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EFTA SURVEILLANCE  
AUTHORITY

Dear Sir/Madam,

**Subject: Communication on State aid for Innovation** HT 343

## I. Introduction

The Directorate for Competition and State aid (the "CSA") in the EFTA Surveillance Authority (the Authority) has reviewed the Communication on State aid for Innovation ("the Innovation Communication") issued by the Commission, which also forms part of the State Aid Action Plan for less and better targeted aid. The Innovation Communication called for comments to be submitted prior to 21 November 2005 and in response hereto the CSA respectfully submits the following comments.

As a preliminary point, the CSA welcomes many of the proposed changes to the existing legislative frameworks on state aid for research & development, risk capital etc. However, as will appear from the comments provided below, the CSA is not convinced that the introduction of a new concept of "*innovation*" or "*innovative activities*" is necessary and will in itself contribute value-added to the substance in the proposed changes. In this regard, it is generally recognised that the introduction of a new term or concept risks introducing legal uncertainty along with inherent potential risks of abuse and it should therefore only be done if strictly necessary. In line with the overall objective of simplifying the state aid rules, the CSA proposes therefore to integrate the relevant changes into the concepts already existing in the current frameworks (such as in the concept of "*industrial research*", "*risk capital*" etc.) and thereby avoid the addition of a new term to the already comprehensive legislative framework on state aid.

## II. Comments

### A. *Principles governing control of state aid for innovation*

It appears from point 6 in Section 1 of the Innovation Communication that the Commission will not provide a definition of innovation. Instead the Commission has identified a series of concrete and targeted innovation *activities* which address market failures that hamper innovation and where the benefits of aid outweigh the harm to competition. The new rules to be developed on the basis of the identified activities will define the limits within which state aid to innovation may be considered as compatible with the common market, and be integrated into existing legislation, such as in the frameworks on research and development (to be expanded to include innovation; OJ 1996

C 45/5), and risk capital (OJ 2001 C 253/3), as well as into the general block exemption, combining current rules in the area of SMEs, research, training, employment and possibly also environment.

The CSA fully agrees with the fact that a definition on innovation will imply a too high level of legal uncertainty to be implemented in practice with all the inherent risks of abuse. However, precisely for that reason it is not clear to the CSA what role the definition given in point 24 of Section 2.3 of the Innovation Communication will play. In point 24 of Section 2.3 of the Innovation Communication the Commission states that state aid for innovation can only be given to activities that relate to *“technological innovation”*. Footnote 4 provides a definition of the term by stating that technological innovation means *“...the implementation/commercialisation of a product with improved performance characteristics such as to deliver objectively new or improved services to the consumer.”* and *“...the implementation/adoption of new or significantly improved production or delivery methods.”*, which could possibly involve changes in equipment, human resources and working methods.

Since it is positively stated that state aid should only be authorized to *“technological innovation”*, it appears almost as if a definition of the concept of “innovation” is being introduced by the back door. In view of the fact that this term was (understandably) left undefined it is not clear to the CSA precisely what role the definition given in point 24 will play in the context of the ex-ante rules. In this respect the CSA is also questioning whether this term is intended also to apply in the context of examinations on a case-by-case basis. In the affirmative it would appear that such a new – and officially undefined – term can easily be abused.

#### **B. Open, transparent and non-discriminatory procedure**

In point 26 of Section 2.3 it is stated that *“in order to limit distortions of competition and negative effects on trade by unduly favouring some undertakings.”*, the beneficiaries of a given aid measure should preferably follow an open transparent and non-discriminatory procedure (for example as regards EU country of origin). The CSA is not certain of the Commission’s intention with this request.

First, if the criteria for qualifying as state aid are met it has already been determined that the measure *is* selective and for that reason the measure *will* per definition be favouring certain undertakings (or productions). In this regard the request for non-discrimination seems to contradict with the fact that a state aid measure has already been identified as a selective measure (otherwise it would not involve state aid).

Secondly, a request for a public tender in order to provide state aid seems to pre-empt the outcome of the discussion of whether a public tender may exclude the presence of state aid. In this regard a request for an open tender *in order to provide state aid* appears to be based on a view that the public tender cannot in itself exclude the possibility that state aid is involved. However, if a state launches a non-discriminatory public tender for the supply of a product/service in return for compensation,<sup>1</sup> it would appear that the only manner in which state aid can be involved is by means of over-compensation (in which case this factor would make the tender discriminatory after all).

This means that if the Commission calls for a public tender in order to improve the possibilities for considering innovation aid as compatible, it is based on a presumption that

<sup>1</sup> The other more rare case is the possibility to launch a public tender in order to award a grant.

there has been over-compensation involved - otherwise there would have been no state aid involved in the first place - and no reason to discuss compatibility.

Based on the above, the CSA takes the view that rather than calling for open public tenders in the context of identifying conditions under which state aid for innovation activities may be authorized, this request could be reformulated into a general encouragement for public tenders for innovation activities in order to avoid that state aid is involved at all. A cross-reference could then be made to this general request in the context of discussing the conditions under which state aid for innovation activities may be found compatible. In this context it could be explained that where the Commission comes to the conclusion that state aid is involved - despite the fact that a non-discriminatory public tender has been held - the fact that a public procurement procedure was followed will, however, be taken positively into account in the context of the compatibility assessment.<sup>2</sup>

### **C. *Support risk-taking and experimentation***

In Section 3 of the Innovation Communication it is proposed to authorize aid to support risk-taking and experimentation. This covers aid to

- (a) Innovative start-ups intending to develop products and processes which are technologically new or substantially improved compared to the state of the art in its industry in the Community;
- (b) risk capital by increasing the flexibility in assessing risk capital and adding specific provisions for post-seed stages; and
- (c) adding further activities eligible for state aid to the research and development framework (referred to as the last research & development stage of pre-competitive activities or as the "experimental development stage").

The proposal is limited to SMEs and is based on the problem of under provision of private funding for projects with a high risk failure and high transaction costs.

The CSA notes that the proposed rules appear to be the result of a review and fine-tuning of the concepts in the frameworks on risk capital and research & development rather than introducing a new substantial area for authorizing state aid.

In this regard the proposal to increase flexibility to grant aid for risk capital, as well as the inclusion of further activities to the last research & development stage are changes that clearly do not necessarily relate to a new concept of "*innovation*". Even the proposal to grant aid to "*innovative start-ups*" (which are younger than five years and which must produce technologically new or substantially improved products) seems at large already to be covered (or with few amendments could be covered) by the present concept of risk capital in the framework on that subject. In this regard the risk capital framework contains specific provisions for authorizing aid to medium-sized companies in their start-up period or other early stages.<sup>3</sup>

<sup>2</sup> This would also ensure a better consistency with the research and development framework which provides that the presumption is that there is no aid involved if research and development contracts are awarded on market conditions and on the basis of an open tender procedure in accordance with the Community rules on public procurement.

<sup>3</sup> See in this regard Section VIII.3 of the framework on risk capital which provides that in assessing compatibility of risk capital the fact that the company is a medium-sized enterprise in its start-up or other early stages will be regarded as a positive element. In this respect the footnote refers to a definition by the

Moreover, one could question whether the assessment for identifying “*technologically new or substantially improved* [products or processes] *compared to the state of the art in its industry in the Community*” is very different from the assessment carried out in the context of the research and development framework for purposes of authorizing aid to “*industrial research*” (defined as “*...planned research or critical investigation aimed at the acquisition of new knowledge, the objective being that such knowledge may be useful in developing new products, processes or services or in bringing about a significant improvement in the existing products, processes or services.*”).

In the light of the above, the CSA is concerned that the introduction of the concept of “*innovation*” or “*innovative activities*” might confuse rather than clarify without adding a substantially new area for authorizing state aid. It seems that a more coherent and simple approach would be to focus on improving, nuancing and expanding the current concepts and thereby limit the scope for un-intended abuse in the future.

#### **D. Aid to support the business environment for innovation**

In Section 4 of the Innovation Communication it is proposed to authorize aid to support the business environment for innovation. This covers aid to the (a) purchase of research and/or business advisory services and services for the provision of facilities; (b) recruitment of qualified personnel or compensation for personnel loan; and (c) collaboration and clustering. The proposal is centered/limited to SMEs and is based on the fact that SMEs do not have the funding to pay for business specific services, recruit qualified personnel etc.

The CSA welcomes the proposal in Section 4 of the Innovation Communication to grant aid to SMEs for purchasing services from clearly defined Innovation Intermediaries. The CSA takes a similar view as regards the proposal to support SMEs for purposes of recruiting highly qualified researchers and engineers and the temporary loan of company personnel or University personnel to SMEs. However, in line with the comments given above, the CSA is questioning whether the recruitment and loan of qualified personnel should be limited only to “*innovation activities*”? It would appear that support for similar measures in the area of research and development could equally be included.

Finally, the CSA considers that the suggestion to change the research & development framework to support technology platforms in the form of collaboration and clustering is constructive. The CSA also welcomes the proposal to relieve a company from giving back *all* the results of the research & development where the work has been carried out in cooperation between industry and public institutes, provided, however, that this new provision will not be limited merely to “*innovation activities*”.

The CSA is similarly positive towards the suggestion to authorize aid to provide infrastructure in grey or white areas with insufficient broadband coverage. However, in view of the fact that broadband has been on the market for quite some time already the authorization of aid to broadband infrastructure on the grounds that it concerns “*innovative activities*” appears to be misleading. If the intention behind this proposal is to authorize aid in order to improve the general technological infrastructure standards

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European Venture Capital Association which defines “start-up financing” as “‘*financing provided to companies for product development and initial marketing. Companies may be in the process of being set up or may have been in the business for a short time, but have not sold their product commercially*’ and other early-stage as ‘*financing to companies still in the stages of research and product development or that have completed the product development stage and require further funds to imitate commercial manufacturing and sales. They will not yet be generating a profit.*’”

available to the general public then authorization of aid to projects concerning broadband infrastructure or third generation telephone networks, for example, should rather be given by reference to the fact that such projects are considered to improve infrastructure of a technological nature, in general (as opposed to a more limited authorization ground of "*innovative activities*").

Yours faithfully,



Amund Utne

Director

Competition and State Aid Directorate