

# Designing incentive programmes in the context of structural transformation – a review of recent policy practice in Germany

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# Outline

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1. Introduction
2. Overview of the incentive framework in Germany
3. Recent trends in designing incentive programmes
4. Case studies of selected incentive programmes
5. Lessons learnt

# 1. Introduction

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**To assist the Ministry of Economic Development and Poverty Reduction of the Republic of Uzbekistan in refining the existing incentive framework, this Policy Briefing reviews relevant experience in designing programmes in Germany**

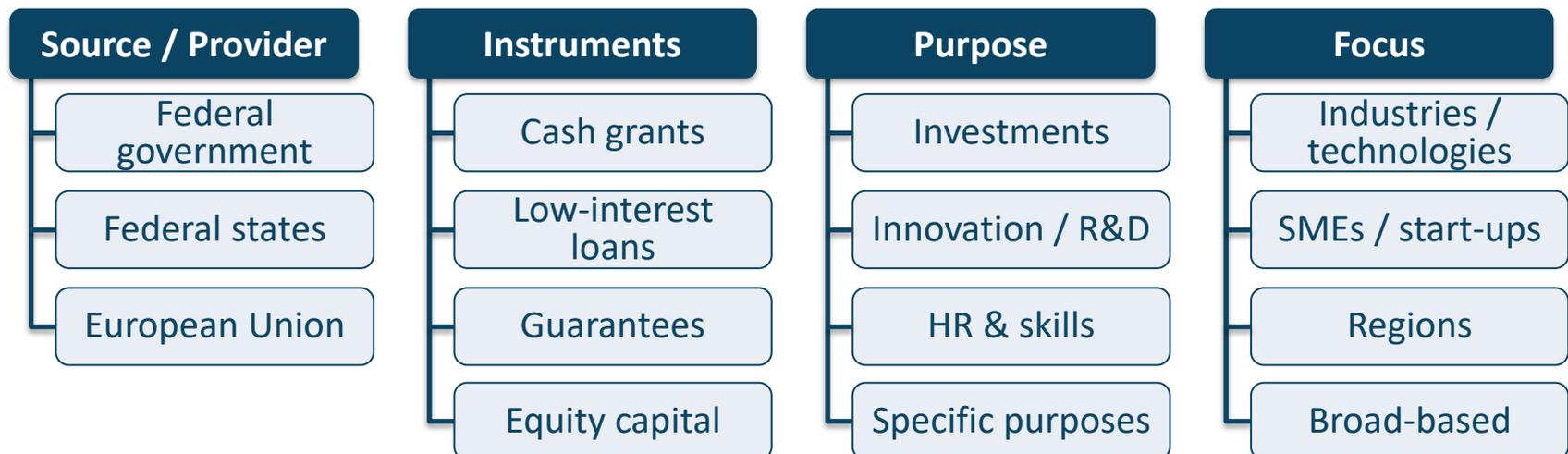
- Incentives belong to the **most commonly used policy tools** in the industrial and investment policy context
- Several countries have **recently reformed their incentive programmes** to enhance their effectiveness
- The Ministry of Economic Development and Poverty Reduction of the Republic of Uzbekistan is also planning to refine and amend the existing framework
- To support this process, this briefing reviews relevant experience in designing incentive programmes in the context of structural transformation in Germany
- The main focus is on the **funding instruments / mechanisms, the application and selection processes** and their alignment with the programmes' objectives
- **Two case studies** are used to illustrate the design principles and identify key success factors

## 2. Overview of incentive instruments

In Germany, both domestic and foreign-owned companies as well as start-ups can benefit from a wide range of incentive programmes

- Funding is provided by the German **federal government**, the individual **federal states** and the **European Union**
- Funding instruments can be grouped as (1) non-repayable **grants**, (2) low-interest **loans**, (3) public **guarantees** and (4) **equity capital**
- Germany does **not offer tax incentives** except in very limited circumstances (e.g. under the German Research Allowance Act)

### *Taxonomy of incentive programmes in Germany*



## 2. Overview of the incentive programme

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**In line with its funding purpose and objective, each programme has a specific set of criteria determining the eligibility, focus and aid intensity (amount of the incentive expressed as a percentage of the eligible costs)**

- The most common **funding purposes** comprise the support of investment projects, innovation and R&D activities as well as human resources and skills development (e.g. wage subsidies, training and recruitment support)
- The focus of the majority of programmes is **not limited to specific industries or technologies** – with the exception of the area of R&D and innovation
- For instance, programmes under the High-Tech Strategy 2025 of the German federal government focus on six priority areas (e.g. healthcare, sustainability)
- Most programmes offer **preferential conditions for SMEs**. Some programmes even exclusively target SMEs
- Equally, a **regional focus or differentiation** with respect to the aid intensity is quite common within the landscape of incentive programmes in Germany

### 3. Trends in designing incentive programmes

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Reviewing recent policy practice in Germany, the following trends in designing incentive programmes can be highlighted

- Supporting **R&D and innovation activities plays an increasingly important role** – in terms of the number of programmes and the funding volume
- This shift has wider implications affecting a range of design principles
- For instance, while, in the past, many incentive programmes were not aimed at specific industries and technologies, **recent policy practice is more targeted**
- Recent programmes also **focus more strongly on linkages**. To foster spillover effects, preferential conditions are often offered to partnerships – in particular between SMEs and research institutions
- **Competition-based selection processes** are increasingly used
  - Calls for proposals are held to select the most promising projects
  - Traditionally, incentives have been awarded to eligible applicants on a first-come-first-served basis

# 3. Trends in designing incentive programmes

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Reviewing recent policy practice in Germany, the following trends in designing incentive programmes can be highlighted (cont.)

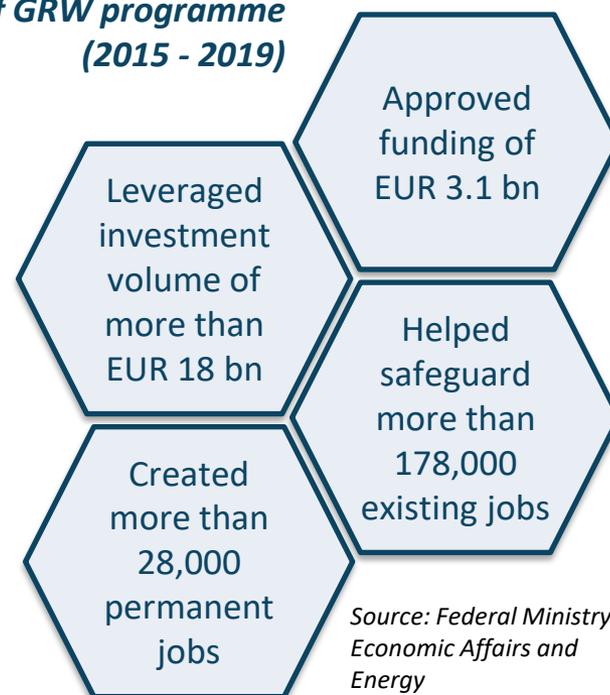
- Overall, **private sector involvement has gained in importance** in the design and implementation of incentive programmes
  - Stakeholder consultations in the design phase ensure that the needs of the beneficiaries are adequately reflected
  - In addition, the private sector is often represented in selection committees (e.g. chambers or associations)
- Furthermore, recent policy practice places **more emphasis on the social and environmental impact** of supported projects integrating corresponding eligibility and selection criteria into the programmes

## 4. Case studies of selected programmes – GRW

The GRW Programme (“Joint task for the improvement of regional economic structures”) plays a central role in Germany’s incentive framework – in particular in the context of the transformation process in the eastern part

- The programme which aims at **promoting investment, job creation and regional development** is based on a collaboration between the federal government and the federal states
- A joint **coordination framework** determines common principles (e.g. maximum aid intensity)
- The **federal states** can further **specify the rules** set out in the framework and define their own priorities (e.g. adding criteria determining the eligibility and aid intensity)
- GRW is **reviewed at regular intervals** by external experts

*Impact of GRW programme  
(2015 - 2019)*



*Source: Federal Ministry for Economic Affairs and Energy*

## 4. Case studies of selected programmes – GRW

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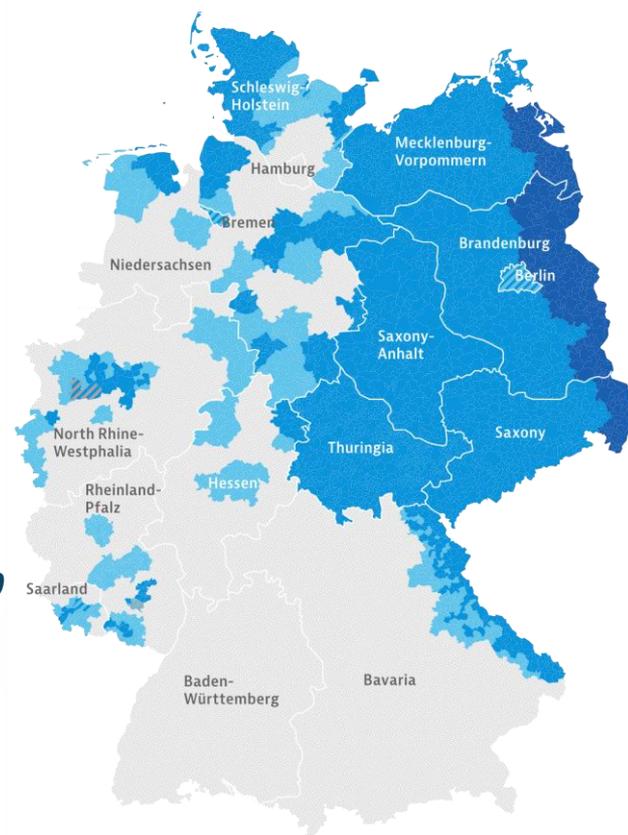
### Grants reducing the investment costs constitute a central funding instrument within the GRW programme

- The following **types of investment projects** can be supported:
  - Establishment of a new business site
  - Expansion of an existing business site
  - Changes of the portfolio of products / services or processes of an existing site
  - Takeover of a site that is closed or facing closure
- **Eligible costs** forming the base for the calculation of the grant can be either ...
  - **Project-related capital expenditure** (e.g. for new buildings, equipment, machinery) occurring in the first three years of the project or
  - **Personnel costs of newly created jobs** in the first two years
- Investors are **free to decide** whether capital expenditure or personnel costs are used as calculation basis
- In addition to investment incentives, the GRW programme comprises further components supporting e.g. the development of industrial parks

## 4. Case studies of selected programmes – GRW

Grants are only available in designated regions that have been defined in line with EU state aid rules – incl. the entire eastern part. The aid intensity varies depending upon the investment location and the size of the investor

- The designated regions are **categorised in three groups** based on a set of economic development indicators (e.g. income, unemployment)
- The maximum **aid intensity depends upon the region and size** of the investor
- For instance, for small companies investing in the border area to Poland, up to 40 % of the eligible costs can be reimbursed



*GRW grants – maximum aid intensity by firm size and region until 2020*

Region	Small companies	Medium-sized companies	Large companies
■ Border area to Poland	40 %	30 %	20 %
■ C region	30 %	20 %	10 %
■ D region	20 %	10 %	EUR 200 thsd.

Source: Germany Trade and Invest

## 4. Case studies of selected programmes – GRW

**GRW grants are provided by development banks of the federal states based on a first-come-first-served approach**

- The development banks of the federal states are responsible for the **grant application and administration process**
- Companies can apply for GRW funding **at any time through online platforms**. Application must be submitted **before the actual start** of the project
- After a first eligibility check by the development bank, a **funding committee** comprising representatives from ministries, chambers of commerce, economic development agencies and labour offices decides on the application
- The development bank issues a **grant agreement** entailing all details, deadlines and obligations
- It is also responsible for the **monitoring process and for ensuring compliance** with the obligations
- Subsidised assets / jobs must be **maintained for at least five years**

### Application documents for GRW grants

- Official application form
- Bank financing statement on secured project financing
- Business plan
- SME status verification (if applicable)

*Source: Germany Trade and Invest*

## 4. Case studies of selected programmes – GRW

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**Decisions of funding committees are based on criteria that are stipulated in the GRW coordination framework (e.g. minimum investment requirements) and can be complemented by further criteria defined by the federal states**

For instance, the Federal State of Brandenburg has defined the criteria set out below. Applicants need to fulfil at least three criteria and one in each category

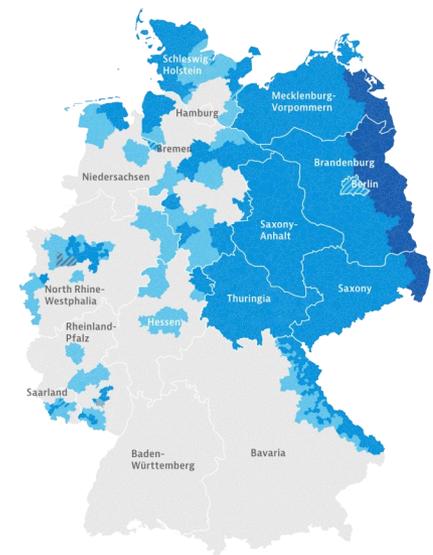
- Category **“competition, innovation, environmental impact”**
  - Competition between several locations for the investment project
  - R&D expenditure of more than 2 % of total turnover
  - Environmental certification according to national / EU standards
- Criteria **“quality jobs”**
  - Share of trainees amounting to more than 7 % of the total workforce
  - Salaries complying with collective agreements
  - More than 75 % of new employees with university / masters / specialist degrees
  - Job growth of at least 30 % in the 3 years before the application

## 4. Case studies of selected programmes – WIR!

The programme “WIR! – Transformation through innovation in the region” constitutes an example of a competition-based programme supporting collaborative projects in the area of innovation and R&D

- WIR! is a **technology-open** programme of the **Federal Ministry of Education and Research**
- It provides **consortia** of businesses, universities, research institutions and further players with **grants for collaborative innovation projects**
- It forms part of an **integrated policy package** of the German government to stimulate economic development in less developed regions
- It aims at strengthening the regional innovation dynamics **complementing existing investment policy tools** to reduce regional disparities

*Regions covered by the programme WIR!*



Source: Germany Trade and Invest

## 4. Case studies of selected programmes – WIR!

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The programme is structured into several stages to focus resources on the most promising projects and raise awareness of the potential of innovations on a broad basis at the same time

- After a **call for proposals**, interested consortia submit their applications with an outline of their project ideas
  - The programme follows an **technology-open approach** allowing the consortia to propose initiatives to address region-specific challenges and opportunities
  - Exemplary topics comprise the provision of quality medical care in declining regions, resource efficiency or structural transition in mining regions
- A jury nominated by the ministry selects **40 consortia for the concept stage**
  - Each selected consortium receives a **grant of up to EUR 250,000** (aid intensity of up to 100 %) for the development of a **regional innovation concept**
  - Eligible costs comprise, amongst others, networking events and workshops, market research and feasibility studies, coaching and organisational development

# 4. Case studies of selected programmes – WIR!

## The programme is structured into several stages (cont.)

- The jury evaluates the regional innovation concepts and selects **25 consortia for the implementation stage**
  - A **grant of up to EUR 8 million** can be provided for the implementation of the regional innovation concept for an initial period of two years (**aid intensity of 50 %**)
  - **Eligible costs** relate to, amongst others, R&D activities and equipment, training, promotion and the management of the consortium
- **Further funding** can be granted after a **mid-term review**

### Timeline of the WIR! programme

- **Until 1<sup>st</sup> February 2020:** Submission of project outlines
- **15<sup>th</sup> April 2020:** Selection of consortia for the concept stage
- **Until 31<sup>st</sup> May 2021:** Submission of regional innovation concepts
- **Mid 2021:** Selection of consortia for the implementation stage
- **Mid 2023 until mid 2024:** Mid-term review
- **End of 2027:** End of implementation phase

*Source: Federal Ministry of Education and Research*

## 4. Case studies of selected programmes – WIR!

In addition to eligibility criteria (e.g. structural characteristics of the region, composition of the consortia), the programme uses a set of selection criteria for the different stages

### Selection criteria for the concept stage

- **Plausibility** of the presented regional profile and the planned strategy design process
- **Relevance** of proposed objectives and innovation activities for structural transformation
- **Degree of novelty** of the thematic and methodological approaches
- **Transferability** of the approaches to other regions
- **Interdisciplinarity** of planned activities
- **Adequate involvement of regional actors** and the proposed coordination mechanisms
- **Traceability** of the described need for funding

### Additional criteria for the implementation stage

- **Competitive situation** of the region and consortium members regarding the innovation area
- **Suitability of the planned measures** to implement the innovation concept
- **Traceability of budget and project planning** reflecting necessary own funds of the involved members
- **Suitability of the measures** planned for further development of the innovation concept during the implementation stage and of awareness raising measures
- **Adequate management structures** of the consortium

## 5. Lessons learnt

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**Policy experience in Germany shows that incentive programmes can play an important role in structural transformation processes. Based on the analysed trends and good practices, the following success factors can be identified:**

- **Integrated approach:** Incentive programmes should not be developed in isolated, but should be aligned to a guiding economic development strategy
- **Targeted approach:** Combining different criteria (e.g. size, industry, region, sustainability) helps to achieve the intended impact and to focus the support on specific target groups (e.g. prioritising SMEs or excluding SOEs)
- **Cost-based approach:** Linking the incentives to the actual expenditure of the beneficiaries reduces the burden on public budgets
- **Monitoring-based approach:** Built-in mechanisms for reviews, monitoring, oversight and enforcement reduce the risk of abuse and unintended effects
- **Non-discriminatory approach:** The same conditions should apply for foreign and local companies
- **Transparent and rule-based approach:** An ad hoc and discretionary system for granting incentives should be avoided

## 5. Lessons learnt

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**To ensure a transparent and rule-based approach, all relevant conditions and processes should be stipulated in a manual or law/regulation, in particular:**

- **Goals and objectives** of the incentive programme
- **Duration of the programme**, incl. reviews
- **Eligible beneficiaries and projects**, detailing all eligibility criteria
- **Funding instrument** (e.g. grants, loans, guarantees – as mentioned, Germany does not offer tax incentives except in very limited circumstances)
- **Eligible costs** (using positive / negative lists) and duration of funded projects
- **Aid intensity and maximum funding volume**, incl. criteria used for a differentiation (e.g. higher aid intensity for SMEs)
- **Application and selection process** (**competition-based processes are advisable** when institutional structures are still at an earlier stage of development)
- **Institutional set-up** (incl. composition of selection committee)
- **Template for grant agreement** (comprising e.g. relevant obligations of beneficiaries, monitoring requirements and payment modalities)

# 5. Lessons learnt

**In this context, transparent and efficient administrative processes and targeted communication measures constitute further key success factors**

- **Electronic application processes** are increasingly used. **Standardised forms** allow a fair comparison of applications
- Modern grant management systems can cover further functions such as eligibility checks or monitoring
- **Information requirements** should be kept **to the necessary minimum**
- Targeted **information measures** have proven helpful to ensure an adequate quantity / quality of applications, e.g.
  - **Information events** (e.g. with chambers, associations or local government)
  - **Online marketing**

The screenshot shows the 'Antragsformular' (Application Form) for a 'Gemeinschaftsaufgabe "Verbesserung der regionalen Wirtschaftsstruktur" (GRW)'. The form is titled 'Investitionsvorhaben' (Investment Project) and includes a section for 'Art des Investitionsvorhabens' (Type of Investment Project). The form is divided into several sections: 'Allgemeines' (General), 'Investitionsvorhaben' (Investment Project), 'Angaben zu den Arbeitsplatzzielen und den Abschreibungen und Buchwerten der zu fördernden Betriebsstätte' (Information on job targets and depreciation and book values of the eligible business premises), and 'Investitionen' (Investments). The 'Investitionen' section includes 'Lohnkostenbezogene Zuschüsse' (Wage-related subsidies), 'Finanzierung' (Financing), 'Erklärungen' (Explanations), and 'Erläuterungen' (Explanations). The 'Art des Investitionsvorhabens' section includes four radio button options: 'KMU, Großunternehmen – Investition zur Errichtung einer neuen Betriebsstätte (Errichtungsinvestition)', 'KMU – Investition zum Ausbau der Kapazitäten einer bestehenden Betriebsstätte (Erweiterungsinvestition)', 'KMU – Investition zur Diversifizierung der Produktion [1] einer Betriebsstätte in vorher dort nicht hergestellte Produkte', and 'Großunternehmen – Investition zur Diversifizierung der Tätigkeit einer Betriebsstätte, sofern die neue Tätigkeit nicht dieselbe oder eine ähnliche Tätigkeit wie die früher in der Betriebsstätte ausgeübte'.

**Online application platform of the IBB  
Development Bank of the Federal State of Berlin**

# About the German Economic Team



The German Economic Team (GET) advises the governments of Ukraine, Belarus, Moldova, Georgia and Uzbekistan regarding the design of economic policy reform processes and a sustainable development of the economic framework. As part of the project we also work in other countries on selected topics.

In a continuous dialogue with high-level decision makers of the project countries, we identify current problems in economic policy and then provide concrete policy recommendations based on independent analysis.

In addition, GET supports German institutions in the political, administrative and business sectors with its know-how and detailed knowledge of the region's economies.

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