Class: 430-01/2013-03/005

Date: 23 December 2013

Case: Ministry of Science, Education and Sports: Decision on the objectives, criteria and procedures in granting of State aid for research, development and innovation

State aid

Opinion

- summary

The Ministry of Science, Education and Sports asked the opinion of the Croatian Competition Agency (CCA) relating to the question whether public research organizations may freely provide consultancy services on the market, and whether by charging lower prices for their services they infringe competition rules. Given that public research organizations are partly financed from the State Budget and enter into business arrangements with other public administration authorities who are also financed from the State Budget, the ministry also sought explanation as to the compliance of this conduct with State aid rules.

The opinion of the CCA was based exclusively on the compliance of the above practices with competition rules, notwithstanding the issue of public interest and strategic goals stated by the ministry in its Strategy Plan for 2014 – 2016.

In its opinion the CCA pointed out the importance of the definition of undertaking, which is under the well-established competition case law an entity which engages in an economic activity, irrespective of its legal status and the way it is financed. Under the Competition Act undertakings are companies, sole traders, tradesmen and craftsmen and other legal and natural persons who are engaged in a production and/or trade in goods and/or provision of services and thereby participate in economic activity but also state authorities and local and regional self-government units where they directly or indirectly participate in the market and all other natural or legal persons, such as associations, sports associations, institutions, organisations, copyright and related rights holders and similar who are active in the market. Competition rules also apply to undertakings which are entrusted pursuant to separate laws with the operation of services of general economic interest, or, which are by special or exclusive rights granted to them allowed to undertake certain economic activities, insofar as the application of competition rules would not obstruct the performance of the particular tasks assigned to them by separate rules or measures and for the performance of which they have been established.

The status of research organizations is not only regulated by the Croatian laws defining the criteria for their establishment and their primary activity but also by the EU State aid rules, in this particular case the EU Framework for State aid for research and development and innovation in force.

The 'research organisation' means an entity (such as universities or research institutes, technology transfer agencies, innovation intermediaries, research-oriented physical or virtual collaborative entities), irrespective of its legal status (organised under public or

private law) or way of financing, whose primary goal is to independently conduct fundamental research, industrial research or experimental development or to widely disseminate the results of such activities by way of teaching, publication or knowledge transfer.

Consequently, where the same research organisation carries out activities of both economic and non-economic nature, the public funding of the non-economic activities will not fall under Article 107(1) of the Treaty if the two kinds of activities and their costs, funding and revenues can be clearly separated so that cross-subsidisation of the economic activity is effectively avoided. Evidence of due allocation of costs, funding and revenues can consist of annual financial statements of the relevant entity.

Generally, the following activities are considered as non-economic activities: first, the primary activities such as education for more and better skilled human resources, independent R&D for more knowledge and better understanding, including collaborative R&D where the research organisation or research infrastructure engages in effective collaboration, wide dissemination of research results on a non-exclusive and non-discriminatory basis, for example through teaching, open-access databases, open publications or open software, and second, knowledge transfer activities, where they are conducted either by the research organisation or research infrastructure with, or on behalf of other such entities, and where all profits from those activities are reinvested in the primary activities of the research organisation or research infrastructure.

On the other hand, where a research organisation or research infrastructure is used for both economic and non-economic activities, public funding falls under State aid rules only insofar as it covers costs linked to the economic activities. Where the research organisation or research infrastructure is used almost exclusively for a non-economic activity, its funding may fall outside State aid rules in its entirety, provided that the economic use remains purely ancillary, that is to say corresponds to an activity which is directly related to and necessary for the operation of the research organisation or research infrastructure or intrinsically linked to its main non-economic use, and which is limited in scope.

However, where research organisations or research infrastructures are used to perform economic activities, such as renting out equipment or laboratories to undertakings, supplying services to undertakings or performing contract research, public funding of those economic activities will generally be considered State aid. These secondary activities which are considered economic or market activities are subject to application of competition and State aid rules on the account of the fact that in this part of its activities the research organisation is considered an undertaking.

Here it must be noted that not all forms of public financing or other financing constitute State aid. Even if the financing may be considered State aid under the existing State aid rules, it may be exempted from the general State aid ban under Article 107 (1) of the Treaty. For example, the Commission will not consider the research organisation or research infrastructure to be a beneficiary of State aid if it acts as a mere intermediary for passing on to the final recipients the totality of the public funding and any advantage acquired through such funding. Where a research organisation or research infrastructure is used to perform contract research or provide a research service to an undertaking, which typically specifies the terms and conditions of the contract, owns the results of

the research activities and carries the risk of failure, no State aid will usually be passed to the undertaking if the research organisation or research infrastructure receive payment of an adequate remuneration for its services particularly where the research organisation or research infrastructure provides its research service or contract research at market price or where there is no market price, the research organisation or research infrastructure provides its research service or contract research at a price which reflects the full costs of the service and generally includes a margin established by reference to those commonly applied by undertakings active in the sector of the service concerned.

The question of whether and under which conditions undertakings obtain an advantage within the meaning of Article 107(1) of the Treaty in cases of contract research or research services provided by a research organisation or research infrastructure, as well as in cases of collaboration with a research organisation or research infrastructure must be answered in accordance with general State aid principles. To this purpose, it may in particular be necessary to assess whether the behaviour of the research organisation or research infrastructure can be imputed to the State.

If a project is carried out through collaboration between undertakings and research organisations, no indirect State aid is awarded to the participating undertakings through those entities due to favourable conditions of the collaboration if one of the following conditions is fulfilled: the participating undertakings bear the full cost of the project, or the results of the collaboration which do not give rise to IPR may be widely disseminated and any IPR resulting from the activities of research organisations are fully allocated to those entities, or any IPR resulting from the project, as well as related access rights are allocated to the different collaboration partners in a manner which adequately reflects their work packages, contributions and respective interests, or the research organisations receive compensation equivalent to the market price for the IPR which result from their activities and are assigned to the participating undertakings, or to which participating undertakings are allocated access rights.

In order to avoid possible spillovers from public financing into market activities, which may consequently lead to price reduction for the services concerned on the market that are below the competitive price , it is necessary to introduce separate accounting for economic and non-economic activities, their costs and financing in order to demonstrate that no undue cross-subsidation would occur. In that context, in line with the European Commission case law, annual financial statements or other proper evidence of cost allocation, such as compulsory declarations by the beneficiaries revised by independent audits or full costing defined as the ability to identify and calculate all direct and indirect costs per activity and/or project that need to be considered in carrying out these activities. In other words, where research organisations carry out activities that are not a part of their primary non-economic activities, and compete in this part of their activities on the market with other undertakings whose goal is to make profit, they must fulfil the above cost separation criteria.

In reply to the other question of the ministry, the CCA stated that the activities carried out by public authorities inartistically form part of the prerogatives of official authority and when performed by the State they do not constitute economic activities. The same applies to State administration authorities and regional and local administrative units. Where these enter into agreements with research organisations they do so pursuing its primary, non-commercial goals, on the basis of objective and transparent criteria.

However, it is likely that research organisations that are funded from the public resources for the provision of their services will offer a lower price from the market price offered by undertakings in the market that are not publically financed. Therefore, where selecting the service provider with the lowest cost for the community, it is necessary to select the most economically advantageous offer in an open competitive tender procedure.

In order to avoid any distortion of competition, research organisations that are financed from the public resources and at the same time pursue economic activities in the market, should by means of separation of economic from non-economic activities and prevention of cross-subsidation ensure compliance with competition rules so as to prevent economic advantage and favourable position on the market in the form of State aid for the activities which cannot be considered primary and non-economic activities.