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EDITORIAL COMMENTS

The EU's integrated policy approach towards competitiveness: The interplay between State aid control and industrial policies

From the beginning of this century, the EU has been facing a succession of crises: the banking crisis (2008–2014), the sovereign debt crisis (2009–mid to late 2010s), the migration crisis (since 2015), the Covid-19 pandemic (since 2019) and Russia's war of aggression against Ukraine (since 2022). Thanks to a mix of financial and economic policies and considerable legal-institutional creativity,[1] the EU managed to contain these crises and to limit their impact on the economy. Today, the challenges the EU faces are not less but increasingly complex, as clearly stated by the European Council in its conclusions of 23 March 2023: climate change, the geopolitical situation, energy prices, repeated supply chain shocks, demographic trends, labour shortages, the growth and innovation gap. It concluded that more than ever, the EU needs to build a robust and future-proof economy that secures long-term prosperity. For that to happen, the European Council called for "an integrated approach across all policy areas to increase productivity and growth throughout the whole economic base of our continent, combined with a deepened Internal market and reinforced industrial, agricultural and trade policies". It added that the EU will ensure its competitiveness by strengthening its resilience and productivity, facilitating financing, aiming at affordable energy, reducing its strategic dependencies, investing in the skills of the future and making its economic, industrial and technological base fit for the green and digital transitions while leaving no one behind.[2] At its June 2024 meeting, shortly after the European Parliament elections, the European Council intends to discuss the progress made in that respect, benefiting at that point in time from the report on the future of the internal market, commissioned by the European Council from former Italian Prime Minister Letta and due in March 2024, as well as the report on the future of the EU's competitiveness, commissioned by the European Commission President von der Leyen from another former Italian Prime Minister (and ECB President) Mario Draghi, that is due in

1. Compare the controversy about an allegedly too flexible interpretation by the EU institutions of Arts. 122–125 TFEU during the sovereign debt crisis and the pandemic.
2. See para 13 of the European Council conclusions, 23 March 2023, EUCO 4/23.

June 2024.[3] These reports are likely to impact the European Council strategic guidelines for the coming five years it will have to adopt by mid-2024 on the basis of Articles 22 and 26 TEU. Past practice shows that those guidelines, in turn, influence considerably the key priorities of the new European Commission and its President, whose mandate is expected to start in November 2024.

However, already in 2022 and 2023, the integrated approach called for by the European Council, has been actively followed by the other institutions, particularly by the European Commission.[4] In fact, the EU's search for more open strategic autonomy responds very much to the same *rationale* for bundling different EU instruments in the area of industrial policy, trade policy, internal market and competition, including State aid control. There are many definitions of that concept, but the one of the European Commission's Joint Research Centre seems to be wide enough to encapsulate it as applied in practice so far: [It] "is about equipping the EU to manage interdependence in line with its interests and values".[5] This concept of strategic autonomy, the origin of which can be traced back to the EU's Common Foreign and Security Policy,[6] is shorthand for the by now well-established EU objective to continue to build on (and benefit from) openness – consistent with its commitment to open and fair trade with diversified and sustainable global value chains – while assertively defending its interests, protecting the EU's economy from unfair trade practices and ensuring a level playing field both internally and globally.[7] At the centre of these policies are a strong and well-functioning internal market, with fair competition, objectives that inform also the industrial, competition and trade policies. In this respect, the policies are not necessarily at odds with each other if they operate together in a coherent manner and reinforce each other. The claim is that the EU needs companies

3. See para 18(f) of the European Council conclusions, 30 June 2023, EUCO 7/23, and European Commission President von der Leyen State of the Union of 13 Sept. 2023, available at <state-of-the-union.ec.europa.eu> (all websites last visited 29 Dec. 2023).

4. See e.g. the measures proposed by the European Commission and in the meantime to a large extent agreed by the legislators implementing the former's Green Deal Industrial Plan for the Net-Zero Age (COM(2023)62 final). This is a response to the European Council's call of 15 Dec. 2022 for such a plan (cf. para 15 of its conclusions, EUCO 34/22).

5. Commission Joint Research Centre (JRC) Science for Policy Report, "Shaping & securing the EU's open strategic autonomy by 2040 and beyond", 2021 Publication Office of the European Union.

6. See Editorial comments: "Keeping Europeanism at bay? Strategic autonomy as a constitutional problem", 59 CML Rev. (2022), 313–326; Smulders in "The new geopolitical dimension of the EU competition and trade policies", the XXX FIDE Congress in Sofia (Korzenov, Ed.), 2023 Congress publications, 119–144; Hoffmeister, "Strategic autonomy in the EU external relations law", 60 CML Rev. (2023), 667–700.

7. See COM(2021)66 final, "Trade policy review – An open, sustainable and assertive trade policy".

that vigorously compete, grow, innovate, benefit from a level playing field both in the internal market and globally, and give customers a choice of products and services, contributing to reliable and diverse supply chains. Legally, the most important challenge to enable a mix of instruments to pursue these objectives is to ensure a proper legal basis therefor in the Treaties. Most of the time, at least as regards the legislation adopted for that purpose, the choice has fallen on the internal market legal basis (Art. 114 TFEU) as one or very often the sole basis, without triggering much, if any controversy among institutions, Member States or other interested parties, as illustrated by the absence of any pending litigation challenging the choice of the legal basis.[8] The questions that arise are more of a substantive nature: whether the EU's industrial policy, controversially inserted in the Maastricht Treaty in what is now Article 173 TFEU, risks clashing with the very essence of the internal market based on openness and non-intervention by States.[9] At the core of this discussion lies the inherent ambiguity in the definition of the concept of industrial policy, ranging from narrow notions of targeted public support to selected firms, to broad interventions aimed at structurally strengthening entire sectors of domestic industry. Looking at the EU's integrated approach, as reflected by policy statements implemented by a series of legislative and other actions, it would seem that its views in this respect are closer to, for example, Criscuolo et al.[10] They propose a very broad interpretation of industrial policy, encompassing all interventions intended to improve structurally the performance of the domestic industry, comprising a vast set of instruments, ranging from the design of intellectual property protection to public procurement, R&D incentives or public support to the provision of skills.

State aid control and the EU's competitiveness

It is submitted that an unqualified dismissal of industrial policies seems neither congruent with a reasoned analysis of the scope for efficient public

8. See e.g. the European Commission proposals for the so-called European Net Zero Industry Act (see note 14 *infra*), the so-called European critical Raw Materials Act (a regulation of the European Parliament and the Council establishing a framework for ensuring a secure and sustainable supply of critical raw materials (COM(2023)160 final), as well as the so-called European Chips Act (Regulation (EU) 2023/1781 of the European Parliament and the Council establishing a framework of measures strengthening Europe's semiconductors ecosystem, O.J. 2023, L 229/1).

9. See e.g. Editorial comments: "Paying for the EU's industrial policy", 60 CML Rev. (2023), 617–624.

10. See Criscuolo, Lalanne and Diaz, "Are industrial policy instruments effective? A review of the evidence in OECD countries", 2020 OECD Science, Technology and Industry Working Paper.

intervention in markets, nor useful in response to legitimate concerns about the limits of a *laissez-faire* approach to markets. In an integrated economy, with significant interdependencies through global supply chains and trade, industrial policies conjure the spectre of global subsidy races, where governments around the world compete through subsidies and tax breaks to attract investment, promote the use of local inputs and support exports. Such subsidy races can easily lead to wasteful dissipation of public resources with limited or no efficiency gains, resulting in net transfers from taxpayers to industrial beneficiaries of aid with regressive impacts on equity. For an economic block as significant as the EU, these risks need to be factored in when formulating any industrial policy. As explained below, while *rent-shifting* industrial policies tend to be ineffective, policies aimed at achieving greater efficiency can be potentially helpful.[11]

What does this mean concretely? Whilst it may be clear that the EU's long-term objective is to pursue a growth strategy based on the green and digital transitions and tapping the full potential of new technologies, there is growing consensus among the EU's political leaders, as reflected by multiple European Council conclusions since the end of last year, this should not be to the detriment of its competitiveness, particularly not vis-à-vis its main trading partners, China and the US. The fact of the matter is that these transitions must take place under very difficult circumstances. First the Covid-19 pandemic, and now the economic consequences of Russia's war of aggression against Ukraine, have exposed dependencies that can harm the competitiveness of EU industry and risk slowing down the transition towards a net-zero economy.

As a response to these challenges and following a request of the European Council in December 2022, that in turn followed the adoption of the US Inflation Reduction Act,[12] at the beginning of 2023 the Commission presented the Green Deal Industrial Plan to strengthen the competitiveness of Europe's net-zero industry through a predictable and simplified regulatory framework and faster access to funding, skills and open trade for resilient supply chains.[13] In the same context and to ensure in particular faster access to net-zero technologies, the Commission proposed also a so-called Net Zero Industry Act.[14] The Act's aim is to enable investments in strategic technologies along the supply chain and simplify and accelerate the authorization of new clean

11. See Piechucka, Sauri-Romero and Smulders, "Industrial policies, competition and efficiency", (2023) *Journal of Competition Law and Economics*.

12. See note 36 *infra*.

13. See note 4 *supra.*

14. See European Commission proposal for a regulation of the European Parliament and the Council on establishing a framework of measures for strengthening Europe's net-zero technology products manufacturing ecosystem (Net Zero Industry Act), COM(2023)161 final. Its legal base is Art. 114 TFEU.

technology production sites. It also aims to ensure that at least 40 per cent of the annual deployment needs of strategic net-zero technologies are manufactured in the EU by 2030. Already as a follow-up to the updated EU industrial strategy of May 2021,[15] a co-creation process was started with industry, public authorities, social partners, and other stakeholders, to jointly agree on an action plan for each industrial ecosystem. In the same vein, the European Commission recently presented a Wind Power package to allow fast-tracking permitting, improving auction systems, focusing on skills, ensuring access to finance, and maintaining stable supply chains.[16]

But *where* does State aid control fit into all of this – and, more importantly, *how* does it fit in? From the following Commission guidelines, it appears that the green and digital transition has not been some afterthought of crisis firefighting, but a deliberate and long-term reorientation of State aid control in the last few years to support huge investments required to make this transition happen:

- The Climate, Energy and Environment Aid Guidelines (CEAG),[17] adopted early 2022, play a critical role in supporting the Green Deal objectives. The Guidelines facilitate State aid in new technologies that are important for the green transition, while also seeking to crowd in private investment. They broaden the scope of the previous guidelines to new areas (industry, clean mobility, circularity, and biodiversity) and to technologies that should contribute to the EU de-carbonization goals.
- The State aid rules on Important Projects of Common European Interest (IPCEIs),[18] updated in 2021, promote ambitious cross-border collaborations between Member States and industry. IPCEIs are supposed to contribute to the development of FOAK (first of a kind) technologies and production processes in all areas of the economy that can contribute to the Green Deal objectives, where the market alone would not deliver.

15. COM(2021)350 final, "Updating the 2020 Industrial Strategy: Building a stronger Single Market for Europe's Recovery".

16. COM(2023)669 final, "European Wind Power Action Plan".

17. European Commission Communication "Guidelines for State aid for climate, environmental protection and energy", O.J. 2022, C 80/1, based on Art. 107(c) TFEU.

18. European Commission Communication "Criteria for the analysis of the compatibility with the internal market of State aid to promote the execution of important projects of common European Interest", based on Art. 107(3)(b) TFEU, O.J. 2021, C 528/10.

- The communication on State aid in relation to broadband networks (Broadband guidelines),[19] updated at the end of 2022, sets out rules under the which the European Commission will assess State aid contributing to the EU's objectives of ensuring gigabit connectivity for everyone and 5G coverage everywhere by the end of the decade, which is essential for the digital transition of the EU.
- The updated Regional State aid Guidelines (RAG),[20] also contribute by allowing public support to the least favoured regions to adapt to the green transition, while ensuring a level playing field between Member States. The RAG indeed maintain safeguards to prevent Member States from using public funds to trigger the relocation of jobs from one EU Member State to another.

However, relaxing State aid provisions, albeit temporarily and in a targeted manner, is not without risks for the integrity of the internal market. Whilst it is difficult to dispute that the Green Deal Industrial Plan and the corresponding State aid measures are a legitimate policy response to genuine and urgent challenges, one should not make the mistake of thinking that all problems that EU companies may face are imputable to a lack of funding – in particular *public* funding – and that State aid is the universal remedy. Other solutions are also required in the field of the regulatory frameworks around environmental and other planning permits, research and skills, and not least in the functioning of the energy market.[21]

Moreover, when relaxing State aid control for such legitimate purposes one should acknowledge that not all Member States have the same fiscal space for State aid.[22] To limit this risk of competition between Member States because of different fiscal capacity, the European Commission proposed to step up EU funding, leveraging the use of the existing REPowerEU and InvestEU

19. European Commission Communication "Guidelines for the application of State aid rules in relation to the rapid deployment of broadband networks", based on Art. 107(3)(c) TFEU, O.J. 2023, C 25/1.

20. European Commission Communication "Guidelines on regional State aid", based on Art. 107(3)(a) and (c) TFEU, O.J. 2021, C 153/1.

21. Arguably, the European Commission proposal for a European Parliament and Council regulation to improve the Union's electricity market design (COM(2023)148 final) based on Art. 194(2) TFEU, on which the legislators reached a political agreement in Dec. 2023 could have been a more appropriate instrument in that respect.

22. See overviews of the considerable amounts of State aid per Member State approved by the European Commission in 2022 and 2023, available at <competition-policy.ec.europa.eu/system/files/2023-06/state_aid_scoreboard_note_2022.pdf> and <competition-policy.ec.europa.eu/publications/competition-policy-briefs_en#state-aid-brief>.

Programmes as well as the Innovation Fund,[23] including a revision of the current Multiannual Financial Framework (MFF) but with limited success so far.[24] It would also be important to mobilize private funding, which will need to play the biggest part in the twin transition and ensure close collaboration with industry and between the relevant actors. For that reason, the Commission proposed the Strategic Technologies for Europe Platform (STEP).[25] This platform should leverage and direct EU funds for investments in fields like microelectronics, quantum computing, AI, biotechnologies, and clean technologies. And while STEP relies on the reprogramming and reinforcement of existing EU funding programmes for supporting strategic investments, it could become a testing ground for further steps towards a European Sovereignty Fund in due course. Finally, private funding would certainly also be boosted if the Banking Union and Credit Market Union were to be completed, a subject that may be addressed by the forthcoming high-level reports mentioned above that are due in the course of 2024.

Returning to the matter of State aid control and competitiveness, there is no denying that there are increased risks of distortion when the scope for State aid is broadened. Indeed, the State aid response to the successive crises of the last few years has been seized upon by some who believe that they have diagnosed a terminal decline of State aid control that would be on the losing side in a perceived conflict with industrial strategy.[26]

Is this diagnosis not correct insofar as these measures are consistent with the basic principles of State aid control, as they follow from the EU Treaties themselves, as interpreted by the Court of Justice of the European Union (CJEU)?[27]

To begin with, one could claim there is *a priori* no inherent conflict of purpose between industrial policy, such as the Green Deal Industrial Plan, and State aid control. Indeed, State aid control has always acknowledged objectives such as cohesion or the promotion of RD&I, rescue and restructuring or the roll-out of broadband which could arguably be labelled "industrial policy" objectives. There is no opposition here, as indeed there is no conflict between State aid control and an industrial policy that seeks to

23. These funds are essentially financed out of the EU budget and through the EIB and Member States are allowed to introduce chapters in their recovery and resilience plans, financed out of the EU's Recovery and Resilience Facility.

24. See para 24 of the European Council conclusions of 15 Dec. 2023, document EUCO 20/23. Compare also Editorial comments cited *supra* note 9, relativizing the impact of these different types of EU funding.

25. See European Commission proposal for a European Parliament and Council regulation establishing a Strategic Technologies for Europe Platform (STEP), COM(2023)335 final.

26. See e.g. "The EU's plan to regain its competitive edge", *Financial Times* (4 Nov. 2023).

27. See the case law cited *infra* in notes 29 and 30.

address market failures to speed up the green transition or – for that matter – to address insufficient investments to ensure security of supply or increase resilience against natural or geopolitical risks.

However, economists are likely to claim that such industrial policies only make sense, and are only justified, if they are efficient; meaning if they are designed in such a way as to avoid wasteful spending and unnecessary distortion of competition.[28]

This means choosing the appropriate policy tool. As stated above, subsidies are not a universal remedy. But in cases where subsidies appear to be the appropriate policy tool to address a market failure, the minimum necessary to incentivize the efficient behaviour should be quantified and allocated to the beneficiaries that are most effective in addressing the market failure.

The State aid principles of necessity, incentive effect and proportionality, following from well-established case law, do precisely this. The CJEU case law also confirms that the existence of market failure may often provide the most compelling evidence of the necessity for aid within the meaning of Article 107(3)(c) TFEU, even if, for that analysis, it is not the existence of a market failure in and of itself, but rather whether the State aid in question would facilitate certain economic activities.[29] The aforementioned principles are therefore entirely appropriate to ensure efficiency when subsidies are the appropriate tool to implement industrial policy. There are different techniques to do this – for instance by applying competitive tendering when possible, or by applying claw-back mechanisms that ensure that the taxpayers receive a return when investments lead to unexpected upsides. Public money should not crowd out private investment, but enable support to develop essential innovations, sectors and technologies that would be too risky or costly for markets to develop alone. State aid control should ensure the best possible use of scarce public resources and keep the public funding to the amounts necessary to address the market failure.[30]

A recent series of European Commission decisions concerning IPCEIs illustrate this approach.[31] As mentioned above, such projects benefit from

28. See Piechucka et al., op. cit. *supra* note 11.

29. See ECJ's landmark judgment in Case 730/79, *Philip Morris*, EU:C:1980:209, paras. 16–17. See also COM(2005)7 final, "State aid action plan – Less and better targeted state aid: A roadmap for State aid reform 2005–2009", and para 18 of COM(2012)209 final, "EU State Aid Modernisation", building on the case law regarding these principles.

30. See for an analysis, including references to ECJ case law and European Commission decisions Nicolaides, "Incentive effect of State aid – necessity and counterfactual", (2023) EStAL, 132–149.

31. See judgment in Case C-594/18 P, *Austria* v. *European Commission* (Hinckley Point C), EU:C:2020:742, paras. 67–68, confirming paras. 617–624 of the General Court's judgment

special rules to incentivize cross-border projects which go beyond the ordinary in terms of scope and ambition.

- Such aid must address a demonstrated market failure: it can only be given if, absent the aid, the project would not take place or only in a manner which would be significantly less beneficial.
- It must also be proportional; the aid can only cover the funding gap, meaning that it compensates for lack of profitability inherent in the market failure.
- And it must provide safeguards against a fragmentation in the internal market by ensuring that – on top of the cross-border nature of the project – there are significant spill-overs by, for instance, sharing the innovative findings across the European industry.

Over the last five years, the IPCEI framework has allowed EUR 27 billion of State aid which has leveraged an expected EUR 50 billion of private investment for the benefit of 208 undertakings in 255 projects involving 21 Member States and covering large parts of the semiconductor and hydrogen value chains.[32]

State aid and geopolitical tensions

Arguably, the same considerations could apply to State aid measures intended to address geopolitical risks and contribute to the EU's open strategic autonomy in so far as the right remedies for the right problems are identified.

Some challenges may concern EU firms lagging behind international competitors in sectors with lots of positive linkages, that is sectors with positive effects for other parts of the economy. The problem may be related to positive externalities: unless companies can monetize these broader positive benefits, they will not have incentives to invest. A market failure of this nature

and following para 104 of A.G. Hogan's Opinion. See for an analysis of the relevance of a market failure for the assessment of the compatibility of a State aid measure e.g. Schwabe, "Klassische Marktversagensgründe: Staatliche Beihilfen als Instrument zur Korrektur von Marktversagen" in *Munchener Kommentar zum Wettbewerbsrecht* (Beck, 2022). Further reflections on what the reasons are for the existence of a market failure, e.g. a lack of legislation creating the conditions for a deepening of the internal market in a given sector, would merit a separate article.

32. See for recent European Commission decisions on IPCEI on microelectronics 1: <competition-cases.ec.europa.eu/cases/SA.46578>; <ec.europa.eu/competition/state_aid/cases1/201952/277354_2120329_283_2.pdf>: on batteries: <competition-cases.ec.europa.eu/cases/SA.54801>; <ec.europa.eu/competition/state_aid/cases1/202231/SA_54801_60A43582-0000-CEC2-BCDC-018723136555_325_1.pdf>; <competition-cases.ec.europa.eu/cases/SA.55858/>.

may be addressed, for instance, by means of subsidies that make up for the lack of incentive, thus increasing overall efficiency.

Another reason why some sectors may lag behind are coordination failures, for instance when actors at different levels in the value chain must simultaneously invest and ramp up production to commercialize a new technology. The level of market integration in the EU means that an efficient response to global challenges de facto requires coordinated policy interventions. Such market failures could in some cases be addressed through the IPCEI rules or under Article 107(3) TFEU. The various IPCEI for hydrogen innovation and first industrial deployment are recent examples of State aid towards nascent clean technologies, coordinated at EU level.

Other geopolitical liabilities may be linked to an exposure to extraneous shocks, such as the exposure to excessive risks of shortages in certain industries because of natural or geopolitical events.

Possible solutions include diversification of extra-EU suppliers, stockpiling, building limited subsidized domestic capacities or investing in adaptation of production sites to facilitate supply side substitution. Some solutions could perhaps take the form of State-aided Services of General Economic Interest (SGEI), coordinated at EU level, as mentioned in the European Commission communication on "Addressing medicine shortages in the EU".[33]

Another geopolitical tension arises when the EU is called upon to respond to industrial policies by other jurisdictions. Here, it is preferable to design defensive strategies instead of offensive strategies that would aggravate the risks of subsidy races and protectionist spirals. An example of this targeted approach is the possibility to grant so-called matching aid under the European Commission's Temporary Crisis and Transition Framework (TCTF).[34] This allows Member States, in certain well-defined situations, to grant higher support to individual companies when there is a real risk of investments being diverted away from Europe, subject to several safeguards.

Looking also beyond the borders of State aid proper, the Foreign Subsidy Regulation[35] which entered into force on 12 July 2023, is precisely such an instrument. By, in a way, extending the discipline of classical State aid control

33. See COM(2023)672 final, "Addressing medicine shortages in the EU".

34. See para 2.8 of the European Commission Temporary Crisis and Transition Framework for State Aid measures to support the economy following the aggression against Ukraine by Russia (based on Art. 107(3)(b) TFEU), a consolidated version is available at <competition-policy.ec.europa.eu/state-aid/temporary-crisis-and-transition-framework_en>. It is submitted that this clause is a response to certain subsidies that may be granted under the IRA.

35. See European Parliament and Council Regulation (EU) 2022/2560 on foreign subsidies distorting the internal market, O.J. 2022, L 330/1.

to certain subsidies given by third countries to companies operating on the EU's internal market, it contributes to a level playing field on that market.

Nonetheless, coordinated approaches across jurisdictions that avoid inefficient industrial policies oriented merely to stealing away each other's businesses are obviously preferable. It leads to higher welfare for all by exploiting the efficiencies that open economies can deliver. It is in that light that the discussions between the EU and the US on certain adverse effects on the latter's Inflation Reduction Act (IRA) should be welcomed.[36]

Provided it remains faithful to a series of principles, deriving from well-established European Commission practice and CJEU case law, EU State aid control can not only fit in but also contribute to the integrated approach which the EU is currently designing and implementing to increase its resilience and competitiveness in an increasingly unstable geopolitical environment. Having a robust framework of assessment, as provided by State aid control rules, can improve the overall design of climate and industrial policies, contribute to a more efficient green transition, preserve competitive markets, and foster the EU's industrial competitiveness. EU State aid control should improve the efficiency of aid. By ensuring the aid is granted only when necessary and in a manner that is proportionate and targeted, it helps in addressing certain market failures or public policy objectives more efficiently. By focussing on areas where aid can be most effective and avoiding over subsidization, this control maximizes the utility of public resources.[37]

36. See COM(2023)684 final, "Report on EU policy initiatives for the promotion investments in clean technologies", assessing also the impact of the IRA on the EU economy. See also the recent study carried out by Bocconi University, "The impact of the US Inflation Reduction Act on the European industry", available at <iep.unibocconi.eu> publications. See for a thought-provoking article on the subject Gros, "The transatlantic subsidies race we need", available at <www.project-syndicate.org/commentary/eu-green-industrial-policy-should-subsidize-tech-innovation-by-daniel-gros-2023-02>.

37. See Piechucka et al., op. cit. *supra* note 11.