

**Submission from Professor Steve Fothergill  
Legislative Consent on the UK Subsidy Control Bill  
December 2021**

*Personal note*

*This submission draws on my role as an academic on regional development and on my role as National Director of the Industrial Communities Alliance (ICA), the all-party association of local authorities in the older industrial areas of England, Scotland and Wales. In all essential aspects, my views on Subsidy Control as an academic coincide with those of the ICA national body and ICA Scotland.*

**What the Bill does and does not do**

Following Brexit, EU State Aid rules no longer apply in the UK (Northern Ireland excepted) so the Bill aims to replace them with UK rules. There is a clear need for rules of this kind to govern public financial support to private sector businesses because the alternative would be an unhelpful free-for-all.

Essentially, the UK Government is taking over the role the EU previously played. This is necessary, and seems reasonable. The UK Government also has the power to do so under the Internal Market Act.

Whilst the Bill sets the rules (or, more accurately, the framework within which the detailed rules will eventually be set) what it does not do is determine how much is then spent on subsidies. In this respect the new UK regime is no different from the EU rules it replaces. Under the EU rules the UK actually spent substantially less per head than comparable member states. This divergence was a political choice, not a result of the rules themselves.

Under the new UK regime, the focus and volume of spending within the rules will remain a political choice. In this respect, therefore, nothing is changing. For example, Scottish Enterprise has for many years provided *Regional Selective Assistance* to support investment that creates or protects jobs in less prosperous areas whereas in England the equivalent budget line was discontinued in 2015. Under the new Subsidy Control regime, the Scottish Government will retain discretion to design and fund its own schemes of financial support, provided of course that they are compatible with the new UK rules.

## **The principles underpinning the Bill**

The Subsidy Control Bill defines seven ‘principles’ with which all subsidies have to be consistent. In summary, these are that subsidies should:

- Aim to remedy an identified market failure
- Be limited to what is necessary
- Bring about a change in the economic behaviour of the beneficiary
- Not meet costs that the beneficiary would anyway have funded
- Be appropriate for an objective that cannot be achieved through other means
- Have benefits that outweigh any negative effects on competition and trade
- Minimise distortions to the UK internal market

The first six of these principles are taken straight from the December 2020 trade agreement with the EU and replicate the principles underpinning the EU rules. The seventh is the UK Government’s own addition, intended to head off ‘subsidy wars’ between different parts of the UK. All these principles seem reasonable.

The Bill includes a limited number of prohibitions – for example subsidies to exports or against imports (prohibited under WTO rules), open-ended bail-outs or guarantees, and subsidies to transfer production from one part of the UK to another. The Bill also raises the level below which the rules won’t apply (the ‘de minimis’ threshold) to £315,000 over three years. These provisions also seem reasonable, indeed desirable in the case of the higher ‘de minimis’ threshold. Other parts of the Bill define institutional structures and processes.

## **Strategic concerns**

### *Lack of detail*

The intention is that there will be ‘streamlined routes’ for subsidies at low risk of causing market distortions. This looks very much like the EU’s General Block Exemption Regulations (GBER) which used to govern the vast majority of State Aid, though the UK Government denies the similarity. Like GBER, the UK’s streamlined routes will require detailed rules to define the subsidies that do not require further scrutiny.

Officials have emphasised the importance of judging schemes against the ‘seven principles’ and indicated that there is unlikely to be guidance as detailed as the EU rules. This is likely to pose problems for most public bodies. Whereas the EU rules used to provide certainty – if a subsidy was within GBER limits it was clearly OK – but an assessment against principles will often be subjective and open to challenge, and in many cases risk-averse public bodies will seek reassurance that their decisions won’t end up in court. Exhaustive assessments, perhaps involving consultants and lawyers, may consequently become the norm. If the UK Government fails to provide detailed

rules it is therefore likely to push a large and unwelcome administrative burden on other players, including local authorities and the devolved administrations.

The UK Government has said guidance will be published, ahead of the new regime coming into force in 2022, to help public authorities comply with the obligations set out in the new regime.

### *Failure to consult*

It would be fair to say of the new UK Subsidy Control regime that ‘the devil is in the detail’ but that the Bill does not set out these details, which will follow in guidance and statutory instruments. This places an enormous amount of discretion in the hands of UK Government ministers.

Prior to publication of the Bill, the UK Government carried out a public consultation on the intended legislation. Having undertaken this in the spring of 2021 it seems that civil servants, at least, feel they have discharged the UK Government’s responsibility to consult. With so few details settled, this is surely wrong.

A comparison with the way EU rules were settled is illuminating. Take the rules on regional investment aid for example:

- The EU issued draft rules for consultation, dealing with issues including aid intensity ceilings, population coverage, eligible investments and the treatment of large and small firms
- When the EU rules had been finalised, the UK Government issued a consultation on how the available population coverage of Assisted Areas should be allocated within the UK
- The UK Government then issued a further consultation on the draft Assisted Area map

This was not a swift process but it was important in building a measure of consensus. The UK Assisted Area map that emerged, for example, did not then prove to be major source of contention.

It is presently far from clear that the UK Government has any intention to engage in consultation on the details of the new Subsidy Control rules.

### *Implications for regional development*

The UK Government says the guidance “*will promote considerations intrinsic to the levelling up agenda and set out the criteria for promoting economic development of relatively disadvantaged areas*”. It also says “*the functioning of the new regime does*

*not require any map prescribing disadvantaged areas” though it adds that “we will further consider if any future UK map may be relevant to consideration of disadvantaged areas for the purposes of the subsidy control system”.*

This leaves important elements of UK regional development policy in limbo. The Subsidy Control regime should in theory help Levelling Up – indeed, it is difficult to see how this can be delivered without deploying tools such as investment aid in less prosperous parts of the country – but whether this will be the case remains unclear.

The UK government will nevertheless need to be mindful that the *Joint Declaration on Subsidy Control Policies*, signed as part of the trade agreement with the EU, says:

*“Subsidies may be granted for the development of disadvantaged or deprived areas or regions. When determining the amount of subsidy, the following may be taken into account:*

- *the socio-economic situation of the disadvantaged area concerned;*
- *the size of the beneficiary; and*
- *the size of the investment project”*

It is difficult to see how the UK can abide by this particular agreement without a map to define ‘disadvantaged areas’.

The UK had an Assisted Area map long before it joined the EU. Indeed, the very idea of a map was one the UK persuaded the EU to adopt. The map has evolved over the years, reflecting the shifting geography of jobs and prosperity. In the 2014-20 version under EU rules, Assisted Area status covered a quarter of the UK population but 41 per cent of Scotland’s population, reflecting more extensive areas of economic disadvantage.

An Assisted Area map defines the places where higher levels of financial support can be given to businesses. This helps attract new investment, and in turn to create and protect jobs in less prosperous parts of the country. It means that more generous subsidies are allowed in Kilmarnock than in Kensington, or in Sutherland than in Surrey. Without a map, everywhere ends up being treated equally.

- There needs to be a new UK Assisted Area map. Reliance on imprecise wording such as ‘disadvantaged areas’ as a basis for assessing the merit of each case for support would pave the way for the selective use of statistics, for manipulation and for inconsistency. It would also fail to provide any certainty for businesses when planning investments.
- The population coverage of the map needs to be increased to better reflect the widespread distribution of economic disadvantage across the UK, and the map might include a hierarchy of areas to reflect the intensity of disadvantage.

- The new map should be drawn following full consultation, in line with previous practice.
- Aid intensity ceilings should be raised to a level likely to make a difference to business decisions, and the flexibility to support re-investment by larger firms in existing plants should be restored along with Assisted Area top-ups for R&D, SMEs and training.

On all these points the jury is still out. The outcome matters across substantial parts of Britain, including the less prosperous parts of Scotland.

### **So how should the legislation be modified?**

The Scottish Parliament and Government need to be pragmatic. With a large parliamentary majority, the UK Government is able to push through the Bill in its present form if it chooses to do so. Whilst it might be desirable for the legislation to include additional provisions this may be a forlorn hope.

What is important, therefore, is that the Scottish Government weighs in vocally and persistently in the debate around the legislation, bearing in mind that just about all the important details will not be settled when the Bill becomes law but only when guidance and/or statutory instruments begin to emerge. In particular, it would be good if the Scottish Government, supported by the Parliament, could focus on:

- The need for a new UK Assisted Area map, to ensure that higher levels of financial support are allowed to help support investment and jobs in the less prosperous parts of Scotland and the rest of Britain.
- The need for full consultation, prior to finalisation, on the operational details and rules of the new Subsidy Control regime.

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