


***CONFCOMMERCIO COMMENTS TO THE EC CONSULTATION ON STATE AID  
FOR INNOVATION***

*09/11/2005*



QUESTIONS ADDRESSED BY THE EUROPEAN COMMISSION IN THE CONSULTATION  
DOCUMENT

*Question 2) Do you think that the problems presented in Annex and the market failures identified by the Commission as hampering the innovation process are accurate? If so, why? If not, why not?*

Market failures identified by the European Commission (EC) do not seem to stress enough that they can concern both products and services.

The definition of technological innovation provided in the EC's communication "*Consultation document on state aid for innovation*" refers to point 24 of Oslo Manual "24. A technological **product** innovation is the implementation / commercialisation of a product with improved performance characteristics such as to deliver objectively new or improved services to the consumer. A technological process innovation is the implementation/adoption of new or significantly improved production or delivery methods. It may involve changes in equipment, human resources, working methods or a combination of these." (see footnote n. 4 on page 7 of the Communication).

Respect to the term "**product**", the Oslo Manual clarifies that it refers both to tangible products and services "21. The body of the manual concentrates on new and significantly improved products (**goods and services**) and processes." And also, "134. The term "**product**" is used to cover both goods and services".

Points 21 e 134 are integral part of the definition of innovation given in the Oslo Manual. When the EC accepts this definition of innovation, it implicitly admits that innovation concerns both tangible products and, also services.

From a sectorial point of view the Oslo Manual clarifies that the definition of technological innovation includes all the market services: "125. Innovation can of course occur in any sector of the economy, including government services such as health or education. Given the focus on the firm, the concepts and definitions that will be presented in this manual are mainly designed to deal with innovations in **the business enterprise sector.**"; "128. Nevertheless, the definitions and concepts used in this manual have been adapted, on the basis of experience gained so far, to apply to **TPP innovations in manufacturing, construction, utilities and marketed services.**"

Finally, as additional proof that market services (commerce, HORECA, etc.) are included in the innovation definition of the Oslo Manual, you have to consider the enumeration of sectors at point 212 of the Manual (see chart 1).

Given these premises, [we underline that] both general principles (par. 2) and aid rules (chap. 3-4) foreseen in the Communication, vice versa, do not seem to clarify enough that the targeted typologies of innovation subject to public support concern both products and services.

That is why, we ask that in the part related to general principles and in the rules for aids it will be clearly stated that public interventions in favour of technological innovation can concern both products and services.

**Table 1. Industrial classification proposed for innovation survey in the business sector based on ISIC Rev. 3 and NACE Rev. 1**

Title	ISIC Rev. 3 Division/Group/Class	NACE Rev. 1 Division/Group/Classes
.....		
MARKETED SERVICES	50 to 74	50 to 74
Sale, Retail, Maintenance & Repair of Motor Vehicles & Motorcycles	50	50
Other Wholesale Trade	51	51
Other Retail Trade	52	52
Hotels & Restaurants	55	55
Land Transport & via Pipelines	60	60
Water Transport	61	61
Air Transport	62	62
Supporting & Auxiliary Transport Activities, Travel Agencies	63	63
Post & Telecommunications	64	64
<i>Post</i>	641	64.1
<i>Telecommunications</i>	642	64.2
Financial Intermediation	65 to 67	65 to 67
Real Estate, Renting	70+71	70+71
Computer & Related Activities	72	72
<i>Software Consultancy &amp; Supply</i>	722	72.2
<i>Other Computer Services n.e.c.</i>	72 less 722	72 less 72.2
Research & Development	73	73
Other Business Activities n.e.c.	74	74
<i>Architectural, Engineering &amp; other Technical Activities</i>	742	74.2

Source: OECD - Oslo Manual, page 46

**Question 5) Stakeholders are invited to provide empirical evidence about the appropriateness of authorising State aid to non-technological innovation, notably in services sectors**

The outrun of the linear model of innovation (*technology-push*) with the adoption of *chain-linked* models (see also point 88 of the Oslo Manual) goes back to the '80s (Kline, Steven, Rosenberg, 1986). Later studies (Christensen, 1997) have underlined that the realisation of innovation comes through a “value proposition” to the market. If this proposition is not recognised, innovation has no economic meaning. The reason of this evolution stays with the fact that the majority of innovations are not *technology-push* but *market-pull*, meaning, finalised to answer the current or potential demand of the market. Cases, such as, IKEA, WalMart o Mc Donald's, or related to the transport sector (*low-cost* airlines companies), cannot be explained by a specific technology but through experimentation and

implementation of a formula of service (representing a complete “new” product, characterised by a novelty able to represent a value for the client). In these cases technology is often present but it is not the main “*driver*” of the innovation while organisational and commercialisation aspects have a fundamental importance. Also in the case of *last-minutes*, or *outsourcing* services, technology is for sure a usual factor but it cannot explain by itself innovation because other elements of equal importance as organisational aspects, intervene. This is the line followed by the European Commission in the “Green paper on innovation” and in its Communication (Com(2003) 112).

The European Commission (*DG Enterprise, European Competitiveness Report 2002, Chapter 3*) has stressed that scarce innovative capacity of the European companies in the services sector is one of the main reasons of the European competitiveness *gap* with the United States. Also on the problem of innovation in the services sector it is important to consider their increasing weight in the most developed Countries.

*And in its Proposal for a “Decision for the European Parliament and of the Council establishing a Competitiveness and Innovation Framework Programme (2007-2013)”, it writes “ innovation is a business process connected with exploiting market opportunities for the new products, services, business processes. Indeed, a strong competitive pressure is indispensable to provide powerful incentives for companies to continuously engage in innovation and RTD. This is closely related to the willingness to take risks and test new ideas on the market, and availability of risk capital is crucial for it. Insufficient innovation is a major cause of Europe’s disappointing growth performance. The Entrepreneurship and Innovative programme will therefore support horizontal activities to improve, encourage and promote innovation (including eco-innovation) in enterprises. This will include fostering sector-specific innovation, clusters, public-private innovation partnerships, and the application of innovation management. It will also contribute to the provision of innovation support services at regional level, in particular for trans-national knowledge and technology transfer and management of intellectual and industrial property” (page 5).*

**Composition of total national added value per sector of activity**

Country	Sector		
	<i>Agriculture</i>	<i>Industry</i>	<i>Services</i>
France	2,6	25,3	<b>72,1</b>
Germany	1,2	29,7	<b>69,1</b>
Italy	2,7	28,3	<b>69,0</b>
Japan	1,3	30,4	<b>68,3</b>
UK	1,0	27,0	<b>72,0</b>
USA	1,6	23,0	<b>75,4</b>

Source: World Bank, *World Development Indicators 2002 Data, 2001 for USA*

In practice, it appears that:

- a) Innovation in services represents an important strategical factor for the European competitiveness;
- b) innovation in services is often not only technological, but it concerns also other aspects, in particular related to organisational character and format (product innovation).

A confirmation of the attention given to non-technological innovation in services is shown by the OECD studies, after the publication of the Oslo Manual, aimed at integrate the following editions of the Manual itself. For example in *Innovation in Services*, realised for the OECD *Business and Industry Policy Forum*, different typologies of innovation in services are stressed, some of them with a real technological character and others are typically not technological.

***Some classes of service product and process innovations***

*Trade:* Formats and formulae in retailing, automated inventory

*Transport and logistics:* Containerisation, third party logistics, aircraft & system

*Financial services:* Derivatives, share funds, database management, internet banking

*Consultancy services:* Intangible asset valuation, rapid design and prototyping, environmental impact analysis

*Telecom services:* Cellular telephony systems, broad band ISDN

*Broadcasting services:* Frequency modulation, pay-per-view

*Health services:* Prophylactic medication, screening techniques

*Other services:* Surveillance systems, strategic games, pattern recognition

From the list it is clear the presence of innovation also when the principal driver is not technological (format in retail sector, financial derivatives, evaluation of intangible assets, ect.).

Hereafter you have two cases of non-technological innovation in services.

**Organisational Innovation**

In respect to the organisational innovation, the Oslo Manual, although it excludes it from the field of analysis on technological innovation, offers a definition of the same. Point 439 of the Oslo Manual indicates within the different forms of organisational innovation:

“ - *the implementation of advanced management techniques, e.g. TQM, TQS;*  
 - *the introduction of significantly changed organisational structures; and*  
 - *the implementation of new or substantially changed corporate strategic orientations.*”

The adoption, for example, of ISO 9000 or SA 8000, does not represent a technological innovation because they correspond to a substantial modification of company activities with the aim, respectively, to quality or social responsibility of enterprises.

It is evident that organisational innovation does not concern exclusively market services but all the businesses.

Among the relevant forms of organisational innovation in services, we underline the creation of SMEs networks aimed at sharing technical and administrative services, common purchases, brand policies, planning and implementation of new commercial formats (see next point on innovative format), managing activities at local level. *Business networks* between SMEs concern the commercial sector, but also the HORECA and the other activities described in question 2 .

Companies networks strength their competitive capacity but also facilitate the introduction of innovations both technological (integrated managing of purchases and logistics according to the concept of *Efficient Consumer Response*, similar to the *just-in-time* in the manufacture sector or the food traceability, taken into account by the European legislation on consumers' protection) and organisational ones (financial and administrative managing, personnel managing, *customer care*, etc.).

In the *retail sector*, the SMEs networks are called “Organised distribution” (OD) and they permit SMEs to compete with the big distribution. The Organised Distribution is present in all the Member States with some international groups. I.e. the “Spar” Group (in Italy “Despar”), which has been created in the Netherlands as an association of wholesales and retailers and today is present in 28 Countries with 17.500 retailers.

In Italy groups such as CRAI, INTERDIS, SELEX, SISA and several other minor groups at regional scale, represent one of the most dynamic forms of *retail* with a strong orientation to SMEs. It is a reality in evolution with a particular attention to technological, organisational and format innovation, aimed at competing with the big distribution companies.

The big distribution itself tends to create affiliate SMEs networks though the creation of different technical and contractual forms in order to cover all the market opportunities, offering diversified types of services to its clients.

Apart from the described commercial networks, we underline the expansion of SMEs networks aimed at managing projects. It is the case of associations aimed at managing common initiatives in urban areas (common promotion, parking, fidelity cards, administrative services, often in collaboration with local authorities).

### **Format Innovation** (or” product innovation”)

In order to understand the importance of non-technological aspects in services innovation, we have to consider, finally, the meaning of “product” in market services. In the retail sector, i.e., the commercial product corresponds to a combination of several elements which together represent the “format”, such as:

- location, surface, parking, cash registers, number of employees, opening hours, machines, number and typologies units;
- number of merceological categories, number of references, influence of perishable food, part of different goods on the turnover, food/non-food composition of the turnover, dishes ready to eat and services, packaging or mono or pluri-portions dishes, etc.;

- identification from the consumer for specific values to associate with that particular brand in order to keep specific *promises* to the client.

Innovation considers different characteristics of the *retail-mix*:

- stocking of goods (wideness and deepness), brand policy for perishable food, commercial brand policy;
- price ( *every day low price* (EDLP), promotions);
- merchandising (equipment layout, merceological layout, merceological display);
- traditional services (self scanning, home delivery, satisfied or reimbursed, etc.);
- additional services (restaurants/snacks, cafés, financial services and insurances, cultural services, payments of utilities and ticketing, etc.);
- relation with the consumer (micromarketing, fidelity cards, *one-to-one marketing*);
- communication (education, promotions, communication in the shop);
- .....

All these characteristics together determine the “**proposal of value**” for the client, that is the core element for the most recent conception of innovation.

Also the “*Frascati Manual*” (OECD’s Manual on research) considers the research of new format, a case of innovation when it says “***Launch of prototype and pilot stores***” (page 50) regarding the research activity.

Following this line, experimentation of new prototypes of format seems to respond to the Commission’s hypothesis where, on its consultation document, it tries to define an extension of the research phase by an “*experimental development stage*”.

### **Distinction between ordinary and innovative activity**

Due to the lack of an objective use of a new technology in non-technological innovation, there is an increasing risk to allow State aids to activities which are not completely “innovative”.

The problem, looking it closer, concerns also the technological innovation, because also in this case, i.e. in ICT technologies, they result to be so spread out and available to represent a “*quasi-commodity*”. In other terms, the use of digital technologies does not ensure in itself an innovative project.

So, the problem of the evaluation on the grade of innovation remains, however, on the floor. In this perspective it seems penalizing and discriminatory to deny in absolute the possibility to allow incentives to forms of non-technological innovation for the simple reason that they do not use electronics devises.

It remains, then, the problem to distinguish between ordinary activity and projects for innovative services. The problem has been discussed in several OECD and EC studies (see SI4S, *Service in innovation – innovation in services*, co-financed by the TSER programme).

From the analysis of the results it emerges the importance of an evaluative approach to innovation, based on the following aspects:

**Innovation:**

- 1) has to create an additional or radical benefit for the client (a completely new *value proposition*);
- 2) has to present a risk. If the risk is not there (meaning a certain degree of uncertainty in the investment, there is not real innovation)
- 3) has to be intentional and a consequence of decisions (a formalisation of a sequence of decisions and activities, that is, an innovation project);
- 4) has to be transmissible because it is formalised, that is, it has to be replicable to an other subject, eventually, via licences, copyrights and similar;
- 5) has to create positive externalities, that is, create added value for other subjects which eventually adopt the same innovation.

In practice, the technology is a “symptom” of the fact that the project is innovative, but it is not enough to show that it is effectively innovative.

On the contrary, a non-technological approach does not mean that the project is not innovative if the 5 mentioned circumstances are present.

**According to this reasoning, then, we ask the Commission to modify its negative prejudice on non-technological innovation, including it in between the possible forms of State aid contributions, even identifying a system of rules to minimize the risk to contribute to ordinary activities. In particular, we ask organisational innovation, networks of services enterprises and format innovation to be included as eligible forms of State aid contributions.**