

**COMMUNICATION FROM THE COMMISSION****CONSULTATION DOCUMENT  
ON STATE AID FOR INNOVATION**

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**AFEP COMMENTS**

Following upon the publication of the European Commission's Action Plan on State aid, to which the Association Française des Entreprises Privées (AFEP) responded on 15 September 2005, the Commission has launched a consultation to identify specific measures to improve State aid for innovation.

AFEP represents more than 85 private companies that include some of the most significant players in the French economy. The purpose of AFEP is to present the views of large French companies to the European Institutions and the French authorities, mainly with regard to the drafting of non-sectoral European Community legislation (on the economy, taxation, company law, financial information, competition, social regulations, employment legislation, environment, intellectual property rights, etc.).

AFEP member companies are in favour of a reflection on State aid to innovation, given that innovation is at the heart of growth and that the contribution of large companies is essential to its development.

In this context, the large companies would like to reiterate some of the positions they previously communicated in response both to the Action Plan and to the European Commission's questionnaire concerning the review of the guidelines for State aid for environmental protection, and to reply more specifically to those questions that concern them directly.

AFEP member companies would very much like to see the Commission take greater account of the international context (1), and once again call for a more precise definition of the concept of "market failure", without, however, making this criterion exhaustive (2). Moreover, they deem that aids to innovation should be the subject of a distinct set of guidelines (3). Finally, the role of large companies in the process of innovation and in the criteria limiting the intensity of State aid should be reconsidered by the Commission (4).

## **I. Large companies would like the international context to be taken into account**

The large companies within AFEP are surprised that the consultation document issued by the Commission fails to take into account the international context. For these firms, the reform under way cannot be carried out without a solid reflection on the way research and development is structured and carried out at the international level.

Thus they regret that, like the Action Plan, this new consultation document omits all consideration of the international environment in which companies operate. It is essential that the European Union should include, in its reflections, the existence of public aid mechanisms or subsidies that European competitors in third countries may receive, and most particularly those in emerging economies.

It would indeed be highly damaging to the European economy if the large companies based in the Union were to be penalised, at the international level, by a disloyal competition on the part of other actors. If access to public financing were to be denied them or rendered particularly difficult, they might prefer, for instance, to locate their research departments in parts of the world where no such constraints exist business.

State aid policy should, moreover, take into consideration of public interventions that seriously distort competition, and should concentrate on the most blatant anti-competitive practices which result in placing companies in uneven situations.

## **II. The concept of “market failure” should be defined and considered alongside other criteria**

If companies welcome the Commission’s explicit intention to develop a rigorous economic approach that will help justify a relevant State aid policy, the large companies cannot but express their concern regarding its use of the concept of “market failure”. At a time when the definition and use of this term arouse numerous reservations on the part of large companies, especially in the field of innovation, this notion can serve as a pretext for the Commission to exclude these companies by definition from the group of potential beneficiaries of such aids.

Market failure cannot be defined as an complete absence of market forces, for that would mean one could not speak of « aid » at all unless some restriction on competition or some impact on intra-community trade were identified. It is, moreover, difficult to define the contours of this notion. It would therefore be useful if the Commission were to outline concretely what is understood by this term, rather than simply declaring, in a quasi-tautological manner, that a market failure is “when the market on its own does not lead to an economically efficient outcome.”

Such a definition is too general and formal to serve as a true guide and criterion for action. It is nevertheless used by the Commission to justify discriminating between large companies and SMEs.

Moreover, the large companies recall that the Commission ought to be able to use the notion of market failure not only in order to justify a State aid (in keeping with article 83 of the Treaty) but also when qualifying an aid (according to article 87-1). Thus, different parameters relating to the market should be taken into account, and in particular the competitive context in which companies operate, the distortions to competition in relation to non-EU member states, the organisation of the innovation process, or the difficulties in absorbing the costs.

### **III. Aid to innovation should be the object of a separate set of guidelines**

The European Commission deems that it is not necessary to create a new and distinct set of guidelines for aid to innovation, insofar as various activities have been identified the aim of which is to correct market failures that hamper innovation, and where the advantages resulting from State aid are likely to surpass any potential impediment to competition and trade.

In response to question 1 of the consultation document, and contrary to the Commission's view, the large companies deem it highly desirable to have specific guidelines for State aid for innovation, and for a number of reasons.

A set of guidelines specifically for innovation, the aims of which are to simplify procedures, would offer greater visibility to companies, who could easily refer to a text defining the principal strategic directions in this area. Such clearly established guidelines would also help to limit the possibility of competitors gaining undue advantages.

Since bringing to market innovative products or services can require greater financial commitment on the part of companies than investment in research and development, a specific set of guidelines for aid to innovation is justifiable for this reason as well.

Moreover, aware of the difficulty of coming up with a precise definition of innovation, the large companies take note of the definition proposed by the Commission in points (1) and (22) of the consultation document.

The State aid policy should therefore be elaborated on the basis of this definition and of the principles defined within the context of a specific set of guidelines for innovation.

### **IV. The Commission ought to reconsider the role of large companies in the innovation process, and the criteria limiting the intensity of State aid**

The large companies first of all consider unjustified the distinction which the European Commission makes between them and the SMEs, as may be seen notably in questions 4, 12 and 20 of the consultation document dealing with poles of excellence in the EU.

These two sorts of structures are in fact most often partners at the economic level (common infrastructures, shared research teams, etc.) in poles of excellence or of competitiveness, with each party contributing to large-scale projects.

Creating distortions within these poles could only prove counterproductive, and would cause harmful administrative constraints.

In general the Commission does not provide any justification for the distinction it makes between SMEs and large companies. In the context of the reaffirmed Lisbon objectives and of a desire to secure the conditions for greater competitiveness on the part of European businesses, the inherently negative treatment of large companies seems to stem from a misunderstanding of the strong and

permanent interactions that exist between small and large companies in the areas of research and innovation, whether among independent SMEs or subsidiaries of large groups.

By way of example, when an SME has carried out the research and development portion, it often happens that a large company then takes charge of managing the process of bringing a product to market, since the latter often involves significant costs that the SME alone cannot fund.

Furthermore, the present system of State aid for R&D is based on a linear model of innovation made up of separate and sequential stages running from basic research to pre-competitive development, by way of industrial development. This model, and the accompanying limitation of maximum rates of intensity of State aid, are now out of step with the reality of R&D and innovation processes. We would suggest replacing the current categories of “industrial research” and “pre-competitive development” with a single category called « industrial research and technological development ». The minimum intensity allowed for this category would thus be 50%, in order to support research projects that are beneficial to competitiveness and to the job market in France and throughout Europe. Finally, it would be very important for this category of “industrial research and technological development” to include major stages for judging the validity and relevance of a research project, such as prototype, software, test phases and experimental launch.

### **Conclusion : encourage innovative capacity in Europe**

The preservation of the fundamentals that underlie the innovative capacity of companies presupposes that the international context is taken into account, and that the concept of market failure is used as one of the criteria for an economic approach that is as finely tuned as possible.

The European policy of State aid should also refer to the objectives of growth and development for R&D set by the Union in order to guide its decisions. In order to satisfy the Lisbon objectives, it is thus essential to give strong encouragement to developing industrial and technological innovation, which in turn presupposes a very strong involvement by large companies, whose role must not be underestimated.

Just as it does with respect to its technological platforms, so too in its State aid regime the Commission should identify those actors that are most likely to be innovative.

More generally, the rules applicable to State aid and community aid to research should be better coordinated, given their common objectives. It would be preferable to use existing notions at the community level, rather than inventing new concepts whose scope is not always evident.