteracting the productivity development in the EU, as well as leading to a state aid race between the EU and third countries. Destructive incentives and the risk of protectionism are created if member states develop and design aid schemes based on what is done in third countries rather than what is appropriate from an economic perspective. Rather, greater subsidies globally should be countered through multilateral measures under the WTO, for example, bilateral contexts such as free trade agreements, and unilateral measures such as recently introduced rules against foreign subsidies as well as previously existing opportunities for equalization measures against subsidised exports. The only positive aspect about this proposal is that it is limited to investment aid, must be time-limited, and includes proportionality requirements.

Regarding changes to the IPCEI Communication

Changes to the Communication on Important Projects of Common European Interest (IPCEI) have also been announced by Executive Vice-President Vestager and President von der Leyen.

IPCEIs may be appropriate to the extent that they address a genuine market failure and where other state aid rules are insufficient. Otherwise, usual state aid rules should be used, preferably the GBER, as the IPCEI is more complicated. This is because they involve several applicant member states, a large number of businesses, and the co-ordination of several aid applications. This instrument should therefore be used in addition to the other state aid rules and with these characteristics in mind.

Despite this, the IPCEI is given considerable weight and described as having a major and important role in efforts to improve European competitiveness. This is despite the disadvantages that exist with the rules, (mentioned above), and the fact that, to date, there is a complete lack of knowledge about the results of these projects. Successes that are sometimes claimed for IPCEI relate to projects being set up and given approval by the Commission – nothing about the results they achieve, let alone whether those results justify the substantial amounts of state aid such projects are typically granted.

The high levels of state aid and options for providing aid for later phases in the commercialisation of research projects mean that the risk of distortions of competition is considerable. The rules have mainly been used by a small number of member states to provide large amounts of support to their own businesses, while other member states have sometimes participated in integrated projects but have not granted support to nearly the same extent. It is also the case that it is mainly larger businesses that have received aid – businesses that often have reasonable conditions to finance these types of projects on their own or on the private capital market. This type of aid therefore risks cementing market structures, leading to weaker competitive pressure, and reduced productivity in the long term. Despite ambitions expressed to include small and medium-sized businesses in these projects to a greater extent, results are so far minimal. This is due to high administrative costs and the complexity of these projects, something which many smaller businesses struggle with.

The ambitions now being talked about to accelerate IPCEI processes to facilitate financing and to make it easier for small businesses and from all member states to participate can only be met with scepticism. Improved processes and increased transparency are desirable, but the model also has its limitations. The IPCEI communication were recently revised, but there is no knowledge about whether the rules are appropriate and effective. Above all, an external review of the rules and projects approved to date is what is needed.

In the short term and while waiting for a review that can provide more knowledge, and to simplify and speed up projects, the Commission should consider the following:

- Divide large integrated projects into smaller integrated sub-projects to an even greater extent to reduce the need for co-ordination and administration.
- Develop guidance/best practice for how beneficiaries, authorities and member states should work with the IPCEI. Lengthy application processes are largely because involved parties are unfamiliar with processes, that applications are substandard, and that other parts of the state aid rules would be more appropriate.
- Increased transparency by announcing which projects have started and which businesses are involved.

Concluding remarks

Swedish Enterprise sees considerable risks with the proposals in their current form. They risk increasing the complexity of the regulatory framework, increasing administrative burdens, increasing the distortion of competition between businesses and member states and, in the long run, lead to reduced competitiveness, dynamism and productivity in Europe. In terms of state aid, the Commission should stick to the principles that have guided the modernisation of the state aid framework – namely to allow most state aid cases to be administered within the framework of the general block exemption, which was designed based on evaluation and open consultations. In other respects, competitiveness in Europe should be strengthened in the long term in ways other than through changes to state aid rules, especially through better regulation and further integration of the single market.

Yours sincerely,

Stefan Sagebro
Competition and State Aid Expert
+46 (0)8 553 43 101
stefan.sagebro@svensktnaringsliv.se