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"Competition, State aid and Subsidies in the European Union"

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I'm very pleased to be here today in only the second week as Competition Commissioner.

The OECD and its Competition Committee play a very important role in the field of competition. I very much appreciate the quality of your work, and applaud your efforts to achieve greater convergence in competition policy worldwide.

My key priority for the next five years is the same as it was under my previous responsibility as Commissioner for Economic and Financial Affairs: to help overcome the current financial and economic crisis and ensure that Europe emerges better equipped for balanced and sustainable growth and more jobs. This is an ambition which we all share for our respective countries – and the reason why we are meeting here at the OECD, to work together to achieve this ambition.

This is also the aim of the proposals the new European Commission is preparing for what we call "The EU 2020 Strategy": to lay the foundations for a more dynamic, knowledge-based, socially inclusive and greener economy that is both sustainable and fair.

I believe that competition policy has a vital role to play in this regard, by making markets work better, for the benefit of business and consumers.

Competition gives business the tools to succeed on the world stage, by enhancing their competitiveness and encouraging innovation. It helps create viable companies that can offer workers long-term employment prospects. And it gives consumers the benefit of lower prices, better choice and better quality of goods and services.

Competition policy is sometimes thought of as only addressing the behaviour of companies and businesses: cartels or abuses of market power, or mergers whose impact on competition needs to be assessed. But state subsidies to business ("state aid" in EU Treaty language) can also distort competition. A review of the impact of subsidies is, I believe, an important aspect of competition policy.

Subsidies are of course an essential tool for policy makers and governments. Government measures to support the financial system and other sectors of the economy over the past 18 months are a case in point. It is widely acknowledged that the money governments poured or committed in support of financial institutions prevented a catastrophic collapse of the global banking system.

On top of the immediate reactions needed to avoid a meltdown of the economy, in normal times subsidies can help remedy a market failure, promote investment in

environmentally friendly technologies, or foster economic and social development in a particularly depressed region. These are important public policy objectives – and it is crucial to ensure that governments have the best-designed tools available to achieve these objectives.

Our aim in recent years, before the crisis emerged, has been to ensure that subsidies are targeted towards horizontal objectives such as these, and to prevent subsidies that merely keep inefficient firms on life-support. In the mid-1990s, around 50 per cent of government subsidies to industry and services in the EU were earmarked for horizontal objectives as opposed to individual bailouts. By 2008 this figure had risen to nearly 90 per cent.

Overall, government subsidies in the EU amounted to just over 0.5 per cent of EU GDP in the period 2004-2008, excluding measures to address the financial and economic crisis. Over the longer term subsidies are on a downward trend, since they are down from nearly 1 per cent of EU GDP in the 1990s.

The EU system for reviewing State subsidies

What we have in the EU is a system that requires the European Commission to review state subsidies to business and to assess their impact on competition. The fundamental principles were laid down in 1957, as a necessary condition to achieving a common market in goods and services in the EU, and remain unchanged today in the new Lisbon Treaty. A single market across the EU requires a level playing field between businesses in different Member States, so that our review of subsidies looks not only at the impact on competition between businesses in a given country, but also at the impact on cross-border competition.

What we do is essentially carry out a balancing exercise, weighing up the efficiency and equity benefits that are expected to result from a subsidy, against the negative effects the subsidy might have on competition in the EU and on trade between EU Member States.

Specifically we consider whether the government's objective in providing the subsidy does not run counter to the common interest of EU Member States – including growth, employment, regional development, the environment, or research and development.

One element we take into account is whether the subsidy addresses a market failure. For instance, we recognise that small businesses find it difficult to access risk capital because of high transaction costs to assess small projects compared to the expected gains from investment. So subsidies to facilitate access to risk capital may be acceptable. Similarly, we are happy to encourage subsidies for the extension of broadband to remote regions, which is not profitable under normal market circumstances. Likewise, we allow subsidies to cover part of the costs of a research project knowing that markets are not always ready to take on the full risk of research especially when profitability horizon is very long.

We check that, in practice, the subsidy will help achieve that objective, that it creates the right incentives for companies to adjust their behaviour. We also check that the subsidy is proportionate, i.e. that the same adjustments to company behaviour could not be obtained with lower subsidy.

This balancing exercise, based on an economic assessment of the impact of the measure, is carried out before the subsidy is implemented. It can lead to the Commission imposing conditions to minimise the distortion of competition, for instance, a reduction in the amount of the subsidy. This helps ensure that subsidy measures do not have an unduly distortive effect on competition in the EU. It also gives Member States an insight into the effectiveness of a planned subsidy and whether it will give value for money to the taxpayer.

Of course, what we don't do – thankfully – is review every single subsidy measure adopted by EU Member States. Following recent reforms, far fewer measures require notification to the Commission. Some of them do not distort competition or trade between Member States, others benefit from a general exemption laid down by regulation, or a general scheme (for instance for aid to research and development, development of small businesses, training and the creation of new jobs, etc). The Commission only carries out an in-depth, individual, review of those large subsidies which have the potential to be really harmful to competition. And what I want to do is to make sure our procedures for notification and review are as simple and streamlined as possible, so as to keep the bureaucratic burden to a minimum.

However, where we find that a State subsidy is unlawful – that is it violates our rules for its acceptance - it must be recovered in full. That is the only effective way of remedying the distortion of competition created by the subsidy.

Why it works

I've mentioned before the role of state subsidies in the global financial crisis. Let me come back to this issue.

Early action by the European Commission helped ensure a common approach by Member States to financial sector bail-outs. Member States may have adopted different measures – those which they felt were best suited to their respective market situation – whether guarantee schemes, recapitalisation measures, or impaired asset relief measures, or a mixture of these. But the European Commission required that all of these measures complied with certain fundamental principles – non-discriminatory access to national schemes, subsidies limited to what was necessary, mechanisms to prevent abuse of state support, restructuring measures for certain financial institutions that received large amounts of aid.

This helped keep to a minimum any distortions of competition between banks within and across national borders, and helped preserve the integrity of the EU internal market. It prevented costly and damaging subsidy races between Member States, with each trying to outdo the other in an attempt to prevent business moving away.

Going forward, EU policy on reviewing State subsidies – notably through the restructuring measures being agreed as a condition of approving bank subsidies – is helping rebuild viable financial institutions which are able to carry out the essential function of providing finance to the real economy.

Reviewing subsidies at national, supranational and international level?

Naturally, the EU perspective on the control of subsidies is closely associated with its powers and role as a supranational body, pursuing common EU objectives such as a level playing field for business and the internal market.

But the underlying principle – that subsidies should not unfairly distort competition between businesses so that companies can compete on merit to the benefit of consumers – is equally important at national level and on national markets for goods or services. Creating or supporting a national champion creates domestic casualties too – those companies that are not chosen for government support. Measures to support inward investment may result in obvious rewards – but it may be worth assessing for just how long those measures continue to produce net benefits, in particular if such support is open-ended.

National regimes for reviewing state subsidies do exist – for instance in Spain, my own country, the national competition authority has the power to issue opinions on subsidies granted by the regions or the central government. On the other hand, countries that are candidates to join the EU are required to set up systems for reviewing State subsidies. One of them, Croatia, has a system that mirrors the EU system – with the national competition authority entrusted with the relevant powers. Looking further afield, Russia also has a system of subsidy control and the Mexican competition authority has powers to deliver opinions on the impact of subsidies on inter-State trade.

I believe that there is scope for individual countries outside the EU to consider adopting a system of controlling State subsidies, for the benefit of business environment and quality of public policies

What about the international level?

All of us here today recognise the benefits of open markets and the downsides of protectionism. Subsidies can be an instrument of protectionism, countering the benefits of trade liberalisation. The WTO rules on subsidies for goods can play a role in removing the most harmful subsidies – but no rule can be applied properly without transparency. So I fully endorse the OECD ministerial conclusions of last June which state that government measures to support industry must be transparent and WTO consistent. Transparency helps contain protectionist measures by opening them up to public scrutiny – and helps ensure a level playing field for business in markets across the world.

With this in mind, I welcome the initiative by WTO Director General Pascal Lamy to report quarterly on measures adopted by G20 countries to counter the crisis. This is particularly important since the G20 is leading the drive towards a coordinated route out of the crisis for the world economy. In a move which underlines the importance we attach to transparency, the EU has already introduced this principle and reports regularly on all Member State actions, regardless of their G20 status. The next report will be published in early March. I look forward for other countries to follow that lead.

Conclusion

Let me conclude.

The EU rules on government subsidies are a key element of EU competition policy in that they help maintain a level playing field for business within Member States and across Europe. They have proved their worth in the context of the financial and economic crisis, helping avoid damaging subsidy races between EU Member States and minimising the distortions of competition resulting from large-scale government bail-outs for financial institutions.

But rules on government subsidies are not an exclusive EU issue. They have a place in all competition regimes – whether national, federal, supranational or international. They help maintain the level playing field between businesses implanted within a country, across regions, and across national borders. They help open up markets to international trade. Ultimately, they help governments assess the effectiveness of proposed subsidy measures, and help channel funds to where they are the most necessary and can deliver the most benefit to taxpayers.