

Case No: 58699
Event No: 363706
Dec. No: 61/06/0COL

EFTA SURVEILLANCE AUTHORITY DECISION
OF 8 MARCH 2006
REGARDING A NOTIFICATION OF AN AMENDMENT TO THE
NATIONWIDE SEED CAPITAL SCHEME
(NORWAY)

THE EFTA SURVEILLANCE AUTHORITY,

HAVING REGARD TO the Agreement on the European Economic Area¹, in particular to Articles 61 to 63 and Protocol 26 thereof,

HAVING REGARD TO the Agreement between the EFTA States on the establishment of a Surveillance Authority and a Court of Justice², in particular to Article 24 thereof and Article 1 (2) in Part I of Protocol 3 thereof,

HAVING REGARD TO the Authority's Guidelines³ on the application and interpretation of Articles 61 and 62 of the EEA Agreement, and in particular Chapter 10A on State Aid and Risk Capital (hereinafter referred to as "the Risk Capital Guidelines"),

WHEREAS:

I. FACTS

1. Procedure

By letter dated 9 November 2005 from the Norwegian Mission to the European Union, forwarding letters from the Norwegian Ministry of Modernisation dated 4 November 2005 and the Ministry of Trade and Industry dated 2 November 2005, all received and registered by the EFTA Surveillance Authority (hereinafter "the Authority") on 9 November 2005 (Event No: 349309), Norway notified an amendment to a new seed

¹ Hereinafter referred to as the EEA Agreement.

² Hereinafter referred to as the Surveillance and Court Agreement.

³ Procedural and Substantive Rules in the Field of State Aid (State Aid Guidelines), adopted and issued by the EFTA Surveillance Authority on 19 January 1994, published in OJ 1994 L 231. The State Aid Guidelines are available on the Authority's website: www.eftasurv.int.

capital scheme: Nationwide Seed Capital Investment Companies (hereinafter “the NSCIC”).

By letter dated 22 December 2005, the Authority requested additional information concerning the notified amendment (Event No: 354867).

By letter dated 30 January 2006 from the Norwegian Mission to the European Union, forwarding letters from the Norwegian Ministry of Modernisation dated 25 January 2006 and the Ministry of Trade and Industry dated 25 January 2006, all received and registered by the Authority on 31 January 2006 (Event No: 360777), the Norwegian authorities submitted further information.

2. Background

The notification concerns an amendment to the NSCIC which was approved by the Authority on 15 July 2005⁴.

The primary objectives of the NSCIC are to increase the supply of seed capital and to increase commercialisation of research-based projects from the universities. Under the scheme, the State will finance up to 50% of four funds’ total capital in the form of subordinated loans. NOK 667 million (some EUR 81 million) has been granted for this purpose. Private investors will finance a minimum of 50% of the funds’ total capital. The funds will be 100% owned by the private investors. In addition, the State has granted NOK 167 million (some EUR 20 million), or 25% of the loans, to cover potential losses. The loans will carry an interest of 12 month NIBOR plus 2 percentage points and must be repaid within 15 years after the investment companies become operational. The Norwegian State will not pay any management fees related to the funds.

3. Description of the notified amendment

Under the scheme which was approved by the Authority on 15 July 2005, the maximum tranches of finance for target enterprises financed under the scheme are EUR 500 000 or EUR 750 000 for enterprises located in regions qualifying for assistance under Article 61(3)(c) of the EEA Agreement. The sums are for a single tranche from a combination of all state aided venture capital funds.

Concerning follow-on investments, the scheme that was approved in July 2005 contained the following cumulative conditions:

“SMEs embarking on a new investment may be eligible for a further tranche of funding up to the same limits if:

- *The investment is in a new product or development, which is wholly different from the original investment;*
- *The original investment has been deemed to have met its outputs and milestones as per the original business plan;*
- *At least six months have passed from the original investment and compliance with footnote 22 to Chapter 10A of the Authority's State Aid Guidelines is ensured.”*

⁴ Dec. No.: 181/05/COL. A copy of the Decision can be found at:
<http://www.eftasurv.int/fieldsOfWork/fieldStateAid/stateAidRegistry/sadecis05/sa181-05.DOC>

Footnote 22 to Chapter 10A of the State Aid Guidelines reads as follows: “*Separate injection of capital within six months of each other would be considered to be part of the same tranche, as would different injections, even over a longer period, to which a commitment is made as part of a single transaction*”.

The Norwegian authorities propose that these conditions are amended to:

“SMEs may be eligible for a further tranche of funding up to the same limits if:

- *The investment is in a new product or development, which is wholly different from the original investment, and*
- *At least six months have passed from the original investment and compliance with footnote 22 to Chapter 10A of the Authority's State Aid Guidelines is ensured.*

or

- *The original investment has been deemed to have met its outputs and milestones as per the original business plan, and;*
- *At least six months have passed from the original investment and compliance with footnote 22 to Chapter 10A of the Authority's State Aid Guidelines is ensured.”*

The Norwegian authorities also state in the notification as a new condition that: “*Follow-on investments cannot de facto be part of previous commitments.*”.

The reasons for this change are, according to the Norwegian authorities, that the conditions which the Norwegian authorities previously notified, and the Authority approved on 15 July 2005, makes it virtually impossible to conduct follow-on investments.

To substantiate this, the Norwegian authorities enclose documentation from potential investors and fund managers which shows that it will not be possible to establish the funds if the conditions remain like previously notified by the Norwegian authorities. The reasons stated are *i.a.*:

- The funds will invest in early-stage projects with high risk. They must expect that a large number of investments will result in losses. The notified change will increase investor's possibility of making profits from successful projects and thus make up for losses from less successful projects;
- there is great risk of dilution of the fund's investments if they are not allowed to make follow-on investments. The chances of this happening are highest in projects with the biggest potential - those that will have to make up for unsuccessful investments;
- the administrative cost for following up an investment is relatively independent of the size of the investment. The proposed change may reduce administrative costs for the funds in the scheme and ensure better administration of the running investments, as there will be fewer small investments to follow up.

The Norwegian authorities regard the notified change as the minimum necessary to attract private investors' interest.

II. APPRECIATION

1. Notification requirement

According to Article 1(3) in Part I of Protocol 3 to the Surveillance and Court Agreement, the EFTA States have an obligation to inform the Authority in sufficient time to enable it to submit its comments, of any plans to grant or alter aid. The EFTA State concerned shall not put its proposed measures into effect until this procedure has resulted in a final decision.

The present notification implies that the guidelines for the scheme will be amended. The notification will not change the legal basis of the scheme.

The Norwegian authorities have stated in the notification that the scheme will not be put into effect before the Authority has taken a decision to approve the scheme. The Authority therefore considers that the Norwegian authorities have fulfilled their obligation according to Article 1(3) in Part I of Protocol 3 to the Surveillance and Court Agreement.

2. Existence of state aid within the meaning of Article 61(1) of the EEA Agreement

The Authority has examined the amendments of the scheme in the light of Article 61 of the EEA Agreement, and in particular on the basis of Chapter 10A, State Aid and Risk Capital, of the State Aid Guidelines.

Pursuant to point 10A.4.(3) of Chapter 10A of the State Aid Guidelines, in order for a risk capital measure to fall within the scope of Article 61(1) of the EEA Agreement, four cumulative criteria must be met:

- The measure must involve the use of State resources.
- The measure must distort competition by conferring an advantage on the beneficiary.
- The advantage must be selective in that it is limited to certain undertakings.
- The measure must affect trade and competition between EEA States.

In the Authority's Decision dated 15 July 2005, the Authority found that the NSCIC constitutes state aid within the meaning of Article 61(1) of the EEA Agreement, both at the level of investors and at the level of companies invested in. The present notified amendment does not change this conclusion, since the amendment has no impact concerning the assessment of the above criteria in relation to the NSCIC.

3. Assessment of the compatibility of the notified measure

Chapter 10A of the State Aid Guidelines does not define rigid criteria by which to determine whether all possible kind of risk capital measures are compatible with Article 61(3)(c) of the EEA Agreement. However, the Guidelines sets out certain elements which the Authority regards as positive and negative in its assessment of compatibility.

When the Authority assessed the compatibility of the NSCIC in its Decision of 15 July 2005, the Authority concluded that the scheme is characterized by a number of positive elements. These include *i.a.*:

- The investments will be restricted to small or micro enterprises and/or to medium-sized enterprises in their start-up or other early stages;
- the managers will focus on risk capital market failure;
- the investment decisions will be profit driven;
- the distortion between investors and investment funds will be minimized;
- the scheme is neutral as regards sectors, but sensitive sectors and low-risk sectors like real-estate are excluded;
- the investments will take place on the basis of investment plans;
- cumulation of aid measures to a single enterprise will be avoided;
- the State will not cover any administrative costs.

On the other hand, the Authority found that the possibility to convert up to 25% of the loans to grants implies a high aid intensity that is a negative element in the meaning of Chapter 10A of the State Aid Guidelines.

In weighing these various elements together in an overall proportionality test, as described in Chapter 10A of the State Aid Guidelines, the Authority concluded that the scheme was compatible with Article 61(3)(c) of the EEA Agreement.

As regards the notified amendment to the NSCIC, the Authority's assessment is as follows:

Chapter 10A.3 of the State Aid Guidelines states that national authorities should, when deciding whether to commit or to authorise public funds for measures designed to promote risk capital, reduce as far as possible *i.a.* the risk of “deadweight”, or lack of incentive effect. If enterprises funded through publicly supported measures could have obtained the same capital in the private market, the public resources are being used unnecessarily.

The amendment to the condition for conducting follow-on investments described in point I.3 above can increase the risk of deadweight. The successful projects in which the partly state financed funds want to conduct follow-on investments in, in order to increase their profits and to avoid being diluted, might have obtained financing in the private market. In such cases it would be an additional negative element in the overall test of proportionality.

On the other hand, if the funds invest at a very early stage of a start-up, it might still be difficult to obtain private finance. The six month limitation contained in the conditions described above in point I.3, is very short compared to the time it takes to establish a successful undertaking. Furthermore, the Authority understands that seed-capital financing has a high risk, and that high profits from the successful projects are necessary to balance out the high losses from the unsuccessful projects. The Authority also takes note of the letters from the investors and potential managers arguing that it will be impossible to establish the funds unless the condition for follow-on investments is amended.

Chapter 10A of the State Aid Guidelines states *i.a.* that not all the positive and negative elements have equal weight. No single element is essential, nor can any set of them be regarded as sufficient on its own to ensure compatibility. Their applicability, and the weight attached to them, may also depend on the form of the measure.

Taking into account all the positive elements of the NSCIC scheme, as described in the Decision of 15 July 2005, the Authority finds that the scheme fulfils the overall test of proportionality set out in Chapter 10A.8 of the State Aid Guidelines, also after the amendment of the conditions for follow-on investments. The Authority therefore

concludes that the amended scheme is compatible with Article 61(3)(c) of the EEA Agreement.

4. Conclusion

The notification concerns an amendment to a scheme which was approved by the Authority on 15 July 2005. The Norwegian authorities argue that with the present conditions of the approved scheme it is virtually impossible to conduct follow-on investments. The Norwegian authorities also claim that it will be impossible to establish the funds without the amendment.

In its decision of 15 July 2005, the Authority concluded that the scheme is characterized by a number of so-called positive elements. The present notified amendment can be a negative element. However, the Authority finds that also after the conditions for conducting follow-on investments are amended, the NSCIC scheme still fulfils the overall test of proportionality set out in Chapter 10A.8 of the State Aid Guidelines. The Authority therefore concludes that the notified amendment to the NSCIC scheme is compatible with Article 61(3)(c) of the EEA Agreement.

HAS ADOPTED THIS DECISION:

1. The Authority has decided not to raise objections to the amendment to the Nationwide Seed Capital Investment Companies scheme.
2. The Norwegian authorities are requested to submit an annual report on the implementation of the scheme.
3. This Decision is addressed to the Kingdom of Norway.
4. This Decision is authentic in the English language.

Done at Brussels, 8 March 2005.

For the EFTA Surveillance Authority,

Bjørn T. Grydeland
President

Kurt Jaeger
College Member