

Event No: 363443
Case. No: 59582 (former Case No: 58806)
Dec. No.: 59/06/COL

EFTA SURVEILLANCE AUTHORITY DECISION
of 8 March 2006

to initiate the procedure provided for in Article 1(2) in Part I of Protocol 3 to the Surveillance and Court Agreement with regard to financial support to unpaid labour in research and development activities
(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 14 thereof on aid for research and development,

Whereas:

I. FACTS

1. Procedure

By letter dated 14 October 2005 from the Norwegian Mission to the European Union, forwarding a letter from the Norwegian Ministry of Trade and Industry, dated 5 October 2005, both received and registered by the Authority on 17 October 2005 (Event no: 346675), the Norwegian authorities notified, pursuant to Article 1(3) in Part I of Protocol 3 to the Surveillance and Court Agreement, a proposal for a new scheme for state aid to support unpaid labour in research and development activities.

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 - Guidelines on the application and interpretation of Articles 61 and 62 of the EEA Agreement and Article 1 of Protocol 3 to the Surveillance and Court Agreement, adopted and issued by the EFTA Surveillance Authority on 19 January 1994, published in OJ L 231, 3.9.1994, p. 1, EEA Supplement No. 32, 3.9.94, p.1, last amended by the Authority's Decision No. 329/05/COL of 20 December 2005 on financing of airports and start up aid to airlines (hereinafter referred to as the "State Aid Guidelines").

The newly proposed scheme is referred to in the following as the “Unpaid R&D Labour Scheme”.

By letter dated 27 October 2005 (Event no: 348209), the Authority acknowledged receipt of the notification.

By letter dated 13 December 2005 the Authority requested additional information according to Article 5(1) in Part II of Protocol 3 to the Surveillance and Court Agreement (Event no: 348961). The Norwegian authorities responded by letter dated 10 January 2006, enclosed in a letter from the Norwegian Mission to the European Union, dated 13 January 2006, both received and registered by the Authority on 16 January 2006 (Event no: 358121).

2. Description of the proposed measures

2.1 The objective, legal basis and function of the Unpaid R&D Labour Scheme

Objective

It appears from legislative preparatory works that the overall objective of the Unpaid R&D Labour Scheme is to stimulate increased investments in research and development activities, particularly by small companies, such as entrepreneur and one-man enterprises.⁴ More specifically, the objective of the new scheme is to stimulate efforts by individuals in research and development oriented companies which, in the start-up phase, often are dependent on work resources that cannot be paid for. Research and development oriented companies are considered by the Norwegian authorities to be important for purposes of value creation derived from research as well as for innovation.

On a more detailed level, the Norwegian authorities have explained that the introduction of the Unpaid R&D Labour Scheme was motivated by the fact that under the existing “Skattefunn Scheme”,⁵ it is not possible to support unpaid labour in research and development activities undertaken by entrepreneur and one-man enterprises due to the fact that the Skattefunn Scheme is a tax deduction scheme.⁶ In this respect the authorities have explained that under the Skattefunn Scheme aid is granted to research and development activities in the form of a tax deduction (or tax credit) whereby an amount, corresponding to a percentage of the eligible costs, is deducted from the amount due in tax by the company. However, the Norwegian authorities considered that it would not be in compliance with general tax legislation to deduct, in the amount to be paid in tax, an amount which is not based on *actual* eligible costs but rather on unpaid labour “costs” which have not been incurred in reality. On this basis it was considered that unpaid labour costs could not qualify as eligible costs under the Skattefunn Scheme.

It is against this background that the Norwegian authorities proposed the establishment of a new Unpaid R&D Labour Scheme under which financial support is

⁴ Section 3.9 of St. prp. nr. 65 (2004-2005).

⁵ The Skattefunn Scheme was approved by the Authority in its Decision No. 171/02/COL of 25 September 2002 and amendments to the Skattefunn Scheme were approved by the Authority in its Decision No. 16/03/COL of 5 February 2003.

⁶ The terms used by the Norwegian authorities for the mentioned company forms are “gründerselskaper” and “enkelpersonforetak”.

to be awarded to unpaid labour in research and development activities in the form of grants which are exempt from tax. As such the Norwegian authorities consider the Unpaid R&D Labour Scheme as a mere correction or supplement to the existing Skattefunn Scheme.

The Norwegian authorities have further explained that many companies have been in charge of projects that were approved under the Skattefunn Scheme but that some of these companies were subsequently prevented from receiving the tax deduction (or had to pay an amount corresponding to an already received tax deduction) due to the fact that unpaid labour was involved. As a result the profitability of entrepreneurs and one-man enterprises has been affected negatively. It is against this background that the Norwegian authorities adopted a decision to introduce a compensation scheme (the “Compensation Scheme”) for purposes of compensating companies for financial losses caused to their research and development projects during the years between 2002-2004 as a result of the fact that unpaid labour could not be covered by the Skattefunn Scheme.⁷ However, the Norwegian authorities consider that the Compensation Scheme does not form part of the notification in the present case as it falls under the *de minimis* threshold in the “*de minimis* Regulation”.⁸

Legal basis

In a proposition on the fiscal budget from the Norwegian Government to the Norwegian Parliament,⁹ which was followed up by a Recommendation from a Parliamentary Committee to the Parliament,¹⁰ the Government proposed to grant a budget of a total amount of NOK 70 million for the establishment of the Unpaid R&D Labour Scheme as well as the Compensation Scheme. The budget was approved by the Parliament on 17 June 2005.

In parallel, the Government presented a proposal to the Parliament in order to amend the Norwegian Act on Taxation of wealth and income for purposes of introducing provisions on tax treatment and ceilings in respect of the grants to be awarded under the Unpaid R&D Labour Scheme (hereinafter referred to as the “Tax law on the Unpaid R&D Labour Scheme”).¹¹ The proposal was furthered in a Recommendation from the Finance Committee in the Parliament.¹² On 17 June 2005 the Norwegian Parliament adopted the Tax law on the Unpaid R&D Labour Scheme.¹³

Aside from the adoption of the budget and the Tax law on the Unpaid R&D Labour Scheme, the measure intended to govern the new scheme in practice consists of draft

⁷ The Compensation Scheme is described in section 3.9 of St. prp. nr. 65 (2004-2005).

⁸ Commission Regulation (EC) No. 69/2001 on the application of Articles 87 and 88 of the EC Treaty to *de minimis* aid (OJ L 10, 13.1.2001, p. 30), incorporated into Annex XV in Section 1(e) to the EEA Agreement by means of Joint Committee Decision No. 88/2002 (OJ L 266, 3.10.2002, p. 56 and EEA Supplement No. 49, 3.10.2002, p. 42).

⁹ Section 3.9 of St. prp. nr. 65 (2004-2005): Chapter 928, item 71 concerns the Unpaid R&D Labour Scheme and Chapter 1500, item 73 concerns the Compensation Scheme.

¹⁰ Innst. S. nr. 240 (2004-2005): Section 10.1.1.2, Chapter 928, item 71 concerns the Unpaid R&D Labour Scheme; and Section 16.2.4, Chapter 1500, item 73 concerns the Compensation Scheme.

¹¹ Section 14.1 of Ot. prp. nr. 92 (2004-2005) which also refers to the original budget proposition in St. prp. nr. 65 (2004-2005).

¹² Section 15.1 of Innst. O. nr. 125 (2004-2005).

¹³ “Lov 2005-06-17 nr 74: Lov om endringer i lov 26. mars 1999 nr. 14 om skatt av formue og inntekt (skatteloven).”

guidelines on the implementation of the Unpaid R&D Labour Scheme (hereinafter referred to as the “Guidelines on the Unpaid R&D Labour Scheme”).

Finally, as regards the Compensation Scheme, the Norwegian authorities have proposed a Royal Decree on the implementation of the Compensation Scheme as well as the authorities’ plan to prepare and issue draft Guidelines on the functioning of the Compensation Scheme.¹⁴

Function of the Unpaid R&D Labour Scheme – eligible projects

It appears from the Guidelines on the Unpaid R&D Labour Scheme that eligible projects must involve research and development activities performed by individuals who are not receiving any pay or other compensation for their labour. Individuals who receive payment by means of other public sources are not covered.¹⁵

As regards the type of the projects covered by the scheme, it appears moreover from the Guidelines on the Unpaid R&D Labour Scheme that eligible projects must be aimed (but also limited to) providing new information, knowledge or experience that is presumed to be of use to the enterprise in connection with the development of new or better products, services or production methods. Moreover, activities where results from industrial research are transferred into a plan, a project or a design for new enhanced products, services or production processes, and the development of a first prototype or pilot project that cannot be commercially exploited are also eligible activities under the Unpaid R&D Labour Scheme.¹⁶ The Norwegian authorities have stated that this definition of eligible research and development projects is identical to the definition of eligible research and development projects under the existing Skattefunn Scheme. In fact, in practice the Norwegian authorities refer to eligible projects under the Unpaid R&D Labour Scheme as projects which meet the “Skattefunn criteria” or have been approved under the Skattefunn Scheme.¹⁷

The Unpaid R&D Labour Scheme is administered and implemented by “Norges forskningsråd”. The latter body is also the secretariat and the administering body, assessing whether projects are eligible under the Skattefunn scheme.¹⁸ The Norwegian authorities have explained that the fact that the definition of eligible research and development activities are defined in the same manner under both the Skattefunn Scheme and the Unpaid R&D Labour Scheme, and that the administering body, assessing whether the projects qualify as eligible, is the same under both schemes, means that for purposes of implementation the two schemes are also closely

¹⁴ “Forskrift om kompensasjon for ulønnet arbeidsinnsats i Skattefunn-godkjente forsknings- og utviklingsprosjekter for inntektsårene 2002, 2003 og 2004”. The draft Guidelines is intended to be based on “Høringsnotat om utkast til forskrift om kompensasjon for ulønnet arbeidsinnsats i Skattefunn-godkjente forsknings- og utviklingsprosjekt for inntektsårene 2002, 2003 og 2004.” (in the following referred to as “Høringsnotat”).

¹⁵ Section 6 of Part III.6.A in the Standard Notification Form and Section 3 of the Guidelines on the Unpaid R&D Labour Scheme.

¹⁶ Section 6 of Part I in the Standard Notification Form and Section 3 of the Guidelines on the Unpaid R&D Labour Scheme. However, ordinary business oriented product development without having the character of research are not encompassed, such as projects that have a continuing character or include modification of methods without requiring the development of new knowledge or the use of existing knowledge in new ways, are of an organisational character, or consist of inquires, etc.

¹⁷ Section 3 of the Guidelines on the Unpaid R&D Labour Scheme; and Section IX of the Tax law on the Unpaid R&D Labour Scheme.

¹⁸ Section 3.9 of St. prp. nr. 65 (2004-2005), Section 14.1 of Ot. prp. nr. 92 (2004-2005) and the introduction to the Guidelines on the Unpaid R&D Labour Scheme.

coordinated. In this regard applicants applying for support to eligible research and development activities must complete one single application form only in which the applicant has had the option to tick off whether support is sought for paid or unpaid labour in the relevant research and development activities.¹⁹ Moreover, financial support to be granted under the Unpaid R&D Labour Scheme will be taken into account when applicants also request support under the Skattefunn Scheme and is also limited by the maximum limit for support under the latter scheme.²⁰ In fact, according to the Norwegian authorities the only difference between the two schemes is the type of eligible costs (i.e., paid as opposed to unpaid labour) and the form in which support is granted (i.e., a tax deduction as opposed to a grant).

2.2 Recipients

The Norwegian authorities have explained that the Unpaid R&D Labour Scheme is open to all tax payers with tax liability in Norway, including all enterprises, irrespectively of their size and sector.²¹ Recipients may include undertakings jointly participating in a co-operation project.²²

The Norwegian authorities have explained that the reason that the Unpaid R&D Labour Scheme includes medium-sized and large companies is to keep it in conformity with the conditions of the Skattefunn Scheme (which is open to all enterprises regardless of size).²³ However, the Norwegian authorities have also made it clear that, in practice, the Unpaid R&D Labour Scheme is intended to target only entrepreneur firms and one-man enterprises: *“Even if the scheme includes enterprises of all sizes, the very nature of the scheme (support for unpaid labour) implies that the incentive effect will be most significant for entrepreneur-firms and one-man enterprises.”*²⁴ In the same vein the authorities have stated that the Unpaid R&D Labour Scheme is *“...primarily targeting newly established technology-based companies with no ability to pay salaries to the individuals performing the R&D activity.”* and *“As the Unpaid R&D Labour Scheme shall give support to unpaid labour performed by R&D personnel not receiving salary or other compensation for the labour, the scheme will not be relevant for ordinary medium-sized and large companies.”*²⁵

On this basis the Norwegian authorities have stated that *“Companies with an annual turnover or an annual balance sheet total corresponding to the ESA definition of medium-sized companies will in practise not receive support for unpaid labour.”* The reason for this is that, according to the Norwegian authorities, *“Larger companies generally use employed and paid R&D personnel to perform the actual R&D activity in a Skattefunn-project.”* and *“The costs of paying these employees will be eligible for*

¹⁹ Section 7 of the Guidelines on the Unpaid R&D Labour Scheme.

²⁰ See further Section 2.3 herein below on “Eligible costs and aid intensity”.

²¹ See also Section 3.9 of St. prp. nr. 65 (2004-2005) where it is stated that the Unpaid R&D Labour Scheme is addressed to one-man enterprises, limited companies and other types of companies.

²² In this case the cost frame of the project is allocated to the participants in proportion to their share of participation.

²³ The Norwegian authorities have in this context stated that *“This is also why there is no formal discrimination against larger companies in the Unpaid R&D Labour Scheme’s definition of beneficiaries.”* (emphasis added).

²⁴ Section 8.1 in Part III.6.A of the Standard Notification form.

²⁵ Letter, dated 10 January 2006, from the Norwegian Ministry of Trade and Industry.

*tax-refund in the Skattefunn Scheme, and such companies will therefore neither have need nor basis for applying for subsidy from the Unpaid R&D Labour Scheme.*²⁶

Finally, the Norwegian authorities point out that the maximum limit for support to an eligible project is the same both in case support is granted exclusively in the form of a tax deduction under the Skattefunn Scheme or by a combination of a tax deduction and a grant under the Unpaid R&D Labour Scheme. There is therefore no incentive for large companies to obtain support from both schemes. By contrast, research and development activities performed by companies which only rely on unpaid labour will not be eligible for support under the Skattefunn Scheme.

2.3 Eligible costs and aid intensity

Eligible costs

Under the Unpaid R&D Labour Scheme, eligible expenditure consists of the unpaid labour costs in an eligible project.²⁷ In terms of identifying the appropriate wage rate(s) for the unpaid labour, the Norwegian authorities have explained that as formal qualifications of an individual are not always reflected in the ability to carry out research and development projects, it was difficult to identify separate wage rates which correspond to relevant education, experience and field of work. It was therefore decided to use one common rate for the calculation of support under the Unpaid R&D Labour Scheme.

The hourly rate is based on 1,6‰ of the nominal annual industrial worker salary which for the year of 2005 results in an hourly rate of NOK 550. However, as a mark-up for social and overhead/administrative costs for purposes of unpaid labour costs was considered exaggerated, it was decided to use one common hourly rate of NOK 500 for unpaid labour performed in 2005.²⁸ The hourly rate of NOK 500 may be subject to adjustment by the Ministry of Trade and Industry on the basis of general wage developments.

As regards a ceiling on the eligible costs, it appears from the Guidelines on the Unpaid R&D Labour Scheme that the unpaid labour costs eligible for financial support is subject to a fixed ceiling of NOK 2 million annually per undertaking.²⁹

Finally, as regards control measures, the unpaid labour and the rest of the project costs must be certified by an accountant.³⁰ The Norwegian authorities have explained that as there is no evidence of reported hours in unpaid labour, companies are required to record the date, tasks, number of hours spent and the name of the relevant individual. In projects with more than one individual, the records must be signed both by the

²⁶ Letter dated 10 January 2006, from the Norwegian Ministry of Trade and Industry.

²⁷ Section 6 of Part III.6.A of the Standard Notification form.

²⁸ A similar method is applied in the context of the Skattefunn Scheme where the basis for the calculation of support to personnel and indirect costs per hour is 1,6‰ of the nominal salary. However, under the Skattefunn Scheme the nominal salary also includes social and overhead/administrative costs.

²⁹ Section 3 of the draft Guidelines on Unpaid R&D Labour Scheme. It appears from Section 3.9 of St. prp. nr. 65 (2004-2005) that the ceiling is a result of the fact that only up to 50% of the maximum limit for support to projects (carried out by the undertaking itself) under the Skattefunn scheme (of NOK 4 million) may constitute the value of unpaid labour in the project.

³⁰ Section 4 of the Guidelines on the Unpaid R&D Labour Scheme.

individual having carried out the unpaid labour and the individual responsible for the project. The reported number of hours may be reduced if it is deemed to be out of proportion of what may be considered as “normal” in comparable projects.

Aid intensity

The Guidelines on the Unpaid R&D Labour Scheme provide that grants awarded under the Unpaid R&D Labour Scheme are subject to the thresholds set out in Section 16-40 of the Norwegian Act on Taxation of wealth and income.³¹ The latter provision is the basis for the Skattefunn Scheme and provides that eligible projects may be supported with aid intensities of up to 18% or alternatively 20% in the case of small and medium-sized enterprises “SMEs” (that is, the support may amount to 18% or 20% of eligible costs).

The Norwegian authorities first stated that this means that the net aid intensities under the Unpaid R&D Labour Scheme are 18% and 20% (for SMEs) which correspond to gross aid intensities of respectively 25% and 27.8% (for SMEs).³² However, the authorities have subsequently explained and confirmed that since the support under the Unpaid R&D Labour Scheme is paid in the form of a grant, 18% and 20% (for SMEs) constitute gross aid intensities.³³ The grants are exempt from corporate tax, the rate of which is currently 28%. Finally, the Norwegian authorities have confirmed that in view of the fact that the ceiling for eligible unpaid labour costs is NOK 2 million, and that the aid intensities are 18% and 20% (for SMEs), the aid ceilings in absolute figures are NOK 360,000 and NOK 400,000 (for SMEs) on an annual basis.³⁴

The grants awarded under the Unpaid R&D Labour Scheme are considered in conjunction with aid received under the Skattefunn Scheme. In this respect it appears from the proposed and adopted Tax law on the Unpaid R&D Labour Scheme³⁵ that if, in an eligible project, it can be concluded that the total amount of the tax deduction (under the Skattefunn Scheme) and the grant (under the R&D Labour Scheme) exceeds the limits set forth in the Skattefunn scheme, the tax deduction will be diminished. The Norwegian authorities have explained that under the Skattefunn Scheme the total amount of support may not exceed 18% or 20% (for SMEs) of eligible costs, and the eligible costs may not be in excess of NOK 4 million. The Norwegian authorities have also clarified that these limits are, however, without prejudice to the fact that the costs of unpaid labour must still be within the abovementioned ceiling of NOK 2 million. Finally the authorities have explained that in case grants under the Unpaid R&D Labour Scheme and public support from sources, other than the Skattefunn Scheme, are the cause of exceeding the limit for total support, a reduction in the support granted under the Unpaid R&D Labour Scheme will be made.

³¹ Section 3 of the Guidelines on the Unpaid R&D Labour Scheme.

³² Section 7 of Part III.6.A of the Standard Notification form.

³³ This should be compared to the situation under the Skattefunn Scheme where the Authority considered in its Decision No. 171/02/COL of 25 September 2002 (approving the Skattefunn Scheme) that as the aid is granted in the form of a tax deduction, the 18% is a net grant which corresponds to a gross aid intensity of 25% (taking into account a tax rate of 28%).

³⁴ Section 3 of the Guidelines on the Unpaid R&D Labour Scheme and Section 6 of Part I in the Standard Notification form.

³⁵ Section 14.2.1 of Ot. prp. nr. 92 (2004-2005) and Section IX of the Tax law on the Unpaid R&D Labour Scheme.

2.4 De minimis

As stated above, the Norwegian authorities consider that the Compensation Scheme does not form part of the notification as it falls under the *de minimis* threshold under the “*de minimis* Regulation”.³⁶

Section 6 of the Royal Decree on the Compensation Scheme provides that the compensation will be calculated on the basis of an hourly rate of NOK 500 and that it must constitute 18% or 20% (for SMEs) of the costs for unpaid labour in eligible projects. The total amount of eligible costs may not exceed NOK 4 million in the relevant financial year where research and development is carried out by the undertaking itself or NOK 8 million in case of research and development activities carried out by research institutions.³⁷

The Norwegian authorities have stated that Article 3(1) of the *de minimis* Regulation has been complied with by virtue of a reference to the *de minimis* character of the compensation in Section 8 of the Royal Decree on the Compensation Scheme. The latter provision provides that compensation will be paid out as *de minimis* aid in accordance with the “*de minimis* Regulation”; and that if the total amount of *de minimis* aid to the applicant exceeds Euro 100,000 during a period of three years, the compensation will be reduced. Applicants which cannot receive *de minimis* aid cannot claim to be entitled to receive compensation under the Royal Decree on the Compensation Scheme.³⁸

Applicants requesting compensation must submit an overview of the total amount of all tax deductions received under the Skattefunn Scheme during the years for which compensation is sought as well as a complete overview of all *de minimis* aid received by the applicant as of 1 January 2003.³⁹ Applicants must request compensation within six weeks of the publication of the Royal Decree on the Compensation Scheme.⁴⁰ The compensation will be paid out in the form of lump sums during 2006.

2.5 Budget and duration

It appears from legislative preparatory works on the fiscal budget that out of a total amount of NOK 70 million, financed by the Ministry of Trade and Industry for 2005, NOK 60 million is the budget for the Unpaid R&D Labour Scheme (of which NOK 5 million is for administration costs) while NOK 10 million is the budget for the Compensation Scheme.⁴¹

The Unpaid R&D Labour Scheme is not limited in time. In this respect the Norwegian authorities have stated that as the objective of the Unpaid R&D Labour Scheme is to stimulate unpaid research and development activities to the same extent as paid research and development activities are stimulated under the Skattefunn Scheme, the time frame for the Unpaid R&D Labour Scheme must be the same as that for the

³⁶ Article 2(1) of the *de minimis* Regulation, see reference in footnote 8 above.

³⁷ Section 7 of the Royal Decree on the Compensation Scheme.

³⁸ It appears from the “*Høringsnotat*” that this statement refers to Article 1 of the *de minimis* Regulation which lists sectors and activities excluded from receiving *de minimis* aid.

³⁹ Section 9(h) and (i) of the Royal Decree on the Compensation Scheme.

⁴⁰ See Section 3 of the Royal Decree on the Compensation Scheme and the second paragraph in the “*Høringsnotat*”.

⁴¹ Section 3.9 of St. prp. nr. 65 (2004–2005) and Section 5 in Part I of the Standard Notification form.

Skattefunn Scheme. In this respect it appears from the Authority's approval of amendments to the Skattefunn Scheme that the Skattefunn Scheme is not limited in time.⁴² However, just as under the Skattefunn Scheme, the continuation of the Unpaid R&D Labour Scheme is dependent on the approval of an annual budget each year.⁴³

II. APPRECIATION

1. Procedural requirements

Pursuant to Article 1(3) in Part I of Protocol 3 to the Surveillance and Court Agreement, *“the EFTA Surveillance Authority shall be informed, in sufficient time to enable it to submit its comments, of any plans to grant or alter aid. [...]. The State concerned shall not put its proposed measures into effect until the procedure has resulted in a final decision”*.

By means of a letter dated 5 October 2005, the Norwegian authorities have submitted a notification for purposes of introducing the Unpaid R&D Labour Scheme under which financial support may be granted to unpaid labour in research and development activities.

As regards the entry into force of the Unpaid R&D Labour Scheme, it appears from legislative preparatory works (on the budget) that entry into force of the scheme is dependent on what would be determined in the context of adopting the Tax law on the Unpaid R&D Labour Scheme.⁴⁴ The Norwegian authorities therefore consider the Tax law on the Unpaid R&D Labour Scheme as the legal measure determining when the Unpaid R&D Labour Scheme enters into force. It appears from the adopted Tax law on the Unpaid R&D Labour Scheme that the Ministry of Finance decides when the law enters into force. It appears, moreover, from the relevant preparatory legislative works that this provision is based on the prerequisite that the Unpaid R&D Labour Scheme must be notified to, and approved by, the Authority before entering into force.⁴⁵ Subject to approval by the Authority the original objective was to have the scheme enter into force during the autumn of 2005.⁴⁶

In these circumstances - where the power of the Ministry of Finance to command the entry into force of the Unpaid R&D Labour Scheme is subject to the condition of obtaining a prior approval by the Authority - the Authority considers that the Norwegian authorities have respected its notification requirement pursuant to Article 1(3) in Part I of Protocol 3 to the Surveillance and Court Agreement.

2. The presence of State aid

2.1 State aid within the meaning of Article 61(1) of the EEA Agreement

⁴² Decision No. 16/03/COL adopted by the Authority on 5 February 2003. The Skattefunn Scheme is currently the subject of an evaluation (to be terminated in 2007) for purposes of determining whether the scheme should be continued in its present form, be altered or terminated.

⁴³ Section 5 in Part I of the Standard Notification form.

⁴⁴ Section 3.9 of St. prp. nr. 65 (2004-2005).

⁴⁵ Section 14.3 of Ot. prp. nr. 92 (2004-2005) which refers to Section 3.9 of St. prp. nr. 65 (2004-2005).

⁴⁶ See Section 7.2 in Part I of the Standard Notification form.

Article 61(1) of the EEA Agreement reads as follows:

“Save as otherwise provided in this Agreement, any aid granted by EC Member States, EFTA States 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 Contracting Parties, be incompatible with the functioning of this Agreement.”

To be termed aid, within the meaning of Article 61(1) of the EEA Agreement a measure must meet the following four cumulative criteria: The measure must (i) confer on recipients an economic advantage which is not received in the normal course of business; (ii) the advantage must be granted by the State or through State resources and must (iii) be selective by favouring certain undertakings or the production of certain goods; and (iv) distort competition and affect trade between Contracting Parties. In the following it is examined whether the four cumulative criteria are met in the present case.

2.2 Economic advantage

The measure must confer on recipients an economic advantage which is not received in the normal course of business.

Under the Unpaid R&D Labour Scheme the Norwegian authorities will award financial grants to tax payers, including all enterprises. The recipients of such grants therefore receive an economic advantage, i.e., a grant, which they would not have received in their normal course of business.

Moreover, recipients of grants are exempted from paying corporate tax on the grants. The tax exemption relieves recipients from a charge that is normally borne out of their budgets and they therefore receive one further economic advantage in addition to the grant.

2.3 Presence of State resources

The measure must be granted by the State or through State resources.

The grants awarded under the Unpaid R&D Labour Scheme are financed by the Ministry of Trade and Industry and are therefore financed by the state.

Moreover, with respect to the exemption of grants from corporate tax, a tax exemption means that the state foregoes tax revenue and a loss of tax revenue is equivalent to consumption of state resources in the form of fiscal expenditure.⁴⁷

2.4 Favouring certain undertakings or the production of certain goods

The measure must be selective in that it favours *“certain undertakings or the production of certain goods”*.

In its decision (16/03/COL) of 5 February 2003 in which the Authority assessed a notified amendment to the Skattefunn Scheme for purposes of extending the scheme to be open to all undertakings, irrespective of their size and sector, the Authority

⁴⁷ See point 3 of Chapter 17.B.3 of the State Aid Guidelines.

considered that the bodies administering and implementing the Skattefunn Scheme (i.e., “Statens nærings- og distriktsutviklingsfond” and “Norges forskningsråd”), enjoyed discretionary powers for purposes of assessing the research character of the projects and the incentive effect of the support measure.

In view of the above and the fact that the criteria for determining the eligibility of projects under the Skattefunn Scheme and the Unpaid R&D Labour Scheme are the same and are assessed by the same administering body, i.e., Norges forskningsråd, the Authority takes the view that the latter enjoys discretionary powers also for purposes of implementing the Unpaid R&D Labour Scheme. This means that the Unpaid R&D Labour Scheme is, de facto, selective. In this regard the Authority recalls that the European Court of Justice has held that discretionary powers enjoyed by the public authorities, administering a financial support scheme, means that the scheme is, de facto, selective.⁴⁸

In addition hereto, it is recalled that the Norwegian authorities state that the Unpaid R&D Labour Scheme will, in practice, only favour one-man enterprises and entrepreneur firms. To the extent that this means that Norges forskningsråd will also implement the R&D Labour Scheme in this manner (i.e., by turning down applications for support from medium-sized or large companies), the Authority considers that this is a mere confirmation of the fact that Norges forskningsråd enjoys discretionary powers and that the scheme is, de facto, selective (in favour of one-man enterprises and entrepreneur firms). Indeed the statement of the Norwegian authorities that “...there is no formal discrimination against larger companies in the Unpaid R&D Labour Scheme’s definition of beneficiaries.” (emphasis added) could be an indication that the scheme is to be implemented in the above-stated manner.

Finally, the assessment set out above is equally valid for the exemption from corporate tax enjoyed by recipients of grants under the Unpaid R&D Labour Scheme.

2.5 Distortion of competition and effect on trade between Contracting Parties

The measure must distort competition and affect trade between the Contracting Parties.

The Unpaid R&D Labour Scheme covers all sectors of the economy established in Norway. In view of the fact that for the year of 2006 exports to the EU will represent about 70% out of total exports from Norway, whereas imports from the EU will represent approximately 68% out of total imports to Norway, there is extensive trade between Norway and the EU.⁴⁹

In such circumstances, the Authority considers that the grant of support and the connected tax exemption in favour of undertakings under the Unpaid R&D Labour Scheme will strengthen the relative position of recipients compared to other undertakings located in other EEA countries and competing in similar sectors or

⁴⁸ See Case 241/94 *France v Commission* [1998] ECR I-7907, paragraphs 23 and 24; Case C-295/97 *Industrie Aeronautiche e Meccaniche Rinaldo Piaggio SpA v International Factors Italia SpA (Ifitalia), Dornier Luftfahrt GmbH and Ministero della Difesa* [1999] ECR I-3735, paragraph 39; Case 200/97 *Ecotrade Srl v Altiforni e Ferriere di Servola SpA (AFS)* [1998] ECR I-7907, paragraph 40.

⁴⁹ The relevant statistics have been issued by “Statistisk Sentralbyrå” and are entitled “Samhandelen med land og landområder. Januar. 2005 og 2006.” (Table 3). The statistics are available at: <http://www.ssb.no/emner/09/05/muh/tab-2006-02-15-03.html>.

businesses. Furthermore, in case the administering body of the Unpaid R&D Labour Scheme may indeed preclude larger companies from receiving support, the position of one-man enterprises and entrepreneur companies, receiving support under the scheme will be reinforced compared to any larger companies which would be denied support. The Unpaid R&D Labour Scheme is therefore to be regarded as affecting trade and distorting or threatening to distort competition.

2.6 Conclusion

In light of the above, the preliminary conclusion of the Authority is that the grant of support, including the tax exemption under the Unpaid R&D Labour Scheme, satisfies the test of Article 61(1) of the EEA Agreement and hence involves state aid.

3. Compatibility of the aid and *de minimis* aid

As the preliminary conclusion of the Authority is that the Unpaid R&D Labour Scheme satisfies the test of Article 61(1) of the EEA Agreement and hence involves state aid, it has to be examined whether the Unpaid R&D Labour Scheme may be considered compatible with the functioning of the EEA Agreement under Article 61(2) or (3) of the EEA Agreement.

3.1 Compatibility with Article 61(2) of the EEA Agreement

It appears that none of the exceptions under Article 61(2) apply in this case as the Unpaid R&D Labour Scheme is not aimed at the objectives listed in those provisions.

3.2 Compatibility with Article 61(3) of the EEA Agreement

A state aid measure is considered compatible with the functioning of the EEA Agreement under Article 61(3)(a) when it is designed to promote the economic development where the standard of living is abnormally low or where there is serious underemployment. However, as no such areas are defined by the Norwegian regional aid map, this provision does not apply.⁵⁰

Moreover, the exception in Article 61(3)(b) of the EEA Agreement does not apply since the state aid granted under the Unpaid R&D Labour Scheme is not intended to promote the execution of an important project of common European interest or to remedy a serious disturbance in the economy of Norway.

However, the exception laid down in Article 61(3)(c) of the EEA Agreement which provides that state aid may be considered compatible with the common market where it facilitates the development of certain economic activities or of certain economic areas and does not adversely affect trading conditions to an extent contrary to the common interest, may be applicable.

In the following the Authority considers the compatibility of the Unpaid R&D Labour Scheme with the functioning of the EEA Agreement under Article 61(3)(c) by virtue of Chapter 14 in the State Aid Guidelines on aid for research and development.

Aid for research and development in Chapter 14 of the State Aid Guidelines

⁵⁰ The Authority's Decision No. 110/98/COL of 28 April 1998 on the map of assisted areas (Norway).

(i) Eligible research and development projects and aid intensities

In Chapter 14 of the State Aid Guidelines aid granted to firms for research and development may be regarded as compatible with the functioning of the EEA Agreement on the basis of Article 61(3)(c) of the EEA Agreement. Chapter 14 sets out indicative definitions of different types of research and development, such as “*fundamental research*”, “*industrial research*” and “*precompetitive development activity*” and the aid intensities which apply.

It appears from paragraph 2 of Chapter 14.2.1 that by “*precompetitive development activity*” is meant “*the shaping of the results of industrial research into a plan, arrangement or design for new, altered or improved products, processes or services, whether they are intended to be sold or used, including the creation of an initial prototype which could not be used commercially. This may also include the conceptual formulation and design of other products, processes or services and initial demonstration projects or pilot projects, provided that such projects cannot be converted or used for industrial applications or commercial exploitation. It does not include the routine or periodic changes made to products, production lines, manufacturing processes, existing services and other operations in progress, even if such changes may represent improvements.*”

The Authority considers that the description of eligible projects under the Unpaid R&D Labour Scheme, set out above in Section 2.1 of Part I hereof, seems to be in line with the description given of “*pre-competitive development activity*” in paragraph 2 of Chapter 14.2.1 of the State Aid Guidelines.

According to paragraph five of Chapter 14.5.1 of the State Aid Guidelines, the permissible gross aid intensity for pre-competitive development activities is fixed at 25% of eligible costs. Moreover, according to paragraph one of Chapter 14.5.3 of the State Aid Guidelines, an extra 10 percentage points may be granted where the aid is given to SMEs (as defined in the Annex to the block exemption on aid to SMEs), bringing the aid intensity up to 35% of eligible costs in the case of pre-competitive activities by SMEs.⁵¹

Since the support granted under the Unpaid R&D Labour Scheme is paid in the form of a grant, 18% and 20% (for SMEs) constitute gross aid intensities. However, the fact that the grant is tax exempt is a further aid element, the value of which corresponds to the current tax rate of 28%. In the present case the total gross aid intensity corresponds, therefore, to the combined maximum value of the grant and the tax exemption which is 23.04% and 25.6% (for SMEs).⁵² The Authority therefore considers that the maximum aid intensities of the Unpaid R&D Labour Scheme are currently on an acceptable level by reference to Chapter 14 of the State Aid

⁵¹ Commission Regulation (EC) No. 70/2001 of 12 January 2001 on the application of Articles 87 and 88 of the EC Treaty to State aid to small and medium-sized enterprises (OJ L 10, 13.1.2001, p. 33), as amended by Commission Regulation (EC) No. 364/2004 of 25 February 2004 (OJ L 63, 28.2.2004, p. 22). Both Regulations have been incorporated into Section 1(f) in Annex XV to the EEA Agreement by Joint Committee Decision No. 88/2002 (OJ L 266, 3.10.2002, p. 56 and EEA Suppl. No. 49, 3.10.2002, p. 42) and Joint Committee Decision No. 131/2004 (OJ L 64, 10.3.2005, p. 67 and EEA Supplement No. 12, 10.3.2005, p. 49).

⁵² 18% and 5.04% (corresponding to 28% of 18%) is in total 23.04%. For SMEs 20% and 5.6% (corresponding to 28% of 20%) is in total 25.6%.

Guidelines. However, if the corporate tax rate should be increased, the total gross aid intensity may become higher. Therefore, in the absence of any general aid intensity ceilings which ensure that individual aid awards under the Unpaid R&D Labour Scheme do not exceed the aid intensities set out in Chapter 14.5.1 of the State Aid Guidelines, the Authority cannot be reassured that the aid intensities, which may result from the application of the Unpaid R&D Labour Scheme, will be on an acceptable level by reference to Chapter 14 of the State Aid Guidelines also in the future. On this basis the Authority has doubts that the aid intensities resulting from the application of the Unpaid R&D Aid Scheme may be considered as compatible on the basis of Chapter 14 of the State Aid Guidelines.

(ii) Eligible costs and incentive effect

Section 14.6 of the State Aid Guidelines sets out a list of costs which are to be regarded as eligible for purposes of calculating the aid intensity set out in Chapter 14. One of such cost items is personnel costs which cover the costs of researchers, technicians and other supporting staff employed solely for the research activity.

While section 14.6 of the State Aid Guidelines does not elaborate on whether personnel costs may cover costs of unpaid labour, the Authority considers that when the word “costs” has been used without any further explanation it means that the intention was only to cover the situation where costs have actually been incurred and paid. Moreover, for purposes of interpreting Chapter 14 of the State Aid Guidelines, which are based on the research and development guidelines established by the European Commission,⁵³ the Authority considers it relevant that under the Community Research Framework Programmes, financial support from the Community for unpaid labour costs cannot be obtained.⁵⁴ In this context the European Commission has adopted the view that if the value of the labour costs cannot be identified and registered in the books of the company it cannot be charged to the Framework Programme either.⁵⁵

As regards the incentive effect, it appears from section 14.7 of the State Aid Guidelines that aid for research and development should serve as an incentive for firms to undertake research and development activities in addition to their normal day-to-day operations or it may encourage firms not carrying out research and development to undertake such activities. Where the incentive effect is not evident the Authority may consider such aid less favourably than it usually does.

In the present case the Authority considers that it is doubtful whether the aid awarded under the Unpaid R&D Labour Scheme may be considered as an evident incentive to carry out research and development activities in line with section 14.7 of the State Aid Guidelines. In this respect the Authority takes the preliminary view that unpaid research and development activities would be carried out in any event, i.e., even without the aid, since the individuals carrying out unpaid labour were apparently

⁵³ Community framework for State aid for research and development (OJ C 45, 17.2.1996, p. 5) as amended.

⁵⁴ The EU’s research Framework Programme is the EU’s main instrument for research funding in Europe. In Part B.II.22.3 of Annex II to the general model contract used for purposes of granting support under Framework Programme 6, it appears that “*Physical persons may not charge any labour cost in relation to their personal involvement in the project.*” and in Part B.II.19.1(a) it appears that eligible costs “*must be actual, economic and necessary for the implementation for the project.*”

⁵⁵ E.g., the Framework Programme 6.

prepared to undertake the relevant work without pay in any event. In other words, the Authority considers that the aid appears not to be necessary in order to achieve the aim of having the relevant research and development activities carried out.

Moreover, to the extent that the Unpaid R&D Labour Scheme would also apply to larger companies, it is clear that such companies could (over time) (re-)organise their research and development activities into basing themselves on using unpaid labour instead of paid labour due to knowledge of the fact that support for unpaid labour may be obtained. In such circumstances it is certain that the support under the Unpaid R&D Labour Scheme is not the incentive for undertaking the relevant research and development activity. In this context the Authority considers that the fact that the company may - for the same project – obtain a tax deduction under the Skattefunn Scheme (by using paid labour) is irrelevant because the reason for using unpaid labour in these cases would precisely be that it is financially more attractive to obtain support for paying the labour than a tax deduction in respect of already paid labour.

On this basis the Authority takes the preliminary view that it is doubtful whether the unpaid labour costs qualify as eligible costs and whether there is any incentive effect under the Unpaid R&D Labour Scheme. In light of the comments set out above, the Norwegian authorities are invited to submit reasons as to why it may be considered that the Unpaid R&D Labour Scheme does create an incentive to carry out research and development activities and on what basis unpaid labour costs should qualify as eligible costs.

3.3 Conclusions

In view of the fact that the Unpaid R&D Labour Scheme appears not to qualify for any of the exceptions provided for in the EEA Agreement, the Authority doubts that the Unpaid R&D Labour Scheme may be considered compatible with the functioning of the EEA Agreement.

3.4 *De minimis* aid: The Compensation Scheme

The grant of state aid may qualify as *de minimis* under the “*de minimis* Regulation” where the total aid granted to any one enterprise does not exceed Euro 100,000 over any three-year period with the consequence that there is no obligation to notify.⁵⁶ It appears from Article 3(1) of the *de minimis* Regulation that the national authorities can only grant *de minimis* aid after first having verified that the total amount of *de minimis* aid received by the company is not raised beyond the ceiling by virtue of other *de minimis* aid having been received during the previous three years. One way of verifying the *de minimis* threshold is by obtaining full information from the recipient on this matter.

In the present case compensation under the Compensation Scheme will be paid out as *de minimis* aid and if the total amount of *de minimis* aid to an applicant exceeds Euro 100,000 during a period of three years, the compensation will be reduced. Moreover, the Norwegian authorities will obtain from the applicants, via their applications requesting compensation, an overview of the total amount of all tax deductions received by the applicant under the Skattefunn Scheme during the years for which

⁵⁶ Article 2 of the *de minimis* Regulation, see reference in footnote 8.

compensation is sought, as well as a complete overview of all *de minimis* aid the applicant has received as of 1 January 2003.

On the basis of the above and on the assumption that the Norwegian authorities will not grant *de minimis* aid under the Compensation Scheme where it is clear that the *de minimis* threshold has been or will, as a result of the new grant, be exceeded, the Authority considers that the Compensation Scheme is in compliance with the *de minimis* Regulation, including the requirement of verifying that the potential recipient has not received other *de minimis* aid in excess of the relevant ceiling.

On the basis of the information available, the Authority therefore takes the preliminary view that the aid granted to undertakings under the Compensation Scheme will qualify as *de minimis* aid.

3. Conclusion

Based on the information submitted by the Norwegian authorities, the Authority cannot exclude that the Unpaid R&D Labour Scheme constitutes aid within the meaning of Article 61(1) of the EEA Agreement. Furthermore, the Authority has doubts that the Unpaid R&D Labour Scheme can be regarded as complying with Article 61(3)(c) of the EEA Agreement, in combination with the requirements laid down in Chapter 14 of the Authority's State Aid Guidelines. Consequently, the Authority has doubts that the Unpaid R&D Labour Scheme is compatible with the functioning of the EEA Agreement.

Consequently, and in accordance Article 4(4) in Part II of Protocol 3 to the Surveillance and Court Agreement, the Authority is obliged to open the procedure provided for in Article 1(2) in Part I of Protocol 3 of the Surveillance and Court Agreement. The decision to open proceedings is without prejudice to the final decision of the Authority, which may conclude that the Unpaid R&D Labour Scheme is compatible with the functioning of the EEA Agreement.

In light of the foregoing considerations, the Authority, acting under the procedure laid down in Article 1(2) in Part I of Protocol 3 to the Surveillance and Court Agreement, requests the Norwegian authorities to submit its comments and to provide all such information which may help to assess the Unpaid R&D Labour Scheme, within one month of the date of receipt of this decision.

HAS ADOPTED THIS DECISION:

1. The Authority has decided to open the formal investigation procedure provided for in Article 1(2) in Part I of Protocol 3 to the Surveillance and Court Agreement against Norway with regard to the "Unpaid R&D Labour Scheme".
2. The Norwegian authorities are requested, pursuant to Article 6(1) in Part II of Protocol 3 to the Surveillance and Court Agreement, to submit their comments on the opening of the formal investigation procedure within one month from the notification of this decision and to provide all such information which may help to assess the Unpaid R&D Labour Scheme.

3. Other EFTA States, EC Member States, and interested parties shall be informed by means of publication of this decision in its authentic language version, accompanied by a meaningful summary in languages other than the authentic language version, in the EEA Section of the Official Journal of the European Union and the EEA Supplement thereto, inviting them to submit comments within one month from the date of publication.
4. This decision is authentic in the English language.
5. This decision is addressed to the Kingdom of Norway.

Done at Brussels, 8 March 2006

For the EFTA Surveillance Authority

Bjørn T. Grydeland
President

Kurt Jaeger
College Member