

WRAP RESPONSE TO STATE AID ACTION PLAN

RESPONSE BY WRAP TO THE COMMISSION'S CONSULTATION DOCUMENT ON ITS "STATE AID ACTION PLAN, LESS AND BETTER TARGETED STATE AID: A ROAD MAP FOR STATE AID REFORM 2005 - 2009"

1 INTRODUCTION

The Waste & Resources Action Programme ("WRAP") is a not for profit company limited by guarantee by the UK's Department for the Environment, Food and Rural Affairs and the devolved Administrations of Scotland, Wales and Northern Ireland. It was established in 2001 and its objectives include the promotion of sustainable waste management. In order to achieve this objective, WRAP's work focuses on:

- § the creation of stable and efficient markets for recycled materials and products for the 100 million tonnes of waste accounted for by commercial, industrial and municipal waste;
- § specific work, including support for research and development and the creation of reprocessing facilities, in a number of material streams: aggregates, glass, organics, paper, plastics, batteries, tyres, plasterboard and wood;
- § reducing domestic waste, by working towards increasing home composting, reducing nappy waste, working with large retailers to reduce supermarket waste and creating a waste minimisation innovation research fund;
- § recycling and composting more, by setting up an advisory service to help councils make their recycling schemes more effective and providing support for the composting industry to expand to absorb the extra material collected; and
- § engaging the public by raising awareness of the need to reduce waste and recycle more, particularly by helping councils to get the most out of their collection schemes by promoting them effectively.

Some of WRAP's work involves providing support which constitutes State aid and accordingly, WRAP provides some of its funding pursuant to a scheme cleared by the Commission in November 2003¹. WRAP therefore welcomes this opportunity to comment on the Commission's proposals to reform the Community State aid regime.

2 GENERAL COMMENTS

Before commenting on specific aspects of the Road Map, WRAP would first like to make a number of more general comments:

(i) Reforms Welcome

First, WRAP strongly welcomes the proposal for reform. In particular, it welcomes the idea of focusing the Commission's efforts on distorting aid and the intention to take a more flexible approach to aid which is designed to achieve key community objectives consistent with the Lisbon strategy (particularly, in WRAP's case, aid promoting the environment and sustainability).

(ii) A Coherent State Aid Policy

Secondly, WRAP endorses the [overall comments] which the UK Government is making in response to the Road Map. In particular, WRAP believes this provides a coherent policy approach to State aid: tough on distortive aid and more flexible for non-distortive aid. In particular, Commission Regulations, Decisions, Guidelines and Practice need to recognise the huge

¹ OJ [2004] L102/59

difference between large handouts to an individual company seeking aid which clearly has the potential to distort competition and, on the other hand, financial support to encourage particular behaviour in support of national and community objectives (for example, to increases in recycling) and which the market would not otherwise deliver.

(iii) **Less and Better Targeted State Aid**

WRAP endorses the maxim of “less and better targeted State aid”. In this context, WRAP comments below on:

- * tackling market failures
- * a reduced dependency on regional aid; and
- * the use of competitive tenders.

(iv) **Market Failures**

WRAP’s raison d’être is to identify market failures which are preventing better use of scarce resources and an increase in recycling, and to identify ways in which those market failures can be remedied - where necessary providing financial support which may constitute State aid. Such support acts as a catalyst or lever to kick start the market. In this way State aid is only provided where it is necessary, where it creates an incentive effect, and where it is proportionate to the market failure identified.

In light of this, WRAP strongly welcomes the Commission’s recognition that a key element of the Road Map, and the more refined economic approach, is an analysis of market failures. WRAP’s experience, however, is that it is necessary to assess proposed funding on a case by case basis and WRAP considers that it is neither desirable, nor likely to be possible, to devise a standard formula for ascertaining market failure.

(v) **Regional Aid**

No doubt regional aid is an important part of the Commissions’ and Member States’ policy mix. However, WRAP shares the UK Government’s concern that there has been a tendency for the Commission to try to assess almost all State aid within a regional aid context. However, this is not appropriate where the aid is designed to tackle other policy objectives, such as environmental issues. For example, WRAP aims to tackle market failures in recycling by providing support in the manner which will most effectively remedy the specific problem identified, i.e. provide the greatest environmental benefit for the minimum amount of State aid. There is no reason why this solution should be found in one of the regions: indeed, a State aid policy which forces such aid to be given in the regions may result in more aid being given, relative to the result achieved.

(vi) **Competitive Tenders**

WRAP agrees that the Commission should be particularly concerned with aid measures which provide unwarranted selective advantages to some firms, preventing or delaying market forces from rewarding the most competitive firms. This risk is minimised where recipients of support are selected by means of a competitive tender (indeed, the winners of such tenders will tend to be the most competitive firms as they are generally committing to provide the environmental benefit sought for the least amount of public support). The use of competitive tenders is also consistent with the Commission’s requirement that member states make choices transparently.

(vii) **Equality between Public and Private Solutions**

WRAP supports the view expressed by the UK that payments to companies to deliver services must be assessed for State aid purposes in exactly the same way as payments to state bodies to

perform the same services. Indeed, a number of the activities which WRAP seeks to promote in the private sector would, in the normal course of things, be carried out by the State in many member states (for example, collection of waste for reprocessing). As the Commission rightly notes *“Member States enjoy a wide margin of discretion when deciding whether, and in what way to finance the provision of services of general economic interest”*.

Even leaving aside the legal difficulties of discriminating between the public and private provision of such services, such discrimination does not make sense from a policy prospective. If member states cannot provide support for key policy objectives (such as promoting sustainability, increasing recycling and reducing landfill), then either important policy objectives will not be achieved or a much greater burden will fall on scarce public resources.

(viii) **Environmental Protection**

WRAP welcomes the Commission’s recognition that environmental protection is in itself essential and its intention to reform the community guidelines on State aid for environmental protection. WRAP will comment on these separately.

(ix) **Internal Commission Practices**

WRAP welcomes the Commission’s proposal to improve its internal practice and administration. This is particularly important in the context of making a clear distinction between aid which is very likely to be distortive of competition (such as a large grant to an individual company requesting aid) and, on the other hand, support offered by a Member State through a competitive tender to help it meet specific community and Member State policy objectives. The latter should be approached positively by Commission staff whilst, of course, ensuring that the relevant State aid rules are respected. As part of its assessment of the likely effect of proposed State aid on competition, the Commission should of course systematically apply the principle of proportionality. Accordingly, WRAP considers that, as a general rule, the Commission ought to view favourably aid schemes providing for a number of small aid grants.

(x) **Use of Independent Bodies**

In principle, WRAP welcomes the Commission’s willingness to consider ways in which the task of the Commission, in terms of State aid enforcement, could be facilitated. In this context, WRAP would propose that the Commission should support the use of third party auditors by aid providers to ensure that no more aid is granted than is strictly necessary. Such third parties (e.g. independent technical experts or firms of accountants) could ensure that aid is only provided in respect of eligible costs, that these eligible costs are correctly valued, and that the aid is only provided once the relevant objectives or milestones have been achieved. WRAP does not, however, consider that the use of such third parties should become compulsory. Rather, WRAP would suggest that if a project or scheme notified to it contained provision for such third party audits, the Commission should feel more comfortable approving support for projects aligned with both State and Community objectives (and be less concerned itself with the minutiae of the precise costs being supported).

In addition to the above general comments, WRAP sets out below some comments on specific aspects of the Road Map.

3 STATE AID RESEARCH AND DEVELOPMENT

As an administrator, in general, WRAP finds that ensuring it complies with Community State aid rules can be disproportionately burdensome and time consuming in relation to the level of funding that it wishes to contribute to a particular project.

This burden is particularly evident when WRAP is looking to provide funding for research and development (“R&D”) projects. WRAP supports the Commission’s view that *“Europe’s future economic development depends on its ability to create and grow high value, innovative and research-based sectors capable of competing with the best in the world.”*² In order to assist in attaining this target of creating a competitive, high value, research-based economy in Europe, the State aid rules relating to research and development need to be clarified and, crucially, greater certainty is required than exists at present as to when funding for research and development will not constitute State aid or need not be notified to the Commission.

To date, WRAP has provided funding for many research and development projects in accordance with paragraph 2.5 of the Community’s Framework for State aid for research and development (the “Framework”). WRAP commissions R&D from firms which it chooses on the basis of bids received following an open tender procedure. WRAP is confident that the funding that it awards in this way does not amount to State aid. All companies have the opportunity to compete for funding and the results of the research are widely disseminated by WRAP, ensuring that the firm that carried out the research and development does not obtain a competitive advantage. However, the use of the Framework unnecessarily imposes an excessive administrative burden on WRAP for the following reasons:

- (a) the Framework, in particular paragraph 2.5, provides no certainty that by following certain guidelines, State aid is not present. Instead, the Framework provides vague guidance that, in certain circumstances, State aid will normally be assumed not to exist;
- (b) many firms that participate in WRAP-funded R&D projects are reluctant or unwilling to assign to WRAP pre-existing intellectual property rights (“IPR”) that may be used in the projects. Much time is consequently spent by WRAP negotiating contracts with potential project partners to try and arrive at a position where WRAP is satisfied that it is not granting State aid and the enterprise is satisfied either that it will receive fair consideration for its IPR or that its IPR is properly protected;
- (c) as a result of (a) and (b) above, WRAP’s experience is that each R&D project raises its own legal and factual questions, meaning that WRAP spends time and expense obtaining legal advice in order to gain comfort that it is not likely to be granting unlawful State aid.

In light of WRAP’s experience, WRAP welcomes the Commission’s recognition that the Framework *“should provide for adequate provisions for collaborative research including the ownership of, access to and exploitation of intellectual property rights obtained in such projects”*. Given the undoubted Community-wide environmental interest in developing and promoting waste minimisation initiatives, including developing applications for reprocessed waste, WRAP would like to see greater flexibility introduced into its ability to fund R&D projects in this area.

In addition to procuring specific projects or acquiring the results of R&D carried out by enterprises, WRAP wishes to be able to fund R&D carried out by enterprises whereby the funding recipient is able to retain ownership of the resulting IPR, rather than passing it to the Member State body. For example, a small, medium-sized or large enterprise may have an idea for some R&D, which, if successful in subsequent trials, would benefit the Community. It is often the case, however, that such ideas are so low on the priority list of companies that they never see the light of day. If WRAP were able to contribute funding for such R&D and the industrial participant were permitted to retain ownership of resulting IPR, with WRAP disseminating the results of the project, then this is likely to encourage more firms to undertake R&D projects. (However, if the industrial participant did not exploit the IPR after a specified period, WRAP would acquire the right to exploit them itself). Indeed, WRAP considers that a more flexible State aid regime relating to R&D could foster a much needed upsurge in R&D activity across the Community, consistent with the Lisbon strategy.

² Paragraph 24 of the Commission’s consultation document.

An alternative example of flexibility, and one that would resolve the unwillingness of some project partners to assign their pre-existing IPR, would be if the Commission could indicate in the Framework the circumstances in which aid recipients could obtain ownership of any IPR generated by the R&D without this constituting aid. One way of dealing with this would be to acknowledge that one form of consideration for recipients owning such rights would be the granting by the recipient to the aid provider of certain rights to pre-existing IPR. For example, in return for the licence of pre-existing IPR, the project partner could have the exclusive right to exploit the results of the project for a limited period (for example, for three years). The Member State would be free to disseminate the results of the project immediately, but initially in a way that did not conflict with the project partner's exclusive rights. However, at the end of the term of the exclusive licence, the Member State would be free to license the IPR to anyone it wished - probably on a royalty-free basis. This would have a number of significant advantages. First it would enable some valuable projects to go ahead which would otherwise not happen (because potential partners would not participate without some initial exclusivity). Secondly, the Member State would be able to disseminate the maximum valuable information resulting from the R&D as soon as possible. Thirdly, all interested parties would be able to exploit the results (generally on a royalty-free basis) after the initial period (and without a licence to the underlying pre-existing R&D, the IPR resulting from the R&D is often useless in practical terms). It is possible that both this approach and the one proposed in the preceding paragraph could both be made available to Member States, which could use the most appropriate one in each particular case.

WRAP also welcomes the Commission's indication that if it *"can establish clear and general compatibility criteria on the basis of experience, it will exempt certain aid measures from the obligation to notify to the Commission"*. WRAP welcomed the introduction of R&D projects into the block exemption for aid to small and medium sized enterprises, but would like to see such exemption criteria expanded, both in the way that funding is granted and to extend the exemption to large enterprises. An example of the sort of R&D project that WRAP would like to be able to fund without incurring significant administrative or legal costs due to uncertainty due to its compatibility with Community State aid rules is as follows.

WRAP may wish to advertise for bids from organisations to undertake R&D into developing a new use for a particular reprocessed material. WRAP would receive bids from a wide range of organisations, including SMEs, large enterprises and not for profit organisations, some of which may be affiliated to further education establishments. WRAP's technical experts would assess each bid and enter discussions with those bidders whose projects appear to offer the best value for money and whose projects appear both capable of being realised and would result in the greatest environmental benefit. WRAP would be willing to fund such projects up to certain levels of eligible costs, depending on whether the proposed R&D is fundamental research, industrial research or pre-competitive development. Eligible costs could be defined as they are currently in the SME block exemption (Regulation 70/2001, as amended). WRAP would insist on being free to disseminate widely across the Community the results of the R&D, but to do so in such a way as not to reveal details of the project partner's IPR resulting from the project. This IPR would remain with the project partner, who would commit to license it on a non-discriminatory basis. Competitors of the project partner would benefit from the results of the R&D and knowledge that the R&D was successful and may license technology from the project partner or may then undertake their own R&D. The initial tender process and dissemination of results minimises, or even removes, the risk that the project partner will receive a specific benefit and/or that competition will or may be distorted.

WRAP would welcome clear and unambiguous guidelines from the Commission that such projects would not involve State aid. This would enable WRAP to carry out the sort of project outlined above, which it considers would not appreciably distort competition. WRAP recognises, however, that its objectives (i.e. environmental) are aimed at improving the lives of all in the Community and that therefore R&D projects linked to environmental benefits may merit their own guidelines or block exemption and may be worthy of different treatment from more general R&D projects. In this regard, WRAP would welcome the introduction either of a stand alone block exemption for State aid for environmental objectives or the incorporation of environmental objectives into a consolidated, general block exemption, either of which should include scope

to award funding for R&D to all types of organisations (whether SMEs, large enterprises, or not for profit organisations).

WRAP would welcome a small but significant amendment to the types of activity to which funding for R&D can be provided in order to ensure that market failures are genuinely addressed. One way of doing this may be to amend the definition of “pre-competitive development” used in the current SME block exemption and the Commission’s Framework. In this regard, WRAP would propose deleting the words “which could not be used commercially” from the first sentence of the definition and similarly, WRAP would propose deleting the words “provided that such products cannot be converted or used for industrial applications or commercial exploitation” from the second sentence of the definition. Such an amendment would not alter the thrust of the definitions insofar as one would still only be referring to a “initial prototype” in the first sentence and a “conceptual formulation” in the second. Crucially, however, it would enable the players in a particular industry to see tangible results that convince them of the possibility of commercialising a particular product or process. This would significantly increase the prospect of the identified market failure being remedied.

In addition to these proposals, or as an alternative to them, WRAP would propose amending the wording found at article 5a(2) of the SME Block Exemption (and any equivalents). This article states that the aided project must fall completely within the aforementioned stages of R&D. This has the effect that, if 90% of the project fell within these stages but a small element fell outside them, then no aid could be granted at all. WRAP considers that the Commission should amend this requirement by stating that the aided project must fall predominantly within the aforementioned stages. Those parts of the project which fell within these stages could then be supported (subject to limits on aid intensity) and those elements falling outside the stages could not be supported.

4 DE MINIMIS BLOCK EXEMPTION

WRAP welcomes the Commission’s proposal to increase the threshold for de minimis aid. WRAP proposes that, in addition to increasing the threshold in block exemption Regulation 69/2001, the Commission should consider introducing a higher de minimis threshold relating to aid given for certain Community objectives, such as environmental aims. This element of de minimis funding could be introduced either into an amended Regulation 69/2001 or into the proposed general block exemption or individual block exemptions.

5 ENVIRONMENTAL PROTECTION

In view of the work WRAP does and its underlying focus on environmental protection, WRAP welcomes the Commission’s tentative proposal for introducing a block exemption for aid for environmental protection. WRAP notes that the Commission has the power to introduce such a block exemption, pursuant to Regulation 994/98³ and believes that it may be possible to draft sufficiently precise parameters for such a block exemption. Clearly, a principal advantage of introducing a block exemption will be that it should lead to a considerable reduction in the administrative burden placed on the Commission, Member State and aid providers. Equally, the certainty that it will provide should reduce the risks that projects that have the potential to offer considerable benefits in the field of environmental protection for the entire Community are not funded.

WRAP considers that the Commission could balance the clear interests in providing certainty via a block exemption for aid for environmental protection against the risks of such aid distorting competition, by introducing caps on the amount of aid that may be granted in any given project (similar to the guidelines on State aid and risk capital, although at a higher level). For example, a block exemption could enable Member States to grant a certain percentage of eligible costs for a given project (such costs being confined strictly to the investment costs necessary to meet the environmental objectives and thereby based on the current

³ Article 1(1) (a) (iii) of Council Regulation (EC) No 994/98 of 7 May 1998 on the application of Articles 92 and 93 of Treaty establishing the European Community to certain categories of horizontal State aid.

guidelines on State aid for environmental protection) up to a certain cap in aid grant. Unlike the current risk capital guidelines, however, WRAP does not consider that it is appropriate to provide for an uplift on the cap depending on the location of the recipient (nor its size). Rather, costs should be restricted to what is necessary in order to achieve the relevant environmental benefit.

The introduction of a cap on the amount of aid that may be granted pursuant to the block exemption should ensure that smaller projects that are least likely to raise issues of competition distortion need not be examined by the Commission, whilst ensuring that larger projects, even if they relate to environmental protection goals, fall for a prior examination by the Commission. In practical terms, this may mean that comparatively small scale funding into, for example, promoting energy efficiency or assisting a company to develop recyclable packaging can be funded in line with the block exemption, whilst aid for the construction of a €20 million recycling plant will fall for prior examination for the Commission. WRAP would be happy to explore its ideas for a block exemption for environmental protection with the Commission in more detail if the Commission considers that such a block exemption is workable.

6 RISK CAPITAL

WRAP welcomes the Commission's statement that it will *"focus on the need to further increase the flexibility of the rules to take into account diversity, especially as regards the level of the safe-harbour investment tranches for which the so-called "equity gap" is presumed to exist"*. Investment in SMEs seeking to operate in the reprocessing and waste minimisation industries continues to be very difficult to obtain and this sector suffers from significant market failures.

Where market failures can be demonstrated to the Commission, WRAP would hope that the Commission would be flexible about the minimum contribution of private capital investment in a new fund and would expect that the Commission could speed up its review of risk capital aid notifications where it is shown that funds' managers and investors are chosen following an open tender procedure, funds are commercially managed and investments are aimed at SMEs.

WRAP's experience through its pilot fund is that the caps on aid provided to an enterprise through risk capital measures as set out in paragraph VI.5 of the State aid and risk capital guidelines⁴, of €500,000, €750,000 and €1 million respectively, depending on where the recipient is located, are too low. In WRAP's experience, they are sufficient for an initial investment in an SME, but the extent of market failure is so great in the environmental sector that whilst an initial investment up to these ceilings may enable an SME to start making a success of its nascent business, often a further injection of investment is required in order to enable the business to consolidate that initial success. Accordingly, WRAP would like to see these ceilings raised so that, in certain circumstances, promising start-up SMEs are not allowed to fail soon after being established due to a want of investment.

7 PRACTICES AND PROCEDURES

WRAP's experience of the State aid notification procedure has sometimes been a frustrating one. This is predominantly because the Commission often takes too long in carrying out its assessments. Accordingly, WRAP welcomes the Commission's proposal that it will try to instil more predictable timelines and ensure higher transparency in the notification procedure.

WRAP agrees with the Commission that delays ought to be reduced by encouraging higher quality notifications and discouraging incomplete notifications. The Commission may wish to follow the notification process used for merger notifications to the Commission, whereby Member States would be encouraged to submit a draft notification to the relevant case team at the Commission who could then indicate whether they considered further information should be provided. Alternatively, so as to reduce the burden on the

⁴ OJ [2001] C235/3

Commission's time and resources and to increase the incentive on Member States to submit complete notifications, if the Commission receives incomplete notifications, then it should reject the notification. This would assist in enabling the Commission to stick to a tight deadline in which to review State aid notifications and ought to encourage Member States to provide higher quality notifications.

Finally, WRAP appreciates the Commission's acceptance of a briefing/memorandum often in advance of a notification and often followed by a meeting with those most closely involved (both within Member States and other stakeholders). This should ensure that the Commission's consideration of the aid focuses on the real issues and should simplify the formal notification process. However, it is important that the Commission does not take too formulaic an approach to the notification itself if the key issues have been identified and addressed in the briefing paper.

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