

Opinion of the European Economic and Social Committee on ‘State aid to firms: is it effective and efficient?’

(own-initiative opinion)

(2016/C 013/05)

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On 19 February 2015 the European Economic and Social Committee, acting under Rule 29(2) of its Rules of Procedure, decided to draw up an own-initiative opinion on:

State aid to firms: is it effective and efficient?

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The Section for the Single Market, Production and Consumption, which was responsible for preparing the Committee’s work on the subject, adopted its opinion on 14 July 2015.

At its 510th plenary session, held on 16 and 17 September 2015 (meeting of 16 September), the European Economic and Social Committee adopted the following opinion by 198 votes to 3 with 9 abstentions.

1. Conclusions and Recommendations

1.1. The European Economic and Social Committee (EESC) considers State aid impact evaluations to be key tools for checking the consistency between results and proposed targets, thus enabling resources to be allocated more effectively and efficiently, improving the transparency and the endorsement of management processes.

1.2. Many Member States have already developed complex, structured evaluation systems. These systems develop in parallel with growing interest from the academic world, which has enabled improvements to be made to evaluation techniques and to the accuracy of measuring instruments available to granting authorities.

1.3. The European Commission, along with the Member States, has set up a high level forum for State aid which also deals with evaluation.

1.4. Last December, in her speech at the high-level Forum, the European Commissioner for Competition Margrethe Vestager stated that: ‘There are two key elements in the State Aid Modernisation programme (SAM) which are of particular importance: **transparency**, which lets citizens know where their money has gone, and **evaluation**, which tells them whether it has been well spent.’ The EESC strongly agrees with this message.

1.5. The EESC welcomes the debate on impact evaluation in relation to business aid policy and urges the Commission to press ahead with the approach that it has been taking for some years now.

1.6. It should be noted however that many aid schemes today are not subject to an impact evaluation, with the exception of evaluations laid down by European Regulations. In many cases, regulations merely require confirmation that individual operations formally adhere to legal requirements — they do not therefore enable a comprehensive, long-term evaluation of the effectiveness and efficiency of all investments made in support of firms. The EESC would like to see a generalisation of impact evaluations and possibly a lowering of the EUR 150 million average annual budget threshold currently set by the General Block Exemption Regulation as a limit, in excess of which aid schemes are required to submit an *ex-ante* evaluation plan — as otherwise this requirement would not apply to many Member States, particularly when the aid in question is considerable in relation to the size of the state.

1.7. The EESC highlights how the overall legislative framework on State aid is gradually transforming the Commission's role, moving it away from a predominantly administrative culture which once dominated, towards a new form of cooperation with Member States which seeks to optimise the results achieved by State aid, by focusing on its effectiveness and efficiency. The adoption of 'modernisation' was an important step forward.

1.8. Member States must establish appropriate mechanisms for evaluation, carried out by independent bodies. The EESC considers it necessary for the social partners to take part in the process of defining the evaluation model without sacrificing the considerable expertise acquired by public authority staff. Such staff should have a role in developing evaluation processes and participate in the drafting of the final report, thus spreading a culture of evaluation within their own organisations and gradually improving the investigative process. The European Commission must contribute towards harmonising evaluation criteria in the Member States. Establishing comparable evaluation criteria will enable an overall assessment of the effectiveness and efficiency of State aid to be carried out.

1.9. Particular attention should be paid to specific circumstances in the regions involved in the State aid system. The Commission's commendable decision to exempt over 80 % of total State aid from prior notification ⁽¹⁾ allows funding to be granted immediately but also significantly increases responsibilities and costs for local authorities, thus increasing public spending. Member States will therefore be required to concentrate on providing the necessary resources to launch targeted training courses and to initiate the sharing of best practices between local authorities. A culture of 'partnerships' must be developed at all levels.

1.10. The EESC believes that the new system which grants Member States responsibility for *ex-ante* evaluation will increase overall costs to public administrations and to firms. Careful planning is therefore required to eliminate unnecessary burdens and simplify procedures. It also notes that the six month duration of the authorisation procedures for evaluation plans of very complex schemes could be too tight and that establishing a counterfactual model could present major difficulties for small states.

1.11. The EESC recommends the rapid adoption of the communication on the concept of State aid, particularly in order to help local authorities. The mass exemption from prior notification has transferred a double burden of defining State aid and implementing it in a manner that is compatible with the market onto these authorities. For instance, in the case of public funding for culture and heritage conservation, the continuing legal uncertainty as to which of these constitutes State aid causes authorities to consider all interventions as subject to regulation on State aid and therefore to all the administrative and procedural burdens that this entails. This same uncertainty also characterises public financing for all infrastructure, in particular since the court ruling on the Leipzig airport case. A clear and concise distinction must be made between public support to firms which does not constitute State aid and support that can be considered as State aid pursuant to the definition set out under Article 107(1) of the Treaty of the Functioning on the European Union (TFEU).

1.12. While welcoming the efforts made, the EESC considers it essential that this evaluation culture is extended to all levels of government, both regional and national. It must not therefore be limited to the cases mentioned above. To this end, the Committee calls for a renewed commitment from the Commission and Member States.

1.13. The analysis carried out indicates that public authorities lack data on management costs incurred through overseeing State aid to firms. It is not possible to carry out a thorough evaluation of the efficiency of these funds without considering how much is spent by public authorities, in addition to measuring the aid itself, in relation to the results obtained. The transparency of this system relies on the publication of these data. From the data available, overall administrative costs would amount to around 5 %. Compliance costs — estimated at another 5 % — should be added to this figure, plus further evaluation costs, that the Commission estimates suggest would be just under 1 %. Objectively, this amount of resources — which is probably an underestimate — seems excessive.

⁽¹⁾ Speech by Margrethe Vestager, Commissioner for Competition, at the High-Level Forum of Member States, 18 December 2014.

1.14. The EESC calls on the Commission not to create additional and unexpected burdens for firms and to guarantee that whole evaluation system is rendered more efficient and effective.

1.15. It is very important that assessments consider the efficiency of administrative costs and costs arising from evaluation models.

1.16. Comparability of different models and flexibility in relation to size, type and indicators should be ensured by simplifying *ex-ante* evaluation and harmonising *ex-post* criteria.

1.17. The EESC calls for an integrated view of Commission activity in different areas of economic policy — structural funds, State aid, trade partnership agreements — in order to ensure a unified European economic policy that is based on growth and development.

1.18. The EESC recommends using criteria similar to those set out in Commission Delegated Regulation (EU) No 240/2014 ⁽²⁾ of 7 January 2014 on the European code of conduct on partnership in the framework of the European Structural and Investment Funds — which establish an obligation to consult all potential stakeholders — in order to formulate a regulation on evaluating the effectiveness and efficiency of State aid.

1.19. Transparency of the evaluation carried out should be guaranteed and given as much publicity as possible — this is already the case in some Member States with regard to firms and the amount of aid granted.

1.20. The EESC recommends that evaluation plans include:

- the achievement of the policy objective;
- the impact on competition and trade;
- the effectiveness/efficiency of the instrument;
- *ex-ante* verification of the prerequisites for continuing the scheme or similar schemes at micro-level (aid specifications);
- the incentive effect.

1.21. The EESC asks to be involved in the processes of evaluating the overall effectiveness and efficiency of the State aid system at the end of the period 2014-2020.

2. Introduction

2.1. Aid to firms may distort competition and fragment the internal market, contradicting the nature and spirit of the treaties, if it is not set within a clear regulatory framework, directed towards productive activities and firms which invest in particular in innovation research and development (and produce economic and social benefits), and if it is not limited and monitored.

2.2. On the other hand, the negative economic predicament which has persisted for several years — entailing serious national crises which inevitably affect businesses, workers and citizens — requires a relatively flexible approach, as implemented by the EU's major competitors on the international markets (which are not subject to a single set of rules on State aid). The competitiveness of European firms should be an important benchmark. Unemployment in Europe is a real emergency. Investments have fallen by 15 % since their peak in 2007 and 25 million Europeans are still unemployed. 5 million of these are young people. The majority are women ⁽³⁾.

⁽²⁾ OJ L 74, 14.3.2014, p. 1.

⁽³⁾ <http://ec.europa.eu/eurostat/tgm/refreshTableAction.do?tab=table&plugin=1&pcode=teilm020&language=en>

2.3. An interesting study by the European Parliament ⁽⁴⁾ highlighted considerable differences between current schemes in place in the EU and the USA. 'EU competition policy has strict rules on State aid, whereas US legislation has no provisions in this area.' An EU proposal for rules on State aid has been included — at the request of the then Commissioner Joaquín Almunia — in the current negotiations between the EU and the USA on the Transatlantic Trade and Investment Partnership (TTIP) ⁽⁵⁾.

2.4. The proposal seems weak and essentially inconsequential ⁽⁶⁾. Europe will continue to have the most restrictive legislation in the world. While on one hand this helps to complete the single market, it also penalises our firms. A European firm which manufactures in the USA is eligible to receive State aid that is inadmissible in the EU. This will be made easier by the adoption of the agreement. The EESC issues a serious warning to the Commission not to give preference to US firms in the free trade agreement.

2.5. Experience to date has shown that there is a need for a thorough review of the European State aid programme.

2.6. The economic and financial crisis of recent years has forced a radical review of the spending criteria used to determine public investment policy and business support policy at all levels of government. Specifically, the need to find a better way of rationalising support (granting aid only when there is sufficient added value), which would improve the quality of aid and — simultaneously — enable proper monitoring of the effectiveness and efficiency of this aid, has become a priority, in light of the scarcity and limited resources available.

2.7. In the EESC's view, it seems appropriate to find out what effect the business aid policies adopted have had, whether instruments for support identified are suitable and whether administrative and management costs are proportionate to the results obtained. We must be mindful throughout that what cannot be measured cannot be identified or improved. The measures adopted so far have set this approach in motion.

2.8. 'Evaluation may seem a technical topic of interest to only a small academic research community, while exercised by a larger, practitioners' community of consultancies specialising in financial auditing or in project and program evaluations. However, as evaluation has risen centre-stage on the European Commission's Smart Regulation agenda, it has become a key topic of regulatory policy, raising important governance and institutional questions beyond the field of expenditure programs' ⁽⁷⁾.

2.9. Since 2008 the Directorate-General (DG) for Regional and Urban Policy has developed counterfactual evaluation programmes to support existing evaluations (*ex-ante* and *ex-post*) which are conducted during the programming of the structural funds.

2.10. In May 2012, as part of its State Aid Modernisation (SAM) reform programme, DG Competition introduced the use of an impact evaluation which employs counterfactual analysis techniques for some aid schemes ⁽⁸⁾. In particular, the new General Block Exemption Regulation makes the evaluation of large aid schemes (with an annual budget of over EUR 150 million) mandatory in specific sectors such as: regional development policy, aid to small and medium-sized enterprises (SMEs), research, development and innovation support, environmental and energy aid and support for broadband infrastructure. Some national plans have already been submitted (four), and others in the field of research, development and innovation and broadband are under consideration (around ten).

⁽⁴⁾ http://www.europarl.europa.eu/RegData/bibliotheque/briefing/2014/140779/LDM_BRI%282014%29140779_REV1_EN.pdf

⁽⁵⁾ http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc_153019.6%20Competition%20SoE%20Subsidies%20merged.pdf

⁽⁶⁾ http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc_153031.pdf

⁽⁷⁾ http://www.lexxion.de/pdf/ejrr/ejrr_2015_01-005.pdf

⁽⁸⁾ Commission Regulation (EU) No 651/2014 of 17 June 2014 declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty Text (OJ L 187, 26.6.2014, p. 1).

2.11. The European Court of Auditors recently intervened in the case of the results evaluation systems used by EuropeAid, judging them to be inadequate⁽⁹⁾. The evaluation systems used in all of the Commission's activities are currently under review.

2.12. Greater coherence between the evaluation methodologies used to evaluate State aid and the results of using structural funds is essential, as is a thorough review of all the Union's expenditure policies.

2.13. The purpose of a counterfactual approach to evaluating the effects of public policies is to verify the policy's ability to effect a desired change in the behaviour or the conditions of a given target population or beneficiary. It essentially defines the extent to which the support — rather than other factors — has contributed towards the achievement of a certain result. This is sometimes referred to as the incentive effect.

2.14. The aim of the evaluation process is to identify the causal impact of the policy adopted, including only the direct effect of that policy. In other words it eliminates any possible distortions due to general macroeconomic conditions or the diverse nature of firms.

2.15. The causal impact is the difference between the observable outcome variables after policy implementation (the factual situation) and what would have happened if this particular policy had not been adopted (counterfactual situation).

2.16. This type of analysis comes in response to requests seeking to establish evidence of the net effect of support, and the extent of this effect. For example it addresses whether aid produces positive or negative effects and to what extent, whether the changes observed are genuinely attributable to the policy implemented, whether results vary between different beneficiaries (large or small firms), between regions or over time, and whether management and administrative costs are proportional and sustainable.

2.17. Although this subject has been addressed extensively in economic literature, particularly in recent decades, there are only a few cases of public authorities in European Member States continuing and generalising the use of impact evaluations to monitor and improve their business aid policies.

2.18. The most interesting cases to note include efforts made by the United Kingdom, which since 2001 has regularly assessed regional aid programmes using quasi-experimental evaluation techniques, and the Netherlands, which in 2012 established an Impact Evaluation Expert Working Group. Similarly, Finland set up the Finnish Innovation Agency (TEKES) and Slovenia approved the Monitoring of State Aid Act in 2001.

2.19. With this opinion, the EESC wishes to contribute to discussions conducted by the European Commission and Member States on the effectiveness and efficiency of aid measures for firms and on the need to extend the use of impact evaluations.

3. Why evaluate? Lessons from the literature

3.1. On the basis of empirical evidence from counterfactual analyses, this opinion aims to demonstrate the importance of evaluation. Evaluation should no longer be considered as an academic exercise, but as an essential, institutionalised practice included within the policy cycle: implement, monitor, evaluate, reshape.

3.2. For this reason it will examine a number of studies carried out in different European Member States and highlight the fundamental lessons learned, namely the policy implications in terms of the impact on investment growth, productivity, employment, innovation and the cost of the scheme. These indicators provide an understanding of the effects on growth and they emphasise the need for targeted, high-quality aid.

3.3. Although the literature tends to emphasise the existence of a positive correlation between public support for firms and the growth of output (investment, employment, new products), it must be noted that the incentivising effect of aid cannot be taken for granted. There are several other factors which influence the success of a policy, such as the general economic trend, the functioning of the market and the overall taxation system.

⁽⁹⁾ http://www.eca.europa.eu/Lists/ECADocuments/INSR14_18/INSR14_18_EN.pdf

3.4. In a study analysing the impact of Law 488 in Italy, Martini and Bondonio (2012) show that on average firms that received direct aid reduced private investments. In this case direct state support to firms seems to have resulted in a decrease in private investment expenditure, thus reducing the need for private resources. State aid must be additional to and not a replacement for investment.

3.5. The literature also highlights some important concerns in relation to the impact of aid on productivity. In an evaluation study on British firms which received support as part of the Regional Selective Assistance Programme (RSA), Criscuolo (2012) explains how growth in productivity was not statistically significant⁽¹⁰⁾.

3.6. These findings seem to be in line with other empirical evidence which shows how direct aid often has a positive effect on production volumes, without however having any effect on productivity. In other words, the firms which receive aid grow without becoming any more efficient. This would increase the risk of keeping non-competitive companies on the market.

3.7. Statistical-econometric models which identify the impact of support using a counterfactual approach also make it possible to show the net effects of specific aid measures on employment. This allows the cost per labour unit 'created' to be measured.

3.8. Often, there is a discrepancy between the number of new labour units that are attributable directly to the aid and the statistics recorded in *ex-post* monitoring. In a study focusing on measures to assist SMEs in Poland, Trzciński (2011) shows that out of the 25 000 new jobs 'created' by the support, only 10 550 are those actually attributable to the policy implemented⁽¹¹⁾. Bondonio and Martini (2012) reached the same conclusion. Out of 89 000 new jobs recorded in the *ex-post* monitoring of Law 488, only 12 500 were effectively created, at a cost of EUR 232 000 per labour unit⁽¹²⁾. The impact that State aid has in terms of existing jobs, and therefore safeguarding the local, regional or national economy, should be taken into consideration.

3.9. Aid to firms produces different effects depending on the amount of support granted, the size of the firm, the geographical area where it is located and the type of aid pledged. Empirical evidence from such analyses should be at the disposal of public decision makers, to guide their choices and to help them understand what type of support is most appropriate and in what context. As has been clearly demonstrated thus far, it is necessary to formulate targeted aid measures, in order to increase the efficiency and effectiveness of policies.

4. Comments

4.1. The European Commission should continue its work on raising awareness of the most common principles and methods employed in the area of impact evaluation. In particular, the EESC believes that workshops on evaluation techniques and available methodologies should be held in various Member States, in collaboration with universities, the social partners, research institutes and other stakeholders. This experience will help the Commission to gain a readier understanding of the obstacles encountered when applying regulation, and allow it to intervene promptly in this regard.

4.2. Although the Commission's efforts must be applauded, it is important that more aid schemes be subject to evaluation, particularly when large amounts of aid are involved. It is also essential to promote a debate on methodology which aims to complement counterfactual evaluation techniques with new evaluation instruments that can also cover the effects of other forms of support to firms (financial support, indirect aid, industrial policy considered *per se*).

4.3. The EESC insists on the need to develop an appropriate pluralist methodology as regards evaluation criteria and indicators. The Commission asserts⁽¹³⁾ that 'this shall ensure that public support stimulates innovation, green technologies, human capital development, avoids environmental harm and ultimately promotes growth, employment and EU competitiveness.' Each of these elements contributes to the evaluation of the impact of State aid, over and above a mere evaluation of cost. The European Parliament is calling to be involved in defining evaluation methodologies, as well as European law on State aid, as this has a strong influence on the economic policy decisions of Member States. The EESC also emphasises that it would be beneficial for research purposes to have free access to evaluation data, in order to improve the methodology used.

⁽¹⁰⁾ Criscuolo, C, R. Martin, H. Overman and J. Van Reenen (2012), *The causal effects of an industrial policy*, CEPR Discussion Papers 8818.

⁽¹¹⁾ Trzciński, R. (2011), *Towards Innovative Economy — Effects of Grants to Enterprises in Poland*, ed. (edited by Jacek Pokorski).

⁽¹²⁾ Bondonio, D. Martini, A. and (2012), *Counterfactual impact evaluation of cohesion policy: impact and cost effectiveness of investment subsidies in Italy*, Report for DG Regio, European Commission.

⁽¹³⁾ COM(2012) 209 final.

4.4. It would be beneficial for the Commission, along with national and European statistical organisations, to discuss the possibility of creating a reliable database on State aid to firms as part of a single methodological framework. This would guarantee the transparency of decision-making processes, and would also encourage research and evaluation activities both by public authorities and researchers involved.

4.5. Universities and research centres could play a decisive role in shifting awareness towards a culture of evaluation and in circulating new and more advanced instruments for evaluating public policies. Moreover the European Commission could use independent research institutes to conduct case studies with the aim of evaluating the effectiveness of aid in certain sectors such as research, development and innovation aid, support for SMEs, aid to the energy sector and infrastructure aid.

4.6. Given that the evaluations required under the new Community regulations do not give due consideration to the effects that business aid policy has on the European economy as a whole, it is advisable that the Commission launch a pilot study on this topic at the end of the current programming period (2014-2020). The study should investigate the main factors which determine how aid is spent, define the relationship between aid to firms and the granting authority's economic potential and seek to understand the existing link between cohesion policy and competition policy.

4.7. This opinion is the first step in the EESC's work on measuring the impact of state to firms. It also responds to and supports the Commission's activity in this area. However the EESC considers it essential to enhance and extend debate. It will continue to follow the Commission's work in this area closely and to promote a culture of effective and efficient evaluation wherever possible.

Brussels, 16 September 2015.

The President
of the European Economic and Social Committee
Henri MALOSSE
