# COMMISSION DECISION

**of 6 May 1998**

**concerning the extension of eligibility for regional aid for the acquisition costs of intangible property for large firms provided for in the 25th outline plan for the joint Federal Government/*Länder* programme for improving regional economic structures**

*(notified under document number C(1998) 1942)*

**(Only the German text is authentic)**

**(Text with EEA relevance)**

(98/667/EC)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community, and in particular the first paragraph of Article 93(2) thereof,

Having regard to the Agreement on the European Economic Area, and in particular Article 62(1)(a) thereof,

Having given notice to the other Member States and the parties concerned to submit their comments, in accordance with Article 93(2) of the Treaty establishing the European Community,

Whereas:

I

By letter dated 25 March 1996, Germany, acting pursuant to Article 92(3) of the EC Treaty notified the Commission of the 25th outline plan for the joint Federal Government/*Länder* programme for improving regional economic structures ('the 25th outline plan'). By letter dated 12 August 1996, the Commission notified Germany of its decision to initiate the procedure pursuant to Article 93(2) of the EC Treaty concerning the 25th outline plan which, *inter alia,* extended eligibility for regional aid for the acquisition costs of intangible property for large firms.

The present procedure concerns the provisions detailed below.

The joint programme for improving regional economic structures, which is jointly financed and administered by the Federal Government and the *Länder,* forms the main regional aid scheme in Germany. It provides for assistance and guarantees for investment and infrastructure projects for economic activities in assisted areas that are eligible for regional aid pursuant to Article 92(3)(a) and (c) of the EC Treaty. The budgetary funds for each aid period are fixed, and any alterations in the terms for aid made, on the basis of annually-adopted outline plans.

The preceding plan, the 24th outline plan, authorised by the Commission (N 531/95)[1] specifies that, in addition to acquisition costs, manufacturing costs and leasing costs of tangible property, the acquisition costs of intangible property which can be included in an enterprise's assets (for example, patents, licences, investment or application planning) are eligible for aid provided that the intangible property:

— is acquired from a third party or from an enterprise which has no business, legal or personal links with the aid recipient,

and

— has remained for at least three years after the termination of the investment project in the ownership of the aid recipient, unless it is replaced by assets of equal or higher value; moreover, during that period the assisted property may not be leased or granted as security other than in the context of corporate restructuring recognised for tax purposes or the creation of a partnership under paragraph 15 of the Income Tax Law while remaining within the business of the aid recipient and/or a related enterprise,

and

— does not account for more than 25 % of the total investment project.

Under the 25th outline plan, Germany intends to remove the third of those conditions, that is the limit on eligibility for aid for intangible property where it accounts for more than 25 % of the cost of the overall investment project.

In its decision to initiate the procedure, the Commission expressed doubts whether the projected aid for large firms was compatible with the common market on the following grounds:

[1] OJ C 291, 4.10.1996, p. 4.

— the amendment envisaged has the effect of broadening the basis of the scheme and, applying the same aid intensity, would have the effect of increasing the permissible volume of aid above that permitted on the uniform basis of assessment laid down in the common method of assessing aid adopted by the first resolution of 20 October 1971 of the representatives of the Governments of the Member States, meeting within the Council, on general systems of regional aid [2],

— under the rules applicable when the decision to initiate the procedure was adopted, the acquisition costs of intangible property other than research and development projects were eligible for aid only in the case of small and medium-sized enterprises pursuant to the Community guidelines for State aid for small and medium-sized enterprises [3],

— in view of the mobility of intangible investments within the common market and in particular within firms belonging to the same enterprise, effective control of misuse of such aid can scarcely be conceived in so far as, even if aid were granted solely in areas eligible for regional aid, it might in reality benefit firms outside those areas.

In addition, the Commission made the following points:

— in the course of the procedure for drawing up the guidelines on national regional aid [4] and at the multilateral meetings on this matter, several delegations emphasised that the expenditure on intangible property by large firms should also be eligible for aid,

— the Green Paper on innovation [5] stresses the need to stimulate innovation,

— in the framework for State aid for research and development [6], the Commission confirmed the need to stimulate investment in intangible property, notably in assisted areas.

Regarding the eligibility of expenditure on intangible property by large firms in the new *Länder* (areas specified in Article 92(3)(a) of the EC Treaty), the Commission made the following points:

— in the areas specified in Article 92(3)(a) of the EC Treaty, under the Commission communication of 1988 on the method for the application of Article 92(3)(a) and (c) to regional aid [7], large firms may be granted, in addition to aid for investment in plant and machinery, operating aid, whose distorting effects undoubtedly exceed those of aid for intangible property up to the ceiling for regional aid,

— in the areas specified in Article 92(3)(a) of the EC Treaty there is often no appropriate local R&D activity, as is in fact the case in the new *Länder*. It is crucial to the success of the development strategy for the new *Länder* that firms there should develop competitive products and processes. In view of their liquidity difficulties, therefore, it may be fully justified to take into account their expenditure on the acquisition of intangible property.

The decision to initiate the procedure was notified to Germany and at the same time it was asked for its comments on that decision. Following the publication of the decision in the *Official Journal of the European Communities* [8], other Member States and interested parties were given the opportunity to submit observations.

II

By letter of 20 September 1996, Germany gave its comments on the decision, which are summarised below.

Germany points out that the Green Paper on innovation stresses the need to assist innovation and intangible investments and the abovementioned Community framework for State aid for research and development also emphasises the need to provide aid for intangible investments.

Regarding the Commission's expressed concern over the risk of misuse of aid because of the mobility of intangible property, Germany's view is that the basic conditions for the grant of aid for intangible investment can be considered an effective means of preventing misuse. It points out that the acquisition costs of intangible property only qualify for assistance if the investor has not acquired it from an associated enterprise, or one having business, legal or personal links to the investor. It considers that those exclusionary conditions ensure that, for example, a parent company set up outside the assisted area cannot benefit from the assistance for the acquisition costs of intangible property by having it remitted indirectly to it. Germany therefore concludes that the programme precludes remitting the aid under an agreement to that effect or an agreement conferring control of the aided company on another company. Moreover, the conditions excluding aid also exclude

[2] OJ C 111, 4.11.1971, p. 1.
[3] OJ C 213, 23.7.1996, p. 4.
[4] OJ C 74, 10.3.1998, p. 9.
[5] COM(95) 688 final.
[6] OJ C 45, 17.2.1996, p. 5.
[7] OJ C 212, 12.8.1988, p. 2.
[8] OJ C 35, 4.2.1997, p. 6.

assistance in cases where the links between the businesses are purely personal. Germany therefore concludes that assistance for the acquisition of intangible property by large firms will only be granted if there are no links, formal or otherwise, between the applicant enterprise set up in the assisted area and other enterprises from which the applicant enterprise acquires the property, whether the latter are set up inside or outside that area.

Regarding the Council resolution of 20 October 1971 ([9]) specifying the common method of assessing aid, Germany's position is that the standard base should reflect the pattern of investments which are typical of the Member State in question. The programme has been in operation for over 25 years and, in the view of the German authorities, it is necessary to adapt it to take account of the increasing significance of intangible property since it should be fully included in that base, and in the case of large firms too.

Lastly, Germany employs current data to bring out the increasing significance of intangible property in investment aid. The data indicate that investment projects for intangible property are more effective in creating jobs than 'classic' investments. In addition, if large firms were no longer excluded, it would be possible to assist investment projects with a particularly high level of innovation.

III

The other Member States and other interested parties have not presented any comments in this procedure.

However, in the process of drafting the new guidelines on national regional aid a number of Member States expressed their views on the eligibility for aid of the acquisition costs of intangible property for large firms. In the course of the multilateral meetings held on 15 May 1996 and 23 May 1997 to discuss the draft guidelines, a number of other delegations gave their opinion, in the German delegation's presence, on the eligibility of intangible property for aid.

In fact a majority of the Member States' delegations advocated that intangible assets should be eligible for aid, to some extent at least. On the other hand, at the multilateral meeting of 23 May 1997 one delegation raised the issue of the mobility of immaterial property and the resultant risk of misuse; another delegation considered that a limit on eligibility for aid of 25 % of the total investment concerned in the standard base was over-restrictive.

Lastly, Germany, in its written observations of 16 June 1997 on the draft guidelines on national regional aid, made no substantive observations on the eligibility of intangible property for aid, but only referred to the procedure involved.

It should be noted that the guidelines were adopted with regard to national regional aid on 16 December 1997 ([10]). They lay down that eligible expenditure may include certain categories of intangible investment (transfer of technology through the acquisition of patents, operating or patented know-how licences and unpatented know-how) provided that the limit of 25 % of the standard base is not exceeded in the case of large firms. Further, the intangible property must be used exclusively in the establishment receiving that aid, regarded as amortisable assets, purchased from third parties under market conditions, included in the assets of the firm and remain in the establishment receiving the regional aid for at least five years. Pursuant to point 6.1 of the guidelines, the Commission has proposed to all Member States as appropriate measures under Article 93(1) of the EC Treaty that all regional aid schemes in operation on 1 January 2000 be altered to ensure that they are compatible with the guidelines on that date.

IV

The investment aid and guarantees including those for intangible property granted under the joint Federal Government/*Länder* programme for improving regional economic structures constitute aid for the purposes of Article 92(1) of the EC Treaty. They are made available through State means to specific enterprises or industries and are liable to affect trade between Member States and thereby to distort competition.

In accordance with the common method of assessing aid indicated in the resolution of 20 October 1971, the Commission, in dealing with regional aid, adopts a standard basis for aid consisting of investment expenditure on land, buildings and plant weighted for each Member State. Under point 5(d) of the Annex to that resolution, in Germany's case this amounts to 65 % for plant and machinery, 30 % for buildings and 5 % for land. If aid is granted for additional expenditure, in this

([9]) See footnote 2.

([10]) See footnote 4.

case intangible property, under the 1971 common method a fresh calculation must be made of the base in the scheme in relation to the standard base.

The base for the costs eligible for aid specified in the 24th outline plan previously authorised by the Commission, already include, together with plant and buildings (but excluding land) the acquisition costs of intangible property provided that they do not account for more than 25 % of the total investment. The aid granted under the 24th outline plan is thus founded on a base other than the standard base. No provision is made for a fresh calculation of the base for expenses eligible for aid under the outline plan for the joint Federal Government/*Länder* programme. It follows that the volume of aid permissible under the 24th outline plan can exceed that permitted through the application of the standard base since the basis of calculation can be extended beyond 25 %, which is only partially compensated by the exclusion of land from the base for the programme.

This decision is not concerned with the compatibility with the common market of the 24th outline plan. Since the Commission has adopted the new guidelines on national regional aid and the proposal for the appropriate measures for their implementation and since, under the guidelines, the acquisition costs of certain intangible property qualify for aid provided that they do not exceed 25 % of the standard base in the case of large firms, appropriate measures pursuant to Article 93(1) to adapt the 24th outline plan for the future to the rules on State aid should not be proposed at the present stage.

The present aid project under the 25th outline plan abolishes the exclusionary threshold for aid for the acquisition costs of intangible property for large firms. The question consequently arises whether allowing without restriction, subject to certain conditions, the acquisition costs of intangible property included in the assets of the firm to be included in the base for regional aid in the case of large firms in national development areas under Article 92(3)(a) and (c) of the EC Treaty can be considered to be compatible with the common market.

The derogation in Article 92(2) of the EC Treaty is not applicable since the aid in question is not aid having a social character (under indent (a)), aid to make good the damage caused by natural disasters or exceptional occurrences (under indent (b)), or aid granted in order to compensate for the economic disadvantages caused by the division of Germany (under indent (c)).

There is also no reason to apply the derogations in Article 92(3)(b) and (d) because the aid is not 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, nor is it aid to promote culture and heritage conservation.

Lastly, the derogation in Article 92(3)(c), which concerns aid for the development of certain economic activities or of certain economic areas, is not applicable. As has been pointed out, the present procedure concerns only the eligibility of aid for the acquisition costs of intangible property for large firms since the Community guidelines on State aid for small and medium-sized enterprises make provision, on certain conditions, for the unrestricted inclusion of the acquisition costs of intangible property in the base for aid for SMEs. Moreover, the present aid project makes no provision for aid for the acquisition of intangible property in connection with the implementation of a research and development project. For this reason the provisions on the eligibility of intangible property for aid contained in the Community framework for State aid for research and development do not apply to the present case.

However, it is necessary to verify whether the aid project can be considered to be compatible with the common market under the derogations concerning particular areas envisaged in Article 92(3)(a) and (c). Since the 25th outline plan was notified before the entry into force of the new 1997 guidelines on national regional aid, the compatibility of the project must be assessed, pursuant to point 6.1 of those guidelines, on the basis of the rules applicable at the time of notification.

As Germany pointed out in its comments, the significance of innovation for ensuring that European enterprises can stand up to globalised competition is emphasised in the 1994 Commission White Paper, 'Growth, Competitiveness, Employment' [11] and in the 1995 Green Paper on innovation. To strengthen the innovatory capacities of European businesses, particular importance is attached, in addition to the completion of the internal market, economic and monetary union and an operational competition policy, to research, further training and dissemination of research. It is observed in that connection, *inter alia*, that there is less investment in research and technological development in the Member States of the Union than in other industrialised States such as the United States of America or Japan. It is also indicated that the cost of registering a patent in the Community is six times what it is in the United States of America. Germany expressly pointed out the particular

[11] COM(93) 700 final.

significance of investment in innovation in the economically less developed areas of the Community, where SMEs in particular encounter difficulties in obtaining financing for innovatory measures.

Regarding the use of public funds to attain these objectives, it is indicated in the White Paper that 'investment in training, research, the promotion of innovation and, generally speaking, the non-physical components of value-added must be treated at least as favourably as traditional forms of investment. The aim should be to promote the emergence of new generations of products that make optimum use of all the technologies available on the world market, and to encourage the dynamic incorporation of innovation into processes, products and organisation. An essential precondition is that there should be an increase in research activities by Community firms and greater selectivity in government assistance' ([12]).

Regarding the provisions on State aid, the Green Paper on innovation focuses on the revision of the Community framework for State aid for research and development.

Lastly, a recent publication ([13]) indicates that expenditure on intangible investments as very broadly defined covers expenditure on research and development, acquisition of technology, public-relations work, training and software and that enterprises' expenditure on such property has increased at both macroeconomic and microeconomic levels.

The foregoing points show that enabling the acquisition costs of intangible property to be included in the assets of a firm forms only one of the proposed measures to promote innovation by enterprises; other measures include legislative and administrative measures to establish an environment favourable to innovation or measures to promote training, research and development and investment in intangible property which cannot be included in the assets of the firm.

Regarding State aid, the Commission has already taken the following steps to support businesses' ability to innovate:

— the Community framework for State aid for research and development published in 1996 lays down that research and development projects, in the case of large firms and outside national assisted areas as well, have greater eligibility for aid up to the limits fixed in the WTO rules on aid and includes among eligible R&D costs 'research, technical knowledge and patents, etc. bought from outside sources',

— regarding SMEs, the 1996 Community guidelines on State aid for small and medium-sized enterprises lay down that aid for intangible investment inside and outside national assisted areas and expenditure on consultancy services, training and dissemination of knowledge qualify for aid,

— the 1997 guidelines on national regional aid lay down that expenditure on certain categories of intangible assets can be eligible for aid, on certain conditions, provided that it does not exceed 25 % of the standard base in the case of large firms,

— in the draft Community guidelines for State aid for training, last considered by the Member States at the multilateral meeting on 10 March 1998, there are greater possibilities for granting aid for training measures, also in the case of large firms.

This shows that the Commission has already adopted considerable measures on State aid with a view to attaining its objective of promoting the innovatory capacities of large firms. In particular, as Germany indicated in its comments, the Commission has, by adopting the new guidelines on national regional aid, adjusted the base for costs eligible for regional aid to the increasing significance of intangible investment in enterprises' investments.

Unlimited eligibility for regional aid for the acquisition costs of intangible property, where those costs exceed the levels in the abovementioned rules, cannot be considered to be compatible with the common market on the basis of the derogations for specific areas contained in Article 92(3)(a) and (c) for the reasons set out below.

First, unlimited eligibility for regional aid for the acquisition costs of intangible property would considerably extend the standard base for calculating the basis for granting investment aid. This would produce a considerable increase in the permissible volume of aid on the basis of the same aid intensity. The result would be an increased risk of distortion of competition through State aid.

Moreover, this extension of the base would reduce comparability of aid between Member States and thus

([12]) Point 2(3)(b).

([13]) Intangible investments, impact on competition and scale effects', *The Single Market Review,* Volume 2 of subseries V, European Commission, 1998.

reduce transparency in this area since the definition of intangible property which qualifying firms could include in their assets would differ in the various Member States and would depend on different accounting rules [14].

Furthermore, extending the base in the case of large firms removes the relative advantage conferred under Community law through State aid for SMEs under the Community guidelines on State aid for small and medium-sized enterprises. Those guidelines are intended to level out the handicaps limiting SMEs' access to the financing necessary to acquire new technology. This does not apply in the case of large firms, which are usually better able to carry through research programmes than SMEs and develop their own intangible property.

Regarding the risk of misuse of aid because of the mobility of intangible property, the points set out below should be made concerning Germany's arguments on this issue. The legal condition referred to by Germany that a person investing in intangible property must not acquire it from a related enterprise cannot preclude a situation where property for which aid was received in implementation of an investment project in an assisted area is transferred to another area, for example one which is ineligible for regional aid; the provision referred to by Germany can prevent the transfer of property for which aid has been granted where intangible property is acquired from a related enterprise and the assignment of the related rights to that enterprise.

On the contrary, under this provision, where intangible property is acquired from a third party not related to the enterprise in receipt of aid and set up in an assisted area, it is impossible to preclude the transfer of the property for which aid has been granted to an area ineligible for aid and the assignment of the rights in the property at a lower price than would have been the case without State aid to a (related) enterprise in an area ineligible for aid.

The fixing of a ceiling for eligibility for aid for intangible property in relation to the total cost of the tangible investments enables the intangible investments to be connected to the tangible investments so that the added value in respect of which aid was granted can be more securely linked to the assisted region. For example, the fixing of that ceiling prevents a business from setting up an enterprise in an assisted area with the sole aim of acquiring intangible property and subsequently transferring it to other enterprises, including enterprises outside assisted areas.

The abovementioned condition under the outline plan for the joint Federal Government/*Länder* programme for granting aid whereby (tangible and intangible) property must remain for at least three years after the implementation of the investment project in the ownership of the enterprise in receipt of aid unless it is replaced by property of equivalent or higher value, cannot by itself prevent the risk of misuse. This provision, in so far as compliance can somehow be verified, ensures that the intangible property will be used for this period in the enterprise in receipt of regional aid; on the other hand, it does not prevent the rights linked to the property being used in other enterprises, including those set up outside assisted areas.

In order to minimise the risk of misuse of regional aid for large firms while at the same time permitting certain acquisition costs of intangible property to be included in the base for costs eligible for aid, it is essential to link aid for intangible investments to the use of those investments for tangible assets, for example plant and equipment and buildings, if the derogations in Article 92(3)(a) and (c) of the EC Treaty are to be applied.

Regarding the existing unrestricted eligibility for aid of these costs in the case of SMEs, it should be borne in mind that SMEs, by reason of their typical handicaps, must buy in intangible property instead of developing new technology through their own research and development more often than is the case with large firms. In adopting the Community guidelines on State aid for small and medium-sized enterprises, the Commission consequently took the view that the advantage of the objective of promoting innovation for SMEs outweighed the disadvantage of the increased risk of misuse. In any event, the risk of distortion of competition through any misuse of aid remains limited in view of the size of SMEs.

Lastly, it is necessary to verify whether, by reason of the lack of innovation on the part of businesses in particularly disadvantaged regions like the new German *Länder*, the unrestricted inclusion of the acquisition costs of intangible property in the base for aid in assisted regions can be considered to be compatible with the common market under Article 92(3)(a).

[14] See footnote 13.

Moreover, in such areas the Commission makes provision for preferential aid, permitting increased intensity in the case of aid for initial investment and, on certain conditions, permitting operating aid to be cumulated with aid for initial investment; in addition, State aid for research and development can be granted with increased intensity. It consequently appears inappropriate to provide a base for costs eligible for aid other than that for cases of aid outside assisted areas pursuant to Article 92(3)(a). The arguments cited above concerning the extension of the base and the consequent risk of distortion of competition, the lack of comparability between the concepts of the intangible investments which can be included in the balance sheet of the recipient enterprise, compensation for handicaps suffered by SMEs in relation to large firms and the risk of misuse of regional aid for intangible investments cannot be disregarded in the case of aid granted in those regions.

On these grounds, the Commission considers the proposal contained in the 25th outline plan for the joint Federal Government/*Länder* programme for improving regional economic structures to repeal the provisions rendering large firms ineligible for aid for intangible property to be incompatible with the common market,

HAS ADOPTED THIS DECISION:

*Article 1*

The repeal envisaged by Germany in the 25th outline plan for the joint Federal Government/*Länder* programme for improving regional economic structures ('the 25th outline plan') of the provisions rendering large firms ineligible for aid for intangible property is incompatible with the common market in so far as it concerns firms that do not meet the definition of small and medium-sized enterprises.

*Article 2*

Germany is not entitled to apply the 25th outline plan in the form envisaged.

*Article 3*

Germany shall inform the Commission, within two months of being notified of this decision, of the measures taken to comply therewith.

*Article 4*

This Decision is addressed to the Federal Republic of Germany.

Done at Brussels, 6 May 1998.

*For the Commission*

Karel VAN MIERT

*Member of the Commission*