

Irish Regions Office Briefing



Latest Consultation with the Member States on Guidelines on National Regional Aid for 2007-2013

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The original document relating to this briefing may be found at:
http://europa.eu.int/comm/competition/state_aid/regional/communication_en.pdf

1. Introduction

On July 15, 2005, the European Commission circulated draft guidelines to the Member States on regional state aid. This is the latest stage in on-going consultations and will conclude with a multilateral meeting on September 15-16 to discuss these latest Commission proposals. The Department of Enterprise, Trade and Employment is responsible for this issue in Ireland and is expected to respond to the Commission in September. The Commission intends to adopt the Regional Aid Guidelines (RAG) 2007-2013 before the end of 2005.

The draft guidelines published in July is the third paper from DG Competition in the consultation process and contains a number of new proposals. These obviously have a number of implications for the Irish regions and potential opportunities for certain areas within these regions.

The Legal Base for Regional Aid

Regional Aid Guidelines refer to derogations permitted under Articles 87.3(a) and 87.3(c) of the Treaty, which allow Member States to give aid to enterprises in lagging regions and regions undergoing economic restructuring. The rules for a region's eligibility and the rates of aid allowable are linked to a region's classification under EU Regional Policy.

Article 87 (EC Treaty) states '*that any aid granted by a Member State or through State resources in any form whatsoever*' is incompatible with the single market. However, there are a number of exemptions where State aid is permissible – in this context Articles 87.3(a) and Art 87.3(c) are the most important:

Art 87.3(a) states that the payment of aid is compatible with the common market, where aid is used '*to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment*' – Objective 1 areas under current guidelines.

Art 87.3(c) states that aid can be used '*to facilitate the development of certain economic activities or certain economic areas, where such aid does not adversely affect trading conditions to an extent contrary to the common interest*' – mainly covering, but not limited to, Objective 1 in transition/Objective 2 areas under current guidelines.

2. Context for the Reform of the Guidelines

The European Commission is undertaking this reform in the context of the enlargement of the European Union and an accelerated process of economic integration following the introduction of the single currency. It is also responding to the conclusions of different European Councils which have called for less and better targeted state aid.

The European Commission is therefore adopting the following general principles in this review of the RAG:

- Regional aid can only play an effective role if the exceptional nature of the instrument continues to be assured;
- Aid ceilings must reflect the relative seriousness of the problems affecting the development of regions concerned;
- Regional aid must be concentrated on the most disadvantaged regions of the Union.
- The advantages that the aid brings in terms of the development of a less-favoured region must out-weigh the resulting distortions of competition.

3. The Demarcation of Regions

In the draft guidelines, the European Commission is proposing an overall population coverage of 42% of the population of current 25 Member States, as eligible for regional aid

2007-2013. However, to limit the adverse effects in Member States of entry into force of these new guidelines, the Commission will apply a 'safety net' to ensure that no Member States loses more than 50% of the population covered during the current period 2000-2006. The application of this 'safety net' has the effect of increasing the overall population coverage to 43.1%.

The distribution of this population coverage is as follows:

Type of Regions	Pop %
(1) Areas below 75% of EU25 GDP per capita (covered by Article 87.3(a))	27.7%
(2) Statistical effect regions (initially covered by Article 87.3(a) but subject to a review in 2009 and could then be covered by Article 87.3(c))	3.6%
(3) Economic Development Regions (including the BMW Region in Ireland) and low population density areas (covered by Article 87.3(c))	4.0%
(4) Other areas, including those under the 'safety net' (covered by Article 87.3(c))	7.8%

Implications for Ireland: Applying the safety net provision, Ireland will have a maximum population coverage of 50%. It is clear that, under the current proposals, no part of Ireland will qualify for the derogation under Article 87.3(a) and thus the 50% will come under Article 87.3(c).

4. Areas qualifying for Derogations under Article 87.3(c)

The selection of the regions eligible under Article 87.3(c) is undertaken in two steps, firstly, the determination by the Commission of the maximum population coverage for each Member State, and secondly the selection of eligible regions.

The Commission considers that the following regions may be eligible for selection by the Member States for Article 87.3(c) status:

- (1) The economic development, or 'Natural Effect' regions (*this includes the BMW Region in Ireland, but selection will be by NUTS III region*);
- (2) The low population density regions (*no regions in Ireland qualify under this*);
- (3) Regions which form contingent zones with a minimum population of at least 100,000 which are located within either NUTS II or NUTS III regions which have either a GDP per inhabitant of less than the EU-25 average or which have an unemployment rate which is higher than 115% of the national average*;
- (4) NUTS-III regions with less than 100,000 population which have either a GDP per inhabitant of less than the EU-25 average or which have an unemployment rate which is higher than 115% of the national average* (*there are no NUTS III regions in Ireland with less than 100,000 population*);
- (5) Islands and other regions categorised by similar geographical isolation which have either a GDP per inhabitant of less than the EU-25 average or which have an unemployment rate which is higher than 115% of the national average*;
- (6) NUTS-III regions or parts thereof adjacent to a region which is eligible for support under Article 87.3(a) as well as NUTS-III regions or parts thereof which share a land border with a country which is not a Member State of the European Economic Area or EFTA (*No such regions in Ireland unless sea border are considered, which is unlikely. But if so then West Wales will be eligible for Article 87.3(c) support and thus opening up possibilities for eastern parts of Ireland*).

* The designation of eligible regions would be calculated on 2000-2002 data for GDP and would be calculated on the average of the most recent 3 years of EUROSTAT data on unemployment.

However, Member States have been given further flexibility to designate other smaller areas (with a minimum population of 20,000) which do not meet the conditions outlined above, in order to target localised regional disparities below the NUTS III level. Member States wishing to designate such areas must demonstrate the level of need, using recognised economic indicators such as GDP per capita, employment or unemployment levels, or local productivity or skills indicators. Regional aid in these areas will be for SMEs but not for large companies.

5. Regional Aid Intensities

The draft guidelines set out aid intensities for each type of region. As a general rule, for Article 87.3(c) regions the ceiling on regional aid must not exceed 15%. However, this is reduced to 10% in the case of regions (at NUTS III level) with both more than the 100% average EU-25 per capita GDP and a lower unemployment rate than the EU-25 average, (based on averages for the last three years). All NUTS III regions in the S+E Region currently fulfil both these criteria. Additionally, there are bonuses for small and medium enterprises above this ceiling, 20% for small and 10% for medium enterprises¹.

Summary of Maximum Aid Intensities 2007-2013

Regions	2000-2006 NGE (Large Enterprises)	Draft Guidelines GGE Large Enterprise	Draft Guidelines GGE Medium Enterprise	Draft Guidelines GGE Small Enterprise
Article 87.3 (a)				
< 75% EU-25 GDP	40%-50%	30%	40%	50%
< 60% EU-25 GDP	50%	40%	50%	60%
< 45% EU-25 GDP	50%	50%	60%	70%
Article 87.3(a)				
Statistical Effect	40%	30% => 20%	40% => 30% (aid rate will depend on review in 2009)	50% => 40% (aid rate will depend on review in 2009)
Article 87.3(c)				
Economic Develop (Natural Effect)	40%	15% => 10% (subject to transitional provision)	25% => 20% (subject to transitional provision)	35% => 30% (subject to transitional provision)
Article 87.3(c)				
Others	10% - 20% ²	15% => 10%	25% => 20%	35% => 30%

¹ The definition of the size of enterprises is set down in the Commission Recommendation of May 6, 2003. For the purposes of the Regional Aid Guidelines, the following definitions will apply:

Small Enterprise: Less than 50 people and an annual turnover of less than €10m
 Medium Enterprise: Less than 250 people and an annual turnover of less than €50m
 Large Enterprise: Greater than 250 people

² The current aid intensities (for large enterprises) of the NUTS III regions in the S+E Region are as follows: Dublin - 17.5%; Mid-East - 18%; South-East, South-West and Mid-West - 20%

Transitional Arrangements for Economic Development Regions: The Economic Development regions will have the highest reductions in aid intensity (potentially from 40% net to 10% gross). With this in mind the Commission is proposing that the reduction of aid intensities for these regions may take place in three stages. A reduction of at least 10% net to gross shall be applied on 1 January 2007. As necessary to meet the new aid intensities allowed under these guidelines, a further reduction of 10% shall be applied on 1 January 2009 and the balance (if any) on 1 January 2011. For the BMW Regions this is likely to result in aid rates of 2007-2008: 30%GGE; 2009-2010: 20%GGE; from 2011: 15% or 10% GGE.

The Position of the Natural Effect Regions

The Natural Effect Regions (NERs) are considering the proposals from the Commission and will make a submission in advance of the September multilateral discussions. It is likely that the key concerns of the NER will be:

- (a) The removal of automatic Article 87.3(c) status at NUTS II level from the Economic Development (NER) regions;
- (b) The break in the coherence between the regions eligible under the regional aid guidelines and the regions eligible under the Structural Fund regulations.
- (c) The creation of more Article 87.3(c) areas across the EU could significantly reduce the competitive advantage of NERs both within and between Member States.

Furthermore, the NERs welcome the transitional scheme proposed for their regions, which should provide some continuity between the current and new regime rather than a sharp reduction in aid intensity. Nonetheless, the NER are likely to make at least two key demands:

- (1) That the Economic Development (NER) regions should be automatically designated as Article 87.3(c) regions at NUTS II level and thus maintaining the direct link with EU Regional Policy.
- (2) That the Economic Development (NER) regions should be eligible for a basic aid intensity of 15% after the transition phase has been completed, regardless of the GDP and unemployment levels of the regions, to sustain their economic development.

6. Other Selected Aspects of the Regional Aid Regime 2007-2013

Aid as part of Coherent Regional Policy: The draft guidelines are very clear in specifying that the regional aid covered by the derogation in 87.3(c) must form part of a coherent regional policy of the Member State and adhere to the principles of geographical concentration. In particular, Para 8 of the draft guidelines states:

“As a general rule, regional aid should be granted under an aid scheme which forms an integral part of a regional development strategy, with clearly defined objectives. Such a scheme may also enable the competent authorities to prioritise investment projects according to their interest for the region concerned. Where, exceptionally, it is envisaged to grant individual ad hoc aid to a single firm, or aid confined to one area of activity, it is the responsibility of the Member State to demonstrate that the project contributes towards a coherent regional development strategy and that, having regard to the nature and size of the project, it will not result in unacceptable distortions of competition.”

Forms of Regional Aid: Regional aid is aid awarded for an initial investment project and the draft guidelines set out what is intended by ‘initial investment’, including the extension of existing establishments and the diversification of output of an establishment into new product markets. The form of regional aid is variable and may, for example, take the form of grants, low-interest loans or interest rebates, state guarantees, the purchase of a shareholding or an alternative provision of capital on favourable terms; exemptions or reductions in taxes, social security or other compulsory charges; or the supply of land, goods or services at favourable prices.

Conditions on Regional Aid: In order to ensure that the investment makes a real and sustained contribution to regional development, the Commission emphasises that aid must be made conditional, on the maintenance of the investment in question in the region concerned for a minimum period of at least five years after its completion. In addition, where the aid is calculated on the basis of wage costs, each of the jobs created through the investment must be maintained within the region concerned for a period of five years from the date the post was first filled. In the case of SMEs, Member States may reduce these five year periods for the maintenance of an investment or jobs created to a minimum of three years.

Change to Gross Grant Equivalent (GGE): A change from current practice is the discontinuation of converting regional aid notified by Member States into Net Grant Equivalent (NGE). NGE is where the Commission takes into consideration the incidence of tax on the amount of financial aid allocated when it assesses whether it is compatible with the Treaty. All aid rates will now be in Gross Grant Equivalent (GGE)

The full effects of this change have still to be assessed. However, the change is generally seen as favouring those Member States with a low (corporate) tax base, as these Member States will effectively be able to give more aid to enterprises. While this would make Article 87.3(c) regions in Ireland more attractive in these terms than regions in many other Member States with similar aid intensities, it is unclear what the impact of changing to GGE will be on any other forms of tax exemptions that Ireland offers to secure investment.

The change from NGE to GGE has been made to take account of a judgement of the Court of First Instance. Furthermore, the Commission considers that the use of GGE, which is also used to calculate the intensities of other types of state aid, will contribute to increasing the simplicity and transparency of the state aid control system, and also take account of the increased proportion of state aid which is awarded in the form of tax exemptions.

7. Regional Aid Maps – Notification by the Member States

Within three months of the adoption of the RAG guidelines, each Member State should notify to the Commission a single regional aid map covering its entire national territory.

This map should clearly identify the regions concerned, the aid intensities envisaged for large companies and all applicable bonuses for SMEs. Member States also have to provide supporting information to explain the designation of the Article 87(3)(c) regions, other than the economic development, the low population density and the border regions, including, the detailed identification of the regions concerned, population data, information on GDP and unemployment levels in the regions concerned, and any other relevant information.

Once agreed the regional aid maps for each Member State form an integral part of the guidelines on regional aid and have binding force.

It will obviously be a matter for each region, county or part thereof, which considers that it may meet the selection criteria for eligible Article 87.3(c) areas (set out in Section 4 above), to make its case for inclusion in the national regional aid map.

Some Possible Implications in Ireland

The draft guidelines provide some clear indications on the regional state aid regime 2007-2013. However, they also raise a number of issues for Ireland in this regime.

For the Border, Midland, Western Region

While the draft guidelines provide no guarantees that the 'economic development' regions must definitely be designated as Article 87.3(c) regions, it would be unlikely that the Irish Government would refuse to designate the BMW Region as such. However, designation of this area would have to be made at NUTS III level, with the effect that the three NUTS III regions could have different basic aid rates from 2011 onwards.

The key issues for the BMW Region at this stage would seem to be:

- (a) Ensure that the entire region is designated, automatically as an Article 87.3(c) 'Economic Development' region, with the transition period from the current to the new regime.
- (b) Ensure that the BMW Region would maintain some competitive advantage over the rest of the country in terms of attracting investment. If regions or local areas in the S+E Region are also to be designated under Article 87.3(c) (at a basic rate of 10%) then the BMW needs to argue that it requires a higher aid rate in order to reinforce and safeguard the policy of achieving balanced regional development.
- (c) Demand, therefore, from the Commission that the Economic Development regions would automatically benefit from the higher basic aid intensity (of 15%), after the transition period has been completed regardless of the GDP and unemployment levels in the region.

For the rest of Ireland

Assuming that the BMW will be designated as an Article 87.3(c) region, there are still opportunities for areas in the Southern and Eastern Region. Applying the safety net provision, Ireland has been allocated a population coverage for regional aid of 50%. The BMW Region has some 26.5% of the national population (in 2002), leaving a significant proportion within the S+E region (approximately a population of about 920,496) still potentially eligible for Article 87.3(c) status.

The draft guidelines provide Member States with some flexibility in terms of designating certain areas for aid purposes (as outlined above in Section 4). The key questions in this regards would seem to be:

- (a) What areas, if any, in the S+E Region meet the GDP and national unemployment criteria for being designated as Article 87.3(c) regions?
- (b) Will the Government use the flexibility permitted by the draft guidelines to designate counties or parts thereof as Article 87.3(c) areas to support small and medium sized enterprises – are there such areas which the Government could argue the case for?
- (c) In approaching these designation issues, how will the Government meet the requirements of having the derogations under Article 87.3(c) as part of a coherent regional policy and adhering to the principle of geographical concentration?

Note on Northern Ireland

While Northern Ireland is not designated with Article 87.3(a) status, it has in fact benefited from the same aid intensities as many of the current Article 87.3(a) regions. Therefore, for the period 2006-2013, the Commission intends to consider Northern Ireland as an

'economic development' region for the purposes of the Regional Aid Guidelines, similar to the BMW region.