State Aid Modernisation Initiative: Revision of the State Aid for Research, Development and Innovation Framework

Background Information

Objective of the consultation

“The Community Framework for state aid for research and development and innovation ("the R&D&I Framework") sets out the conditions Member States should respect when granting aid to industry for R&D&I-activities. It entered into force on 1.1.2007 and expires by end 2013. The purpose of the present consultation is to collect views on the first draft text of the revised Framework.”

Reference Documents

* Community Framework for State aid for Research and Development and Innovation, OJEU 2006/C 323/01
* EC Communication COM(2012)209 on EU State Aid Modernisation (SAM)
* Issues Paper on the Revision of the State aid Rules for Research and Development and Innovation
* Draft General Block Exemption Regulation (GBER)
* Draft General Block Exemption Regulation II (GBER II)
* Explanatory Memorandum on additional categories of exemptible aid

Memo

Article 107(1) TFEU (ex Article 87 TEC): “Save as otherwise provided in the Treaties, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market”.

Article 107(3)(b) TFEU: “The following may be considered to be compatible with the internal market: [...] (b) aid to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State”

Article 107(3)(c) TFEU: “The following may be considered to be compatible with the internal market: [...] (c) aid to facilitate the development of certain economic activities or of certain economic areas where such aid does not adversely affect trading conditions to an extent contrary to the common interest”
The purpose of this document is for ASD to present, on behalf of the European Aerospace, Security and Defence industries it represents, a common position in relation to the on-going reform of the EU State Aid for Research and Development and Innovation, by identifying a limited number of major related issues.

**Rules applicable to aid for Research, Development and Innovation (RDI) are of key importance, as they can directly and significantly foster or hamper the EU’s ability to increase its overall Research & Development (R&D) effort in order to remain competitive on the worldwide market.** Non-EU companies do not have to obtain any competition law clearance before receiving domestic State support. A sub-optimal EU control can thereby result in creating an unfair playing field for EU companies.

In order to allow EU companies to effectively compete and remain competitively strong, we call for the following comments to be taken into account with respect to the proposed RDI State aid Framework and General Block Exemption Regulation (GBER), in their currently available versions. These comments are fully in line with the fact that European Commission pushes the EU State aid modernization initiative as an efficient means to effectively contribute to the EU2020 strategy and to the overall effort of simplification of legislation.

As a general principle, the **Commission should avoid changing the rules** which are currently applicable. It took significant time and effort for companies and States to understand their characteristics. **Emphasis should be placed on predictability, legal certainty and simplification.**

**Comments on swifter notification and clearance process**

The **EU clearance process of RDI aid must be significantly accelerated**, as per the joint declaration of the Commission and the Council of 30 May 2013. Currently, the clearance process of notified aid lasts over 9 to 10 months on average. **Focusing, as of the pre-notification contacts, on the assessment of the proposed measure’s impact on competition**, in close cooperation with other EU Commission Directorates with experience in the activities and markets concerned, would enable the Commission and Member States to accelerate the clearance of cases raising manageable competition concerns.

The Commission should therefore **initiate the process of improvement of the Code of Best Practice as well as seek, together with Member States, to apply more systematically the Mutually Agreed Process.** Avoiding undue extra complexity of analysis and focusing from the outset of the assessment on the impact on competition of the measures will undoubtedly contribute to reducing the process duration.

**Comments on Increase exemption thresholds (GBER)**

A **further increase in the exemption thresholds**, notably concerning downstream research and **Key Enabling Technologies** projects would greatly simplify the process and accelerate time-to-market. Further increases would strongly contribute to the simplification effort:

- From €40 to 50 million for fundamental research
- From €20 to 25 million for industrial research
• From €15 to 20 million for experimental development. It is essential to favour downstream research, as acknowledged by the Commission
• Thresholds should be tripled with respect to projects relating to Key Enabling Technologies.

Comments on the exclusion from the exemption of aid schemes (GBER)
Aid schemes annually exceeding 0.01% of the annual GDP or €100 million would be excluded from the benefit of exemption.

This proposal should be clarified, notably as regards the purpose of evaluation which is considered. In any event, excluding aid schemes from the benefit exemption, and therefore requiring a filing, in order to perform such evaluation would appear disproportionate. Alternative possibilities could be found to allow the Commission to get additional visibility on such aid schemes without creating cumbersome processes. Again, simplification and acceleration of procedures will be key to the reduction of the cost of regulation and of EU’s firms time-to-market.

We also note that the proposed criterion (% of GDP) could reveal discriminatory, as it will mechanically concern small Member States with a strong industrial specialization.

Comments on Innovation aid to large enterprises (GBER)
Innovation aid would only appear to be exempted for SMEs, and there only up to €5 million. A possibility for large companies to benefit from a similar exemption should be introduced in order to avoid that all innovation aid, even for limited amounts, require a burdensome notification.

Comments on incentive effects
The Commission considers among the additional conditions for individual aid a counterfactual scenario consisting also in an alternative project carried out outside the Union.
This is welcome as it implies the recognition that some economic sectors have a global dimension, also with competition between EU and extra-EU. In this respect any reference to incentives should take into account the global market.

Comments on the manifest negative effects
On this topic, the focus is on discriminatory national measures violating the Union law.
It seems necessary to clarify that the above does not exclude measures restricting the possibility for those beneficiaries not executing R&D and production activities within EU, in order to avoid any extra-EU utilization of the results of research, which can lead to distorting competition at the disadvantage of EU.

Comments on Net extra Cost
With respect to proportionality, the Commission proposes to introduce a new cap to the aid, in addition to the limits which already exists on intensities. The new cap would amount to the difference between the net present value (NPV) of the aided project and the counterfactual
project, taking into account the probabilities of the two business scenarios (hereafter the NPV comparison method).

The proposed introduction of the NPV comparison method raises a number of serious concerns. First, introducing an NPV comparison method would not be adapted to RDI aid. It would contradict the key objectives of the Commission’s simplification initiative as well as business needs. Indeed, the basic features of RDI projects show that applying an NPV comparison method would trigger significant complexity, legal uncertainty, delays and potential reduction of aid amounts.

The net extra cost calculated as a difference in NPVs would constitute an additional (and newly introduced) cap to the aid amount. Given the complexities and uncertainties in the calculation method proposed by the Commission, there is a serious risk that applying such additional cap could result in legal uncertainty and a reduction of the allowed funding. This could impact EU firms’ ability to innovate and remain competitive vis-à-vis their non-EU competitors (in addition to the fact that the suspensory clearance requirement already constitutes a hurdle for EU companies).

Secondly, applying an NPV comparison method to RDI projects would deviate from the positions taken by the Commission in other types of aid.

Positions already taken by the Commission are consistent in showing that for RDI aid (i.e. for investment aid aimed at an efficiency objective), net extra costs should be calculated by comparing the internal rate of return of the aided scenario to the minimum profitability that would be required for the given project (“hurdle rate”) [hereafter the Project Profitability Method] rather than by applying an NPV comparison method.

The Commission’s 2009 Communication on “Common principles for an economic assessment of the compatibility of State aid under article 87.3”, supports the assessment of net extra costs in a different manner with respect to aid with an efficiency objective and aid with an equity objective. In this Communication, RDI projects are aimed at an efficiency objective.

In its recent “Guidelines on regional State aid for 2014-2020” (July 2013), the Commission applies a consistent approach: it distinguishes investment decisions from location decisions, and defines different net extra cost calculation method for these two types of decisions. If for relocation decisions, the Commission opts for the difference in net present values, it precisely chooses to exclude such method with respect to investment decisions and to calculate, in this respect, net extra costs based on a Project profitability method. It is clear that RDI aid falls within the category of investment aid.

These elements show that, in line with the Commission’s past practice, the next extra cost for RDI projects should be calculated based upon a Project profitability method. It should be stressed, in this respect, that such method should not be applied in a “one-size-fits all” way. In particular, the specificities of RDI projects such as the specific levels of complexity and risk (technological and commercial) of given projects as they affect a given undertaking, should be taken into account.
Since the Commission already applies a comparable method in practice to RDI projects; the current practice should not be fundamentally modified. This would have the advantage of maintaining predictability and legal certainty, and avoiding extra complexity. Again, it is important to recall that our non-EU competitors would not be subject to such analysis when obtaining their domestic RDI support.

Comments on repayable advances (RDI Framework)
The Commission stresses that “insofar as the identified need for aid relates mainly to difficulties in attracting debt finance from the market, rather than a lack of profitability, a particularly apt way to ensure that the aid is kept to the minimum may be to provide the aid in the form of a loan, guarantee or repayable advance instead of a non-repayable form, such as a grant”. This shows that there would not be a need to perform an additional test to verify that such aid is kept proportionate. As a consequence, no Net Extra Cost approach should be applied to repayable advances.

Even if applying a net extra cost approach for repayable advance was considered, this should not be based on the NPV comparison method, but rather on the project profitability method, for reasons expressed above.

In any event, it would be necessary to ensure that the applicable intensities would not be reduced compared to the currently applicable framework.

With respect to the Commission’s draft Methodological Guidance paper on the (ex post) evaluation in the field of State aid, we note that cases related to aerospace, security and defence are generally of significant size with a limited number of intra EU competitors, most of the competition being based outside. It is therefore at best difficult to identify pertinent counterfactual scenarios. We understand that the framework is not specific to aerospace, security and defence but specific cases should be also taken into account in a horizontal policy measure.

Comments on the important projects of common European interest (RDI Framework)
This notion should be defined in a less restrictive manner and used as a tool to incentivise State to contribute to EU industrial policy. Indeed, the concept of “important projects of common European interest” can play a key role in incentivising Member States to support projects which contribute strongly to the EU industrial and innovation policy and thereby promote jobs in high technology industries.

In its Issues Paper, the Commission proposed that such projects could, subject to a precise economic analysis, benefit from an arguably more favourable treatment: project could receive funding up to where an appropriate return on investment ratio would be reached for the project (“funding gap”).

The draft framework indicates the precise definition of important projects of common European interest and modalities for their compatibility assessment will be subject to a separate communication, for which the public consultation will be launched shortly.
The **criteria** that projects should fulfill to qualify as important projects of common European interest **must be widened**, in order to increase the number of eligible projects (currently, projects virtually never qualify). For instance:

- Measures which contribute to achieving EU2020 or Innovation 2020 objectives should qualify;
- The criteria should be based upon the fact that positive effects are perceived on several countries in the EU, regardless of whether RDI aid is granted by several States;
- Projects where EU funds are provided on the side of national funds should also qualify as this would constitute a strong incentive to combine EU and national financing.

In addition, such projects should be granted a more predictable and specified favourable treatment: exemption from notification, application of a funding gap approach or at least higher intensities allowed, simplified procedure, reduced delays etc. It should be ensured that applying a more refined economic analysis still allow quicker clearance delays.

**Comments on the definition of RDI project (RDI Framework)**

A definition of R&D project is introduced. A definition is suitable to the extent that it sets out the elements that allow characterizing a project.

The **newly introduced definition of R&D projects should be amended**: whether or not projects should be assessed together or separately under the State aid rules should be determined based on a sufficiently wide and pragmatic span of concordant evidence, and not primarily by focusing on whether they do or do not have independent probabilities of technological success. Indeed, focusing the analysis on the comparison of likelihood of technological success reduces the assessment to a single parameter, which is not accurate. It would be much more relevant either to **remove the above underlined wording** altogether, which would allow the Commission to keep flexibility and adaptability, or to base the analysis on a **wider span of concordant items of evidence**, which would allow catching accurately the specificities of the various projects.

**Matching Clause**

The wording of the proposed matching clause should not be less favourable than the wording originally contained in the 2006 RDI Framework. We therefore propose that the following amendments are made to the clause provided for at para. 92 of the draft RDI framework in order to maintain the wording of the current RDI framework:

"In order to address actual or potential direct or indirect distortions of international trade, and under the condition that aid is kept to the minimum necessary, higher intensities than generally permissible under this framework may be authorised if, directly or indirectly, competitors located outside the Union have received in the last three years or are going to receive aid of an equivalent intensity for similar projects. However, where distortions of international trade are likely to occur after more than three years, given the particular nature of the sector in question, the reference period may be extended accordingly. Where possible, the Member State concerned will provide the Commission with sufficient information to enable it to assess the situation, in particular the need to take account of the competitive advantage enjoyed by a third country competitor. Where the Commission does not have"
evidence concerning the granted or proposed aid, it may also base its decision on circumstantial evidence, as acquired for instance through the use of its investigative powers.

Indeed, not making such amendments would unduly create a de facto new cap to the aid and limit the States’ and beneficiaries ability to benefit from the matching clause.

Transparency

Systematic transparency measures (such as publication of granular information on the internet) could endanger the position of EU companies by allowing non-EU companies to attack more easily while the opposite is not possible, as no State aid regimes apply outside the EU.

As a final point, we would reiterate that beneficiaries should be given an opportunity to attend, together with Member States, discussions with the Commission. This would help accelerate the process by allowing industry to explain directly the project and the market characteristics from a business standpoint.

From a wider perspective, we would welcome explanations from the Commission concerning the inclusion of State aids in the context of the Transatlantic Trade Investment Partnership. Increased reciprocity from the US, at least on transparency of State support, would be a positive development to the extent it would be as complete and exhaustive as what the EU players and States have to disclose publicly. This could also be sought with other countries with whom the EU is engaged in free trade negotiations.

In conclusion, the proposed reform should accelerate the EU control of RDI aid, simplify its application (applicable tests, focus on cases which effectively raise competition concerns) and preserve a level playing field between the European industry and its competitors. RDI State aid rules should finally be used to incentivize States to invest in projects which contribute to the EU industrial and competitiveness policies.