

How to Play Fair – A User Guide

This publication is aimed at UK further and higher education staff working in areas related to knowledge transfer, work based learning, community links, outreach, CPD, employer engagement, wider participation, and lifelong learning.

It is one of a series of publications produced by JISC Legal to raise awareness of the potential legal issues related to the use of technology by colleges and universities in relation to their business and community engagement activities.

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1. Overview

- 1.1 This guidance document is intended to assist relevant personnel within further and higher education institutions ("institutions") when dealing with State Aid issues in the context of Business and Community Engagement ("BCE") activities. It builds upon the JISC Legal Guidance "Competition and State Aid – What is the Law?" by providing practical advice on how to identify and manage State Aid issues.
- 1.2 Many institutions are now providing services to the private sector – some common examples are noted below. The key issue for institutions is that, in providing these services, the institution itself is likely to be treated as a **commercial enterprise** for the purposes of the State Aid rules.

Examples of BCE activities

Providing consultancy or research services

- Producing plans or specifications
- Carrying out safety testing or a risk assessment
- Designing a website or software
- Providing conference or business incubation facilities
- Providing training courses
- Carrying out research and development

1.3 This guidance will consider the following areas:-

- When is an institution an undertaking?
- The distinction between economic and non economic activities
- Direct and indirect State Aid
- Assessing the aid measure

2. Introduction

- 2.1 The State Aid rules prohibit national governments from providing selective financial assistance or other economic support where such intervention may distort competition and affect trade between Member States. Where a Member State proposes to grant any such assistance or support to an undertaking¹, it must first notify that measure to the European Commission ("the Commission") for clearance. State Aid which is not notified or which is granted prior to the Commission's approval is unlawful.
- 2.2 However, while the obligation to notify the measure rests with the Member State in question², the consequences of unlawful aid ultimately rest with the recipient of that measure. Quite simply, if the aid is unlawful, the Commission will order the Member State to recover the aid (with interest) from the recipient.³
- 2.3 It is therefore important that both the granters of State Aid and potential recipients (institutions, for example) understand the State Aid rules and are able to assess whether a proposed measure may raise issues under them. This Guidance document focuses on when the institution will be caught by the State Aid rules; the implications for Funders (such as Funding Councils and Research Councils) are considered in the JISC Legal Guidance "Providing Funds for BCE".
- 2.4 While each measure has to be assessed on its own merits, it is possible to follow a general framework to assist with such assessments in the context of BCE activities. This Guidance document will consider the first two stages of the framework, a summary of which is described below:-

¹ Where an entity offers goods and/or services on a market, it is referred to as an "undertaking" under EU and UK competition law.

² This will be the Member State which is granting the aid or from whose resources the measure derives.

³ The only exception to this is where such recovery would be contrary to a general principle of Community law.

Assessment Framework

If the recipient is an "undertaking"
- Paragraph 3

Assess measure
- Paragraph 4

Tests not met
- No State Aid

Tests met
- May be State Aid
(refer to JISC Legal Guidance
"**Providing Funds for BCE**")

Do any Block Exemptions Apply?

Yes
- No need to notify

No

Does it fit within an existing Scheme?

Yes
- No need to notify

No

NOTIFY

3. The Concept of an Undertaking

3.1 The State Aid rules only apply where and to the extent that the recipient of the assistance or support is an "undertaking".

General

3.2 An entity will be regarded as an undertaking when it is engaged in an economic activity (i.e. offering goods and/or services) on a given market. It should be stressed that the significant factor here is the **nature** of the activity, rather than the status of the entity. The fact that the entity is a public body, a charity or a not-for-profit organisation is, by itself, largely irrelevant for competition purposes. Rather, the issue is whether that entity provides goods or services in a commercial market.

3.3 Importantly, while an entity may be treated as an undertaking for some purposes (i.e. economic activities), at the same time that entity may not be an undertaking for other purposes (i.e. its teaching and research functions). Accordingly, the status of "undertaking" is very much activity focused.

Non Economic Activities

3.4 This issue is considered in the Community Framework for State Aid for Research and Development and Innovation ("the Framework")⁴, where the Commission states that:

" ... the primary activities of research organisations are normally of a non economic character, notably:

- education for more and better skilled human resources;
- the conduct of independent R&D for more knowledge and better understanding, including collaborative R&D;
- the dissemination of research results.

The Commission furthermore considers that technology transfer activities (licensing, spin-off creation or other forms of management of knowledge created by the research organisation) are of non-economic character if these activities are of an internal nature and all income from these activities is reinvested in the primary activities of the research organisations."

3.5 So, a University will generally not be regarded as an undertaking when carrying out its core teaching and research functions – such functions are generally considered to be public and non economic in nature. Indeed, the Commission extends this to cover technology transfer activities, provided the conditions of internality and reinvestment are met. On this basis, the public financing received by an institution in respect of its non economic activities will normally fall outwith the scope of the State Aid rules.

⁴ The Community Framework for State Aid for Research and Development and Innovation (2006/C 323/10)

Example

The Department of Computer Science has developed a new software programme which it decides to commercially exploit on the market. It plans to licence the software for an annual fee and then reinvest the revenue generated in the University's primary activities.

In terms of the Framework, this activity would normally be regarded as a non economic activity in which case the University would not be regarded as an undertaking for this purpose. However, the software should be licensed at the market rate and on normal market conditions – if not, there may be an argument that the licensee of the software has benefitted from indirect State Aid.

Status of Colleges

3.6 The Framework refers to "research organisations", which it defines as:-

" ... an entity, such as university or research institute, irrespective of its legal status (organised under public or private law) or way of financing, whose primary goal is to conduct fundamental research, industrial research or experimental development and to disseminate their results by way of teaching, publication or technology transfer; all profits are reinvested in these activities, the dissemination of their results or teaching; undertakings that can exert influence upon such an entity, in the quality of, for example, shareholders or members, shall enjoy no preferential access to the research capacities of such an entity or to the research results generated by it;"

3.7 Although there is no express reference to colleges and other further education institutions specifically, it does appear likely that they would be considered as falling within the scope of this definition. This view is supported by a later Communication⁵ from the Commission which refers to the Framework in the context of knowledge transfer.⁶

Economic Activities – Direct Aid

3.8 Where an institution's BCE activities involve the provision of goods and/or services in a commercial market (in other words, a market in which commercial entities provide competing goods and/or services), the institution will be treated like any other commercial entity in respect of those activities and will be subject to the State Aid rules. Quite simply, the institution should not use its core funding (whether directly or indirectly) for these economic activities. Rather, any such goods and/or services should be provided in normal market conditions with full recovery of the institution's costs.

⁵ Communication from the Commission to the Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions (COM (2007) 182)

⁶ The Communication refers to "Research Institutions" as covering "all higher education institutions (irrespective of their name and status in the Member States, e.g. universities, colleges or polytechnics) ...".

- 3.9 Indeed, the Framework advises that the costs and revenues of economic and non economic activities should be clearly separated to avoid any issues of cross subsidisation. The economic activities should be carried out on a wholly commercial and transparent basis with the appropriate allocation of costs and overheads associated with such activities. If the institution's resources (such as materials or facilities) are used for an economic activity, these resources should be charged and accounted for internally at the market rate. Essentially, the economic activities should be treated as a distinct and standalone unit.⁷

Example

The University is planning to offer health and safety training for local businesses. It plans to hold the training sessions in one of the training suites on the campus. These suites are frequently hired out to local businesses for their own "in house" training events, so the suites will be perfect for the University's courses.

In this case, the University should attribute a cost for the use of the training suite for the training sessions, with this cost being charged to the economic activity. As it does hire the suites on a commercial basis to third parties, the cost to be attributed to the economic activity in this case (i.e. the training sessions) should reflect that commercial hire rate.

By doing this, the University is not deriving any advantage from the use of the training suite as it is "paying" the same rate as third party hirers. The same principle applies to other University resources which are used for the economic activity.

This cost (together with other attributable costs) should then be reflected in the amount charged by the University for the training sessions. As noted above, the University should charge the market rate with full recovery of its costs.

- 3.10 If this financial separation is not implemented in practice, there is a risk that public resources may be used (whether intentionally or otherwise) to support the economic activities. Any such support is likely to constitute State Aid in favour of the institution.⁸

Economic Activities – Indirect Aid

- 3.11 There is also the risk that, rather than being viewed as a recipient of aid itself, the institution is regarded as the provider of State Aid to a commercial entity. In other words, through its dealings with a state funded institution, the commercial entity receives some advantage or

⁷ Some organisations establish a separate legal entity (i.e. a trading subsidiary) to carry out commercial activities, whereas others operate an internal division which is accounted for on a separate basis

⁸ As discussed at paragraph 4.2, the support would have to distort competition and impact on trade to breach Article 87.

benefit which it would not normally receive under normal market conditions.

3.12 The key here is to ensure that, when dealing with commercial organisations, the institution does so on fully commercial terms and treats each such organisation equally.⁹ If the institution provides a service at the market rate, there will generally be no advantage to the recipient and therefore no distortion of competition.

3.13 The Framework considers this issue of indirect State Aid in the context of contract research.¹⁰ It provides that the business will not receive State Aid through the institution if:

- The institution provides the service at market price, or
- If there is no market price, at a price which reflects the institution's full costs plus a reasonable margin.

If the service is provided on this basis, there is no advantage to the business procuring the research and there is therefore no State Aid.

Example

The University has been engaged by a local authority to carry out a contract research project. The project had been put out to competitive tender in accordance with EU procurement law.

The Commission states that, if a contract is awarded on market conditions, there will normally be no issue of State Aid. The fact that the local authority has procured and awarded the contract in line with EU procurement law will indicate that the contract has been awarded on market conditions.

3.14 Where an institution and commercial organisations participate in a collaboration project, the Framework states that:

"... no indirect State aid is granted to the industrial partner through the research organisation due to the favourable conditions of the collaboration if one of the following conditions is fulfilled:

- (1) the participating undertakings bear the full cost of the project.
- (2) the results which do not give rise to intellectual property rights may be widely disseminated and any intellectual property rights to the R&D&I results which result from the activity of the research organisation are fully allocated to the research organisation.
- (3) the research organisation receives from the participating

⁹ See example at paragraph 3.5 regarding software licensing

¹⁰ This is where an institution is engaged by a business to carry out research with the business owning the results.

undertakings compensation equivalent to the market price for the intellectual property rights which result from the activity of the research organisation carried out in the project and which are transferred to the participating undertakings. Any contribution of the participating undertakings to the costs of the research organisation shall be deducted from such compensation."

- 3.15 In other words, the commercial organisations do not derive any advantage (in State Aid terms) if the commercial organisations meet the project costs in full or if the institution acquires the IP rights in and to its results (or receives remuneration at the market rate for those IP rights).¹¹ Also, there may not be a State Aid issue where the allocation of the IP rights in, and access rights to, the results of the collaboration adequately reflects the parties' interests in and contributions to the project.¹²
- 3.16 Essentially, if none of these conditions can be met in respect of the collaboration, the Commission will consider the institution's contribution to the project to be State Aid.

4. Assessing the Aid Measure

4.1 Having established that the recipient of the aid is an undertaking, the next step is to assess the measure itself. The Commission will apply 5 tests (which reflect the key elements of Article 87) when considering a scheme which has been notified to it or when investigating a measure which has not been notified. The tests are:

- Is there a measure?
- Is it granted by the State or through State resources?
- Does it favour certain undertakings?
- Does it distort competition?
- Is the activity tradable between Member States?

Accordingly, any assessment by the proposed recipient and/or the Member State should also follow this approach.

4.2 A summary of the tests is provided below, with more detailed consideration in the JISC Legal Guidance "Competition and State Aid – what is the law?".

Summary of the Tests

¹¹ It should be noted that the remuneration for the IP rights is distinct from any contribution made towards the institution's costs (although any such contribution may be deducted from that remuneration).

¹² This condition is based upon an individual assessment, upon which the Member State may rely - in other words, having carried out this assessment, the Member State considers that there is no State Aid. The Framework makes it clear however that this does not modify the obligation to notify certain measures under Article 88(3). Accordingly, if the Member State errs in its assessment and the aid was in fact notifiable, a failure to notify will render the aid unlawful.

Is there a measure?

The scope of what constitutes a measure extends to many different forms of state financial assistance or economic advantage. Some common examples are direct State grants or subsidies, loans on favourable terms, State guarantees, free or subsidised consultancy advice and deferral of tax liabilities. The key feature however is that the measure involves some direct or indirect financial benefit for the recipient.

Is the measure granted by the State or through State resources?

The State extends to the UK and devolved Governments (and their departments), local authorities and other public sector or publicly funded bodies (including non departmental public bodies). Even where the measure is granted by a private sector body, the prohibition will still apply where that measure comprises state resources (i.e. public funds or charges).

Does the measure favour certain undertakings or the production of certain goods?

The measure must favour certain undertakings or the production of certain goods. If it does not, then it cannot be State Aid. Firstly, the measure must be selective - it must favour one entity (or group of entities) or sector over another. Secondly, the measure must confer an advantage on the recipient – in other words, was it granted in circumstances and on terms which would not have been available in the normal course of business?

Does the measure distort or have the potential to distort competition?

The Commission assumes that, subject to the de minimis threshold, any State Aid is capable of affecting competition by giving the recipient a competitive advantage over its rivals. So if a measure strengthens the recipient's position, it distorts competition.

Is there an effect on trade?

If the recipient's activities are tradable between Member States, then an effect on trade will be presumed, subject to the de minimis threshold.

5. Next steps

5.1 If all of the tests have been met, this will indicate that the aid measure may constitute State Aid. The next stage is to consider:-

- Does a Block Exemption apply?
- Does the measure fall within an existing Approved Scheme?

If neither of these applies, then it is likely that the aid measure will require to be notified to the Commission. These issues are considered in more detail in the JISC Legal Guidance "Providing Funds for BCE".

6. Summary - How to play fair

6.1 In summary, the following points should be noted:-

The Concept of an Undertaking

- An institution may be regarded as an undertaking when it is engaged in BCE activities
- It should not use its core funding to support or subsidise BCE activities
- Economic activities should be accounted for separately to avoid cross subsidisation, with full recovery of costs
- Any goods or services provided to third parties should be charged at the market rate to avoid issues of indirect aid
- An institution's core functions (teaching and research) are generally considered to be non economic in nature

Assessing the Measure

- Is there a measure?
- Does it involve the State/State resources
- Does it favour certain undertakings?
- Does it distort competition?
- Is the activity tradable between Member States?

If so, then you may be required to notify the Commission. However, the application of a Block Exemption or existing Approved Scheme may remove or reduce the obligation to notify.

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