New United Kingdom subsidy control regime

The Government publishes its proposals for a new UK-wide subsidy control regime — a "flexible, principles-based approach for the UK"

In brief

Since the end of the Brexit transition period on 31 December 2020, there has been significant uncertainty regarding the practical application of the UK's international commitments (in particular, under the EU-UK Trade and Cooperation Agreement) on subsidy control. However, on 30 June 2021, the Government outlined its main legislative proposals for a new UK subsidy control regime. It introduced its long-awaited Subsidy Control Bill (the Bill) to Parliament, published a number of policy papers and provided a response to the public consultation that ran from 3 February to 31 March this year. The Bill is intended to come into effect in 2022, with the Government expected to publish secondary legislation and further guidance for public authorities over the next few months.

Key takeaways

The Government proposes the following aspects for the new subsidy control regime:

- The Bill includes a new definition of subsidies and seven subsidy control principles (against which most subsidies will need to be assessed), and it identifies certain categories of automatically exempt or automatically prohibited subsidies.
- A new, independent Subsidy Advice Unit (SAU) will be created within the Competition and Markets Authority (CMA). The SAU will have responsibility for monitoring the effectiveness of the new regime and preparing advisory reports for public authorities on the compliance of proposed subsidies. The SAU's advisory function is significantly more limited than the enforcement role of the European Commission under the EU State aid rules.
- The Government intends for public authorities to be able to self-assess the compliance of the vast majority of subsidies, either against the subsidy control principles or, for low-risk categories of subsidies, certain "streamlined" criteria (not yet published).
- For subsidies that are more likely to have negative effects, the Government proposes the introduction of voluntary or mandatory (depending upon the risk level) processes for public authorities to obtain non-binding advice from the SAU on how the authority's assessment of compliance and the design of the subsidy might be improved.
- The Government will have (i) a "call-in" power to require public authorities to seek advice from the SAU and (ii) a power to refer subsidies to the SAU for a compliance review even after they have been granted.
- A process will be introduced for interested parties and the Government to challenge subsidy decisions in the Competition Appeal Tribunal (CAT) on judicial review grounds. The CAT will have the power to order the recovery of non-compliant subsidies.

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In depth

Prior to the end of the Brexit transition period, subsidies awarded by UK public authorities were subject to the EU State aid rules. This meant that they had to be notified to and approved in advance by the European Commission (subject to exemptions, in particular for measures covered by block exemption regulations). However, one of the Government's key priorities in the Brexit negotiations was to ensure that, post-Brexit, the UK could move away from the EU State aid rules (on the basis that this would enable the UK to provide more "agile" and "flexible" support to UK businesses).

During the final stages of the Brexit negotiations, the Government agreed with the EU to certain commitments on subsidy control, most notably in relation to the introduction of a system with an "appropriate role" for an independent authority. These commitments are in addition to the Government's obligations under World Trade Organization rules in this area and in other free trade agreements that the UK has concluded.

The Government was not in a position to introduce a system to implement its new commitments immediately and, as a result, there has been significant uncertainty regarding the practical application of these commitments over the past six months. However, with the publication of the Bill, we now have a much greater understanding of what the new regime will look like. While the Bill will be subject to some debate (in particular, this is likely to focus on the scope for central government intervention in measures awarded by other authorities), the key elements of the Bill (as set out below) are unlikely to change significantly.

Definition of subsidy

The Bill defines "subsidy" as financial assistance that is given, directly or indirectly, from public resources by a public authority, and that:

- confers an economic advantage on one or more enterprises
- is specific, in the sense that it benefits one or more enterprises over one or more other enterprises with respect to the production of goods or the provision of services
- has, or is capable of having, an effect on: (i) competition or investment **within** the UK; (ii) trade between the UK and a country or territory outside the UK; or (iii) investment between the UK and a country or territory outside the UK

Most of this definition follows the definition of "subsidy" in the EU-UK Trade and Cooperation Agreement, which in turn closely resembles the definition of "State aid" under the EU rules (albeit with different terminology). However, there is one notable addition — the provision relating to effects on "competition or investment within the UK" — which appears aimed at protecting the UK's internal market (this was a recurring theme in the Government's public consultation and it is a key government priority post-Brexit).

Seven subsidy control principles

The Bill requires public authorities not to give subsidies unless they are consistent with the following seven general subsidy control principles ("**Principles**"):

- **Common interest**: Subsidies should pursue a specific policy objective to remedy an identified market failure or to address an equity rationale.
- **Proportionate and necessary**: Subsidies should be proportionate to their specific policy objective and limited to what is necessary to achieve it.
- **Designed to change the economic behaviour of the beneficiary**: Subsidies should be designed to bring about a change of economic behaviour of the beneficiary. That change should be conducive to achieving the subsidy's specific policy objective and should be something that would not happen without the subsidy.
- **Costs that would be funded anyway**: Subsidies should not normally compensate for the costs that the beneficiary would have funded in the absence of any subsidy.
- **Least distortive means of achieving the policy objective**: Subsidies should be an appropriate policy instrument for achieving their specific policy objective and that objective cannot be achieved through other, less distortive, means.
- **Competition and investment within the UK**: Subsidies should be designed to achieve their specific policy objective while minimising any negative effects on competition or investment within the UK.

- **Beneficial effects to outweigh negative effects**: Subsidies' beneficial effects (in terms of achieving their specific policy objective) should outweigh any negative effects, including, in particular, negative effects on (i) competition or investment within the UK and (ii) international trade or investment.

Six of the Principles were included in the EU-UK Trade and Cooperation Agreement. However, the "competition and investment within the UK" principle is new and again demonstrates the Government's concern regarding the protection of the internal market. Other specific principles are included in the Bill for particular types of subsidies, including energy and environmental subsidies.

Automatic exemptions

The Bill excludes certain types of subsidies from the subsidy control requirements, including the following:

- minimal levels of financial assistance (less than GBP 315,000 over three years)
- subsidies to providers of Services of Public Economic Interest, i.e., entities entrusted with a public service obligation (less than GBP 725,000 over three years)
- subsidies to compensate for damage caused by natural disasters or other exceptional occurrences

Automatic prohibitions

The Bill includes a number of automatically prohibited forms of subsidies, including (i) unlimited guarantees, (ii) subsidies contingent on export performance or the use of domestic or imported goods or services and (iii) subsidies granted for the rescue or restructuring of an ailing or insolvent enterprise (unless certain conditions can be met).

Most notably, the Bill prohibits "displacement" subsidies. In broad terms, this refers to a subsidy that is given to an enterprise on the condition that it relocates some or all of its existing UK economic activities to another area of the UK in circumstances where the enterprise would not otherwise relocate those activities. This is a further measure designed to protect the UK's internal market and, in particular, to avoid "subsidy races" between different areas of the UK (as, for example, is sometimes observed when different US cities/states compete to offer tax breaks and other forms of support when vying for investment).

Self-assessment

The Government intends for public authorities to be able to grant the vast majority of subsidies via one of the following two self-assessment routes:

- **Baseline route**: This route requires public authorities to self-assess the compliance of a proposed subsidy against the Principles.
- **Streamlined subsidy schemes**: The Government will create streamlined routes for low-risk categories of subsidies. Provided that the public authority self-assesses that a proposed subsidy meets the criteria for the particular streamlined route, it will not need to self-assess the compliance of the subsidy against the Principles.

In practice, it is likely that public authorities will try to push this self-assessment onto potential beneficiaries, e.g., by requiring that the beneficiary receive legal advice confirming compliance with the Principles or the fulfilment of the criteria for a streamlined subsidy scheme.

Referral to the SAU

For subsidies that are more likely to cause negative effects, the Government proposes the following two routes, which will involve increased scrutiny of compliance with the Principles:

- **Subsidies of Interest**: For subsidies that are more likely to have distortive effects on UK competition and investment or international trade, public authorities will be encouraged to undertake a greater level of analysis to ensure compliance with the Principles. In addition, they may request a report from the SAU (a "voluntary referral"), which will provide non-binding advice on how the authority's assessment and the design of the subsidy might be improved. Unlike for Subsidies of Particular Interest (see below), authorities can give Subsidies of Interest before they receive the SAU's report (although such action is unlikely in practice given that the authority will have sought the SAU's advice voluntarily and so, presumably, will want to find out its conclusions before taking action).

- **Subsidies of Particular Interest**: For subsidies that have the highest likelihood of having distortive effects, public authorities will be required to undertake more extensive analysis and to request a report from the SAU (a "mandatory referral"). In addition, after the publication of the SAU's report, there will be a mandatory five working day "cooling off" period before the authority can give the subsidy.

In addition to the above routes, the Government will have (i) a "call-in" power to require public authorities to seek advice from the SAU and wait for a short "cooling off" period before granting the subsidies in question and (ii) a power to refer subsidies to the CMA for a compliance review even after they have been granted.

Further detail on the criteria for the routes and the Government's powers will be set out in secondary legislation and laid before Parliament in the next few months.

The CMA's SAU

The Bill establishes a new, independent unit (the SAU) within the CMA. The SAU will have responsibility, in particular, for (i) monitoring the effectiveness of the new regime and (ii) preparing reports for public authorities on the effects of subsidies on competition or investment within the UK. This (advisory) role of the SAU (as the independent body in the UK regime) will be significantly more limited than the (enforcement) role of the European Commission under the EU State aid rules.

Enforcement

A party whose interests are affected by a subsidy decision (e.g., a competitor of a beneficiary) or the Government may bring a legal challenge at the CAT. Such challenges will be limited to the judicial review standard (i.e., not a review "on the merits"). The CAT will have the power, among others, to order a public authority to recover the amount of a subsidy if it is found to contravene the subsidy control rules.

Keywords (Use Title Case)

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