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The Reform of the European Structural Funds and the Cohesion Fund

(revised edition)

The programmes of assistance available under the European Structural Funds and the Cohesion Fund are presently being renegotiated between the Commission and the Member States. This renegotiation is part of a much wider reassessment of the financing of the EU as a whole necessitated, not only by the likely enlargement of the EU, but also because the present framework of expenditure (the Financial Perspective) expires in 1999.

This Paper provides an overview of the operation of the European Structural Funds and the Cohesion Fund. The Commission's proposals for the new Objectives and the reforms of the Cohesion Fund are then considered. There is also a discussion of the review of the NUTS regions that the UK Government has recently undertaken.

The symbol "• " denotes the Euro, the currency in which the future spending plans of the EU are now denominated.

This Paper has been revised to take account of the new data for GDP per capita that were published by the Office for National Statistics on 22 October 1998.

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Summary of main points

The programmes of assistance available under the European Structural Funds and the Cohesion Fund are presently being renegotiated between the Commission and the Member States. These negotiations are likely to continue into the early part of next year. They are part of a much wider reassessment of the financing of the EU as a whole necessitated, not only by the likely enlargement of the EU, but also because the present framework of expenditure (the Financial Perspective) expires in 1999.

The Trade & Industry Committee recently reported on the reform of the European Structural Funds.[1] This Report is due to be debated in the House of Commons on Thursday 22 October. The House of Lords Select Committee on the European Communities has also produced a report on the same topic.[2] Unless otherwise stated, all references to Select Committee Reports in this Paper are to these two documents. This Paper provides a background to the issues likely to be raised in this debate, and updates some of the information contained in the two Reports.

The structural operations as a whole (the Structural Funds and the Cohesion Fund) account for around 40 per cent of total EU expenditure each year. In 1998 the EU committed 34 billion ECU to structural operations - over £22 billion at current exchange rates. Over the period 1994 to 1999 the United Kingdom will receive 13.7 billion ECU in 1998 prices, or approximately £10.1 billion. The outcome of these negotiations could have significant implications for both the total amount received in the future, and the regions of the United Kingdom that will benefit from the spending.

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[1] Trade & Industry Committee, *Reform of European Structural Funds*, 17 June 1998, HC 697 1997-98

[2] House of Lords Select Committee on the European Communities, *The Reform of the Structural Funds and the Cohesion Fund*, 28 July 1998, HL 138 1997-98

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I Current Arrangements

A. Introduction

The principal means by which the EU encourages greater economic and social cohesion and uniformity of living standards is to channel financial assistance and resources to the less well-off regions through a series of inter-related funds, collectively known as the Structural Funds. These are the European Regional Development Fund (ERDF), the European Social Fund (ESF), the European Agricultural Guidance and Guarantee Fund (EAGGF) guidance section and the Financial Instrument for Fisheries Guidance (FIFG). Assistance is also given through the European Investment Bank and the Cohesion Fund.[3]

Various parts of the UK are designated as being eligible for assistance under the different programmes. In most cases, designations last for several years since the programmes are organised on a multi-annual basis. The Commission provides global sums of money for the implementation of national development plans. As most regional funding is provided on a programme basis, the sums allocated under each scheme are often received over a period of years rather than in one lump sum.

Structural Fund expenditure is expected to complement national policies and actions: it should supplement rather than displace resources allocated at a national level. As a general rule, the EU contributes no more than 50 per cent of the total cost of projects.

B. The Objectives

Financial assistance from the Structural Funds presently concentrates on six Objectives which focus attention on the regions and groups in society most in need of assistance. All parts of the EU are equally eligible for support under Objectives 3, 4 and 5(a). However, it is under the other Objectives - 1, 2 5(b) and 6 - that specific *regions* and *areas* qualify for support.

Objective 1	to promote the development and structural adjustment of regions whose development is lagging behind the rest of the EU
Objective 2	to convert regions seriously affected by industrial decline
Objective 3	to combat long-term unemployment and facilitate the integration into working life of young people and of persons exposed to exclusion from the labour market
Objective 4	to facilitate the adaptation of workers to industrial changes and to changes in production systems

[3] FIFG is concerned solely with programmes under Objective 5(a). The Cohesion Fund is only applicable to Greece, Spain, Ireland and Portugal under the provisions of the Maastricht Treaty, but cannot be used to finance projects that receive support from the ERDF, the ESF or the guidance section of the EAGGF.

Objective 5 (a)	speeding up the adjustment of agricultural and fisheries structures in the framework of the reform of the Common Agricultural Policy
Objective 5 (b)	facilitating the development and structural adjustment of rural areas
Objective 6	assisting the development of sparsely-populated regions (Sweden & Finland only)

Areas that are eligible for Objective 1 funding are not eligible for assistance under the other regional Objectives; furthermore, they do not, at present, qualify for assistance under Objectives 3 or 4. The table below shows the amounts of money allocated to each Member State under each Objective (together with the Community Initiatives outlined in Part C below) for the programming period 1994 to 1999.

Table 1

Structural Fund Allocations 1994 - 1999

million ECU, 1998 prices

	Main Objective Programmes						Community	
Country	1	2	3&4	5(a)	5(b)	6	Initiatives	Total
Belgium	757	353	481	201	80	..	298	2,170
Denmark	..	124	312	276	56	..	106	874
Germany	14,139	1,621	2,011	1,181	1,272	..	2,287	22,511
Greece	14,492	..	..	..	..	..	1,196	15,688
Spain	27,262	2,500	1,908	461	688	..	2,884	35,703
France	2,270	3,906	3,316	1,996	2,319	..	1,663	15,470
Ireland	5,826	..	..	..	..	..	461	6,287
Italy	15,404	1,514	1,776	842	934	..	1,967	22,437
Luxembourg	..	16	24	41	6	..	20	107
Netherlands	156	673	1,117	170	155	..	440	2,711
Portugal	14,492	..	..	..	..	..	1,098	15,590
United Kingdom	2,446	4,742	3,496	465	847	..	1,656	13,652
Austria	174	106	413	406	430	..	153	1,682
Finland	..	167	544	218	144	264	134	1,471
Sweden	..	192	358	370	204	482	161	1,767
Total EU 15	97,418	15,914	15,756	6,627	7,135	746	14,524	158,120

Source: Trade & Industry Committee Report, HC 697 1997/98

Note: The UK's total allocation of 13,652 million ECU is worth approximately £10.2 billion using an exchange rate of £1 = 1.34 ECU.

1. Objective 1

Objective 1 is to assist those regions whose development is lagging behind the rest of the Community, and is financed from all three Structural Funds. Objective 1 areas attract the largest share of regional aid - currently some two thirds of the total budget. The principle Regulation governing the way in which the structural funds operate at present is Council Regulation (EEC) No 2081/93. Article 8 of the Regulation refers to Objective 1 regions:[4]

> The regions covered by Objective 1 shall be regions at NUTS level II whose per capita GDP, on the basis of the figures for the last three years, is less than 75% of the Community average.
>
> Northern Ireland, the five new German Länder, east Berlin, and the French overseas departments, the Azores, the Canary Islands and Madeira shall also be covered by this Objective, as shall other regions whose per capita GDP is close to that of the regions referred to in the first subparagraph and which have to be included within the scope of Objective 1 for special reasons.
>
> Abruzzi shall be eligible for aid under Objective 1 for the period 1 January 1994 to 31 December 1996.
>
> Exceptionally, in the view of their unique adjacent position and their regional GDP at NUTS level III, the "arrondissements" of Avesnes, Douai and Valenciennes as well as Argyll and Bute, Arran, the Cumbraes and western Moray shall also be covered by this Objective.

The sole criterion for awarding Objective 1 status is the application of the 75 per cent of per capita EU GDP per capita criterion to NUTS 2 regions.[5] The Regulation shows that are a number of exceptions have been made – both on the 75% threshold and on the geographical areas used. Objective 1 is funded by the ERDF, the ESF and the Guidance section of the EAGGF.

2. Objective 2

Funds distributed under Objective 2 are intended to revitalise regions affected by serious industrial decline, where traditional industries such as coal, steel, shipbuilding and textiles have contracted significantly, causing major economic and social hardship and dislocation for the local workforce. In drawing up lists of eligible areas for the 1994 to 1999 programming round the Commission took into account statistics on unemployment and job losses, together with special factors drawn to its attention by the Member States themselves.

Within the United Kingdom the following areas are eligible for Objective 2 funding: the North East of England, South Yorkshire, parts of West Yorkshire, Humberside, Nottinghamshire and Derbyshire; parts of the West Midlands, the North West (including

4 Council Regulation (EEC) No 2081/93, Article 8

5 The Nomenclature of Territorial Units for Statistics (NUTS) is a single, uniform breakdown of territorial units for producing regional statistics across the European Union. NUTS regions take a hierarchical form, usually following administrative areas.

the western part of Cumbria), central Scotland, South Wales, Plymouth, the Lea Valley in London and Thanet in Kent. Objective 2 is funded by the ERDF and by the ESF.

The criteria used for the present round of Objective 2 funding are more complicated than those used for Objective 1, and more flexible:[6]

> …the areas referred to must represent or belong to a NUTS level III territorial unit which satisfies all the following criteria:
> (a) the average rate of unemployment recorded over the last three years must have been above the Community average;
> (b) the percentage share of industrial employment in total employment must have equalled or exceeded the Community average in any reference year from 1975 onwards;
> (c) there must have been an observable fall in industrial employment compared with the reference year chosen in (b).

Article 9 of the Regulation also allows the scope for assistance to be extended to other areas not meeting these main criteria. The following areas may also be included, subject to the provisions shown in the paragraph labelled "4" below.

> - adjacent areas satisfying criteria (a), (b) and (c) as well as areas satisfying criteria (a), (b) and (c) that are adjacent to Objective 1 areas;
> - urban communities with an unemployment rate at least 50% above the community average which have recorded a substantial fall in industrial employment;
> - areas which have recorded substantial job losses over the last three years or are experiencing or are threatened with such losses in industrial sectors of decisive importance for their economic development, including losses brought about by industrial changes and changes in production systems, with a consequent serious worsening of unemployment in those areas;
> - areas, especially urban areas, with severe problems linked to regeneration in derelict industrial sites;
> - other industrial or urban areas where the socio-economic impact of the restructuring of the fisheries sector, assessed on the basis of Objective criteria, justifies such assistance.
>
> 4. In implementing the criteria defined above, the Commission will take account of how the national situations with respect to unemployment rate, industrialisation rate and industrial decline compare with the Community average.
>
> For the application of these criteria, Member States may also take as a reference basis the specific realities influencing the actual activity rate or employment rate of the population.

This extends the scope of the areas that can potentially be included, and also introduces a certain amount of flexibility into how areas are assessed. Article 9 also includes provisions for Member States to nominate particular areas for consideration:

[6] Council Regulation (EEC) No 2081/93, Article 9

> In establishing that list [of eligible areas] … the Commission and the Member States shall seek to ensure that assistance is genuinely concentrated on the areas most seriously affected, at the most appropriate geographical level, taking into account the particular situation of the areas concerned. Member States shall supply to the Commission all information which might be of assistance to it in this task.

3. Objectives 3 and 4

Objectives 3 and 4 are not considered in great detail in this Paper, since they are 'horizontal' Objectives applicable to all Member States on a national basis, rather than being regionally-based Objectives.[7] Funding under objective 3 is targeted at helping the long-term unemployed, young people entering the job market and other people facing particular disadvantages in finding or keeping work (such as single parents, people with learning disabilities etc.). Objective 4 funding is directed towards those already in employment and aims to ensure that the workforce is trained to enable it to adapt to industrial and technological change. Objectives 3 and 4 are funded only by the ESF.

4. Objective 5(a)

Objective 5(a) is also a horizontal Objective, being applicable throughout the EU. Its aim is to provide assistance for rural areas where either agriculture or the fishing industry needs to be reorganised as a result of the reform of the Common Agricultural Policy and the Common Fisheries Policy respectively. It is funded by the Guidance section of the EAGGF and by the FIFG.

5. Objective 5(b)

Objective 5(b) is intended to help with the development of rural areas. Unlike funding available from the guarantee section of the EAGGF (which is aimed at supporting agriculture), the funding made available under Objective 5(b) from the guidance section is intended more for helping to diversify the economy of rural areas away from a dependence solely on agriculture. Measure that will facilitate early retirement, convert or diversify production, build up the rural infrastructure, improve communications and irrigation, encourage tourism, protect and conserve the environment or increase woodlands are all eligible for support.

The Objective 5(b) map includes the English Northern Uplands, rural Wales and the Marches, parts of the Fens, parts of the Peak District, all of Cornwall, parts of Devon and Somerset and much of rural Scotland.

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7 Objective 3 and 4 funding is not applicable in Objective 1 areas

Article 11a of the 1993 Regulation governs the operation of Objective 5(b):

> 1. The rural areas outside Objective 1 regions that may receive Community assistance under Objective 5(b) are those which have a low level of socio-economic development assessed on the basis of GDP per inhabitant and also satisfy at least two of the following three criteria:
> (a) high share of agricultural employment in total employment;
> (b) low level of agricultural income, in particular as expressed in terms of agricultural value added per agricultural work unit (AWU);
> (c) low population density and/or a significant depopulation trend.

Other areas not meeting these criteria can also be covered:

> 2. The Community assistance may also be extended to other rural areas with low levels of socio-economic development that are outside Objective 1 regions if they meet one or more of the following criteria:
> - the peripheral nature of areas or islands in relation to major centres of economic and commercial activity in the Community,
> - the sensitivity of the area to developments in agriculture, especially the framework of the reform of the common agricultural policy, assessed on the basis of the trend in agricultural incomes and the size of the agricultural workforce;
> - the structure of agricultural holdings and the age structure of gainfully employed agricultural labour force,
> - the pressures exerted on the environment and on the countryside,
> - the situation of areas within mountain or less-favoured areas classified pursuant to Article 3 of Directive 75/268/EEC(*),
> - the socio-economic impact on the area, as measured by Objective criteria, of the restructuring of the fisheries sector.

Objective 5(b) is funded by the ERDF, the ESF and the Guidance section of the EAGGF.

6. Objective 6

Objective 6 was agreed in 1995, a year after the other Objectives, and applies only to northern Finland and Sweden. It provides assistance for NUTS level 2 regions with very low population density, defined as being eight inhabitants per km^2 or less and, some adjacent and contiguous smaller areas fulfilling the same population density criterion. Financed by all four Structural Funds, Objective 6 will be used to stimulate new economic activity (and improve the competitiveness of business in the eligible areas) in order to create jobs, to support farmers in coping with the necessary structural adjustments and to maintain acceptable living conditions in remote rural areas.

C. Community Initiatives

In addition to these main Objectives, there are a number of smaller and more focused Community Initiatives that provide more modest levels of funding. These are outlined below.

INTERREG	to assist certain cross-border areas in the Community
LEADER	to promote rural development; targeted at those areas which have Objective 5(b) status.
REGIS	to foster closer integration into the Community of the most remote regions (i.e. the French overseas departments, Madeira, the Azores and the Canary Islands)
RECHAR	to help those areas affected by coalfield closures
KONVER	for areas seriously affected by the contraction of the defence industry
RESIDER	for areas affected by closures in the steel industry
RETEX	to encourage diversification of economic activities in those areas heavily dependent on the textile industry
URBAN	to help find solutions to the serious socio-economic problems experienced by urban areas
SME	to assist small and medium-sized enterprises adjust to the single European market and to compete in international markets
EMPLOYMENT	labour market measures to promote equality and to aid the integration of those on the margins of the labour market, such as the disabled and those from ethnic minorities
ADAPT	to help with training and job creation in areas of industrial and technological change
PESCA	to assist areas dependent on the fishing industry
PEACE	economic and social measures to assist the peace and reconciliation process in Northern Ireland and the border regions of the Republic of Ireland

II Renegotiating the Structural Funds

At the present time the European Commission is engaged in a full review of the way in which the Structural Funds operate. This review has been necessitated by a number of factors:

- The current programming round for the Structural Funds will expire at the end of 1999;
- The current structure for the financing of the whole of the European Union - the Financial Perspective - expires at the end of 1999. Related to this is a commitment for the Commission to re-examine not just the patterns of expenditure within the EU Budget, but also the way in which it is financed.[8]
- The likely enlargement of the EU. The potential entrants to the EU are significantly less affluent than the current Member States, and are therefore more likely to need assistance from the Structural Funds for economic development than some of the existing Member States. It would simply not be possible to

[8] *Financing the European Union: Commission Report in the Operation of the Own Resources System,* European Commission DG XI, 7 October 1998

extend the current system of funding at its present level and intensity to new entrants without significant increases in the size of the EU budget. Indeed, if the programmes currently undertaken by the Structural Funds and the Cohesion Fund were extended without reform to the new Member States then the total costs could more than double.

A. Agenda 2000

The European Commission published a document on 16 July 1997 entitled *Agenda 2000*. This provides the starting point for the review of the Structural Funds and regional policy.

Some of the key proposals in the document are as follows:

- Objective 1 and 2 areas will cover between 35 and 40 per cent of the Union population, against 51 per cent currently (a greater concentration of expenditure).

- To help achieve the greater concentration of expenditure, the Commission proposes a **strict** application of the GDP criterion for Objective 1 by which assistance will only go to regions whose per capita GDP is less than 75 per cent of the Union average.

- For all the regions confronted with major economic and social restructuring needs, the Commission proposes a 'new' Objective 2. This would include areas affected by change in the industrial, service or fisheries sectors, rural areas in serious decline because of a lack of economic diversification, and urban districts in difficulty because of a loss of economic activities. This Objective will take particular account of the unemployment rate, of the level and rate of change of industrial employment and agricultural activity, including changes linked to fisheries, as well as the degree of social exclusion. The 'new' Objective 2 will also incorporate much of the work currently being undertaken through the various Community Initiatives, such as RECHAR (for former coal-mining areas).

- A new horizontal Objective 3 will apply to regions not covered by Objectives 1 and 2 in order to help Member States adapt and modernise their systems of education, training and employment.

- Separate amounts of expenditure have been allocated for the existing fifteen member states (• 218.4 billion in 1999 prices over the period 2000 to 2006) and for potential new members (• 40 billion).[9] Thus the existing member states will

[9] The figures quoted here are taken directly from Article 7 of the draft Resolution. Essentially, they represent the 1997 figures quoted in *Agenda 2000* inflated by 4 per cent to move them to a 1999 price base.

only be affected to the extent that • 40 billion has been "reserved" for new accessions to the EU; the number of countries that actually join should not affect the amounts available.

B. The Draft Regulations

On 18 March 1998 the European Commission published drafts of the Regulations that will govern the operation of EU regional aid for the period 2000 to 2006. There are very few substantial differences between the proposals outlined in *Agenda 2000* and those contained in the draft Regulations. It is proposed that there will be just two regional Objectives, and a third horizontal Objective for areas not covered by the former group. The key features of the proposed schemes for funding are as follows.

1. New Objective 1

Objective 1 will continue to assist the regions whose development is lagging behind the rest of the Community. This will be defined as regions at NUTS level 2 that have a GDP per capita of less than 75 per cent of the EU average, based on an average of the latest three years figures. The Canary Islands (due to their ultra-peripheral status) and the current Objective 6 regions (by virtue of their low population density) will also be covered. Objective 1 areas will be restricted to 20% of the EU population. Objective 1 is likely to take up in the region of two-thirds of Structural Fund expenditure. For areas losing their current Objective 1 status there will be a six-year phasing out of existing funding.[10]

2. New Objective 2

Objective 2 will in essence be a merging of the current Objectives 2 and 5(b), and will also incorporate a number of the existing Community Initiatives. This Objective will provide support for many different areas: those facing industrial decline; rural areas affected by depopulation; deprived urban areas; regions heavily dependent on the fishing industry and those undergoing structural change in the services sector. Support for Objective 2 will cover 18% of the EU population. The draft Regulations indicate that industrial and service sectors should represent 10%, rural areas 5%, urban areas 2% and those dependent on fishing 1% (these thresholds apply to the EU as a whole, not necessarily to each Member State).

For areas losing their current Objective 2 or 5(b) status there will be a four-year phasing out of existing funding. Under a concession, reportedly negotiated by Commissioner

[10] For areas that qualify for funding under the new Objective 2, this will be a seven-year phase-out.

Kinnock, there will be a safety net whereby no Member State will see a reduction in the coverage of current Objective 2 and 5(b) areas of more than a third.

It is for the Member states to make the case for exactly which areas should be proposed for assistance under the new Objective 2, subject to the overall population restrictions shown above. The draft Regulations emphasise that the Commission and the Member States between them have to ensure that assistance is genuinely concentrated on the areas most seriously affected and at the most appropriate geographical level.

3. New Objective 3

The activities of the European Social Fund currently undertaken by Objectives 3 and 4 are to be re-grouped under the new Objective 3, which will remain a horizontal Objective applicable to those areas not covered by Objectives 1 or 2. There are five areas of activity proposed: active labour market policies to fight unemployment; promoting social **in**clusion; lifelong education and training; facilitating economic and social change; and improving the participation of women in the labour market.

4. Community Initiatives

The Community Initiatives are being severely rationalised, from the existing thirteen to just three:

- trans-national, cross-border co-operation, to stimulate balanced regional economic development;
- rural development;
- a new initiative on trans-national co-operation to fight discrimination and inequality preventing access to employment.

5. The Operation of the Structural Funds

In addition to the proposed schemes of regional aid, the draft Regulations include proposals for changing the way in which funding is administered. Some of the key principles underlying these changes are partnership, clarification of responsibilities, better monitoring, transparent implementation and improved financial management. These are outlined below.

The use of partnership in the administration of Structural Funds programmes is no longer just encouraged, but will have to be guaranteed by the Member States. Regional and local authorities, environmental authorities, economic and social partners (including non-governmental organisations) will all be involved in the future. The Commission believes that broadening the degree of partnership must go hand-in-hand with decentralisation away from the Commission.

With the involvement of more parties, it is essential that responsibilities are clearly stated. The Commission wants the responsibilities of all partners to be clearly defined at all stages of the operation of the Structural Funds. To this end, the Commission will be publishing a summary of guidelines to be used by each Member State. The Commission will retain responsibility for defining the strategic targets of Structural Funds operations, the financial allocations and the rules governing the operation of the Funds. Member States will have responsibility for allocating funding to different operational measures, designating the final beneficiaries and defining the criteria for the selection of individual projects. Each Member State will appoint a managing authority that will take on these roles. The managing authority will have a wide degree of autonomy: it will prepare programming documents for forwarding to the Commission; it will have to guarantee compliance with Community policies and ensure the quality of the implementation.

The monitoring of programmes will continue to be the responsibility of a Monitoring Committee, chaired by the managing authority. To ensure the widest degree of partnership, all types of partners will have to be represented on the Committee. A distinction will be made between those participating directly in the financing of programmes and those who have a purely advisory role. In the future, it is proposed that Commission representatives will only participate in an advisory capacity, so as not to conflict with the principle of decentralisation.

While the new proposals for the administration of the Structural Funds involve a greater degree of decentralisation than has previously been the case, such decentralisation must not conflict with the Commission's responsibility for the execution of the Budget. To ensure that this takes place a number of provisions have been included in the draft Regulations:

- An annual implementation report will be produced, containing information on the progress of the programmes and the impact of funding on the Member States.

- A greater emphasis on data collection and evaluation. This will allow the Commission and the managing authorities to ensure that the programmes are being properly implemented, and will also permit the examination of areas of particular interest to the EU, such as equality between men and women.

- Annual monitoring meetings between the Commission and the managing authority in each Member State, to examine results of the previous year and make recommendations (where necessary) for improving management.

- A detailed mid-term evaluation of all programmes, required because of the length of the programming period (seven years) and to consider the allocation of the performance reserve (see below).

No one would doubt that the financing of Structural Funds operations is exceedingly complex at the present time. Decision-making procedures are protracted, often leading to delays in payment. Many of the other changes contained in the draft Regulations will help in the simplification of the administration: the reduction in the number of programmes, better clarification of responsibilities and so forth. The Commission's proposals for the reform of financial management propose a simpler and more automatic system for budget commitments. The first annual commitment will be made at the time the assistance package is approved. This should reduce the delay between approval and the initial receipt of any funding. Subsequent commitments will automatically be triggered at the beginning of each year. Coupled with this, however, the Commission is also proposing to an automatic decommitment of those funds not used after the end of the second year following the commitment year. There is also the possibility that funds clawed back in this way could be re-budgetised.

6. The Performance Reserve

One of the more innovative proposals contained within the draft Regulations is the establishment of a 'performance reserve'. Under this proposal, some ten per cent of the total Structural Funds budget will be withheld at the beginning of the programming period, to be allocated after a mid-term evaluation. It is proposed that the reserve will be awarded to operational programmes that are judged to be performing "well or very well" on the basis of their score against a range of measurable indicators assessed mid-term in comparison to targets defined at the outset. These indicators will be designed to ensure that assistance achieves the expected results (quality programming), that correct monitoring, financial management and project selection have been applied, that funds are spent at the correct rate and that an effort has been made to lever in private capital.

Whilst the performance reserve offers a carrot to those projects performing particularly well, it is also proposed to apply a stick to those projects not performing properly. The mid-term evaluation will also be used to verify that the principle of additionality is being applied correctly. The draft Regulations state that:[11]

> "Programmes in Member States where undertakings with regard to additionality have not been respected will experience a reduction in favour of other programmes."

7. Transitional Support

The draft Regulations contain provisions for those regions losing their existing eligibility for assistance to receive transitional support. For existing Objective 1 regions, the

[11] COM(98) 131 Final, page 27

transitional period is proposed to be six years (but seven years for those regions that qualify for funding under new Objective 2). For existing Objective 2 and 5(b) areas, the transitional period will be four years.

Because the reduction in population coverage of the new Objective 2 in comparison to the existing Objectives 2 and 5(b) is significant, a "safety net" is also proposed. This is intended to ensure that the reduction in population coverage is shared between the Member States. The draft Regulations therefore place a restriction on the extent of the reduction in each Member State to being no more than one third of the current population covered under Objectives 2 and 5(b). This could be of considerable benefit to the United Kingdom, which, if the proposals were to be adopted in their current form, could well lose eligibility for several regions.

8. State Aids

The Commission has also proposed that in the interests of efficient programming there should be a 'consistency' between Objective 1 and 2 areas for the purposes of the European Structural Funds and the areas covered by Member States' own programmes of regional assistance to industry (referred to as 'state aids').

9. Timetable of Negotiations

Negotiations on the financing of the Structural Funds and on the eligibility criteria are likely to continue into the early part of next year. Once the main Structural Fund and Cohesion Fund Regulations have been agreed by the Council of Ministers, they will be submitted to the European Parliament for approval. (This is an example of the increased powers conferred on the Parliament following the ratification of the Amsterdam Treaty.) The other Regulations (one for each of the Structural Funds) are subject to different procedures, but will follow a similar timetable. The Regulations will need to be adopted in early to mid-1999 to allow time for eligible areas to be identified and regional plans devised if the new programmes are to commence on time.

III Issues for Discussion

The proposals for the reform of the Structural Funds have aroused much discussion in the United Kingdom. The following section looks at some of the issues raised.

A. Fairness between Member States

Fairness is one of the key priorities to the UK Government's negotiating position on the reform of the Structural Funds: [12]

> It will be a Government priority to secure reform which delivers a system that is affordable, efficient, durable and fair.

Fairness can, of course, be interpreted in different ways. The Deputy Prime Minister, John Prescott, expanded on the Government's approach in an address to the European Committee of the Regions in May 1998:[13]

> The overall system of eligibility and allocations should have a truly redistributive effect so that:
>
> - A poorer Member State should receive more per capita than a richer Member State;
> - No Member State should receive more than at present; and
> - Regions which continue to be eligible for assistance under a particular Objective should not see an increase in per capita receipts while others face cuts.

Others have interpreted fairness in rather different ways. One (perhaps rather Eurosceptic) version says that the UK is a net contributor to the EU budget, and the UK should therefore continue to receive substantial sums back from the EU if continued membership is to be justified.[14] This view was echoed in the comments of Lord Pearson of Rannoch earlier this year: [15]

> My Lords, is the Minister aware that the United Kingdom pays about £11,000 million annually to the European Union under this sort of heading? Of that, the EU is graciously pleased to give us back about £7 billion. Would it not be more sensible for us to take control of the whole of the £11,000 million and spend it wisely on our real needs, no doubt saving several billion pounds along the way?

The issue of the equitable distribution of contributions to the EU budget more generally was discussed in the Library's Research Paper *EC Finance* last year.[16]

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[12] HC Deb 16 July 1997 c228W

[13] DETR Press Notice 98/369, *European funding must be fair - Prescott*, 13 May 1998

[14] Figures from the 1996 *EU Court of Auditors Report* show that the UK was the third biggest net contributor in absolute terms and the sixth largest in per capita terms.

[15] HL Deb 22 April 1998 c1154

[16] Library Research Paper 97/137

Another - very different - view of fairness says that if the EU is to welcome less wealthy central and east European countries as new members within the next few years, then there must be sufficient funds. Given that growth in the overall size of EU budget is constrained, and the UK Government supports the principle of enlargement, then it is inevitable that relatively wealthy Member States such as the UK, France and Germany should expect to lose some of their Structural Fund allocations.

B. Concentration and Coverage

Concentration is perhaps the overarching principle driving the reforms of the Structural Funds:

- concentration of the number of priority Objectives (a reduction from seven to three) and of the number of Community Initiatives (from thirteen to three);
- concentration on areas of priority assistance: EU-wide priorities as defined by the Commission;
- geographical concentration (a reduction in the population eligible for Objectives 1 and 2 from the current 51 per cent to 35 per cent); and
- financial concentration, allocating around two-thirds of the funds to Objective 1 programmes.

It is the third of these points - geographical concentration - that has aroused the most debate. Over the last six years the Structural Funds have been spread quite widely, covering half of the total EU population. There have clearly been substantial benefits over this period, measured in terms of jobs created or safeguarded, infrastructure developments and environmental improvements. There is little explicit justification of the principle of geographical concentration from the Commission: if relative disadvantage is widely spread, then there is no obvious reason not to spread the resources appropriately.

The Lords Select Committee was more supportive of the Commission's proposal for geographical concentration than the Trade & Industry Committee. The Trade & Industry Committee recommended that the Government should explore the idea of concentrating Objective 1 funding on the poorest 20 per cent of regions, rather than relying on statistical distance from a norm (the 75 per cent of EU GDP per capita criterion).[17] The Committee also made the suggestion of establishing an EU-wide target for reductions in Structural Fund population coverage within each Member State. This could have the advantage of being perceived as a visibly fair method of achieving a reduction in population coverage

[17] Trade & Industry Committee, Report, page xiv

(and indeed a similar approach has already been proposed for reducing the areas covered by Objective 2).

C. Eligibility Criteria

1. Objective 1: General Principles

Given that it will account for around two-thirds[18] of total Structural Fund expenditure (almost • 150 billion over the period 2000 to 2006 as a whole), it is inevitable that eligibility for Objective 1 has attracted a lot of comment. This is perhaps compounded by the simplicity of using a single criterion: only regions with a GDP per capita of less than 75 per cent of the EU average will be eligible.

The UK Government advocates that there should be a certain degree of flexibility around the 75 per cent threshold. This approach was used for the current programming round (1994 to 1999). A small number of areas are currently eligible for Objective 1 despite not having strictly met the criteria:

- parts of northern France were included, despite not being NUTS 2 regions in their own right;
- Abruzzi in Italy was eligible for half the programming period;
- Western Moray, Arran and the Cumbraes in Scotland were added to the strict definition of the Highlands and Islands NUTS 2 region.

While many would wish to avoid a prolonged period of political horse-trading over the inclusion or exclusion of certain areas, the Government is strongly in favour of there being some flexibility. This view has two main strands. The first concerns the reliance that would be placed on the accuracy of statistics. The Trade & Industry Committee itself expressed the same view in the conclusions of its enquiry:[19]

> The intellectual argument for an inflexible threshold for Objective 1 status cannot withstand the reality of the fragility of statistical listing, based on an inevitably imperfect methodology, as the sole means of determining eligibility. We recommend that the Government pursue with vigour the question of maintenance of a degree of flexibility over the threshold for Objective 1 eligibility, taking account of the proposal we have made for a "grey zone" giving potential but not absolute eligibility to a handful of regions.

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[18] COM (98) 131; *Draft Regulation laying down general provisions on the Structural Funds*, Article 7

[19] Trade & Industry Committee, Report, page xviii

The second strand relates to the relatively balanced distribution of wealth within the United Kingdom, as measured by GDP per capita. In the United Kingdom the poorest regions have a GDP per capita in the range of 75 - 80 per cent of the EU average. In Germany and Italy there is a much wider variation. (As an example, the former East German Länder have a GDP per capita of between 55 and 60 per cent of the EU average, whilst Hamburg is almost double the EU average.) The argument runs that the United Kingdom, with a GDP per capita on a national basis ranking in the bottom half of Member States, but for one reason or another has less regional variation in GDP per capita, should not be penalised by the application of a strict threshold.

There is a considerable degree of support for this approach; in evidence to the Trade & Industry Committee the Convention of Scottish Local Authorities (CoSLA), the Local Government Association, the Alliance for Regional Aid and the House of Commons Backbench Structural Funds Group all echoed these comments. The dissenting voice in this instance is the Lords Select Committee, which stated in its report:[20]

> For Objective 1, the 75 per cent of GDP criterion which the Commission proposes is tough but just. We recognise that the concentration of assistance is desirable. Tinkering with the margins of any cut-off will undermine this aim. We conclude that the 75 per cent of GDP criterion for Objective 1 eligibility should be strictly enforced.

The European Commission would appear to be quite adamant that there should be no flexibility over the 75 per cent criterion. Lord Barnett, the Chairman of the Lords Select Committee, had the following exchange with Marc Vanheukelen, a Member of the Cabinet to Monika Wulf-Mathies (the Commissioner for Regional Policy):[21]

> 254. But no flexibility? In other words, Northern Ireland has about 77 per cent.
> A. Too bad.
> 255. If it was 75.1?
> A. It would also be too bad.
> 256. No flexibility at all?
> A. No.

2. Eligibility of UK Regions for Objective 1

The possible eligibility of regions in the United Kingdom for Objective 1 funding is complicated by the fact that its map of NUTS regions has been revised this summer. The need for this revision has arisen for two main reasons. Firstly, the reorganisation of local government has meant that throughout Wales and Scotland (from April 1996), and in parts of England (between April 1996 and April 1998), unitary authorities are replacing

[20] Lords Select Committee, Report, page 23
[21] Lords Select Committee, Evidence, page 72

the two-tiered structure of counties/Scottish regions and districts. This affects NUTS level 3 and 4 regions. Secondly, the adoption of Government Offices for the Regions as the standard unit for presentation of statistical data for regions was implemented in April 1997, replacing standard statistical regions. This affects NUTS level 1. There has also been a desire to break up very large regions into smaller ones. The points below, taken from the press release issued by the Office for National Statistics (ONS), summarise the more significant changes:[22]

- The separation of Cornwall and Devon into two separate areas, recognising the very different economic conditions of the two counties, and Cornwall's sparsity of population, geographical peripherality and distinct cultural and historic factors reflecting a Celtic background.

- The separation of London into Inner and Outer London, recognising the differences between the inner city and the outer fringe, as well as the fact that London was one of the largest NUTS level 2 areas in the whole of the European Union.

- The two-way split of Wales to be on an east/west basis, rather than the current north/south structure. This reflects the evolving differences between the east and the less accessible western and Valleys areas.

- Changes to boundaries in Scotland to recognise the area represented by Highlands and Islands Enterprise (HIE). This enables the structure to more closely reflect the uses to which NUTS-based statistics are put. The HIE area is defined by Act of Parliament and is currently recognised for economic development purposes by the EU and the UK.

New data for GDP per capita were published by ONS on 22 October 1998, using the new NUTS structure for the first time. Table 2 (overleaf) shows the GDP per capita of NUTS regions in the United Kingdom indexed to UK = 100. Figures for each year 1993 to 1996 are shown; an average for the three-year period 1994 to 1996 has also been calculated. Since the GDP per capita in the UK is very close to the EU average, these figures provide a useful guide to the likely eligibility of regions for Objective 1 funding. For example, in 1996 GDP per capita in the UK was 98 per cent of the EU average. It should be emphasised, however, that these figures will **not** form the basis of any official decisions regarding eligibility. Such decisions will be made on the basis of Eurostat data, which will be based on these figures (but converted to a common currency basis and subject to other minor adjustments). These are expected to be published in December.

[22] ONS News Release (98) 199 dated 29 July 1998

The Office for National Statistics is due to publish a press release containing figures for GDP per capita for the new NUTS 2 regions for the years 1993 to 1996 on Thursday 22 October. These will provide a more reliable guide to the likely eligibility of regions within the United Kingdom. The figures will, however, be indexed to UK =100 and not EU15 = 100. To convert from the UK base to the EU base in approximate terms, it will be necessary to reduce the figures by two percentage points. (GDP per capita in the United Kingdom as a whole is around 98 per cent of the European average.) For example, an area with a GDP per capita of 98 per cent of the UK average would approximate to 96 per cent of the EU average.[23]

Looking at existing data for GDP per capita, it seems likely that Merseyside will retain its Objective 1 status, and South Yorkshire and Cornwall will gain it. South Yorkshire was already a NUTS 2 region before the review, but its GDP per capita has fallen in recent years, not least because of the effects of closures in the coal-mining industry. Cornwall has always had a low GDP per capita in comparison to other counties in the UK. Until now, it formed part of the larger NUTS 2 region of Devon and Cornwall (Devon's much higher GDP per capita meant that the average for the two counties was above the 75% threshold). Treating Cornwall as a NUTS 2 region in its own right makes it highly likely that it will qualify for objective 1 funding.

3. The Highlands and Islands of Scotland

In the Commission's draft Regulations it is proposed that the current Objective 6 areas in northern Sweden and Finland should receive Objective 1 funding because of their sparse populations, **even though they exceed the 75 per cent of EU GDP per capita rule**:

> The most remote regions (the French overseas departments, the Azores, the Canary Islands and Madeira) and the areas eligible under Objective 6 for the period 1995-99 shall also be covered by this Objective.[24]

The Government's view is that the Highlands & Islands of Scotland should be treated on a par with northern Finland and Sweden, and be eligible for Objective 1 funding on the basis of population sparsity despite having a GDP per capita above the 75 per cent threshold. In giving evidence to the Scottish Affairs Committee, the Minister, Calum MacDonald MP said:[25]

> We are arguing very strongly and at the highest levels that that criterion of sparsity logically should include an area like the Highlands and Islands as well because we believe that Northern Finland, Northern Sweden, the Highlands and Islands can be grouped quite

[23] In precise terms it is necessary to multiply the figures on the UK base by 0.98

[24] 7609/98 COM (98) 131 Final: *Reform of the Structural Funds: Proposals for Council Regulations 2000 - 2006*; Article 3

> closely together in terms of their remoteness and in terms of the population spread. They form a distinct grouping as opposed to the next regional group you would take in along these criteria which would be very far distanced from these other three. We are arguing that population sparsity should now be explicitly acknowledged by the Commission and logically that that should require the inclusion of Highlands and Islands within the proposed new Objective 1.

Both the Trade & Industry Committee and the Lords Select Committee were in favour of the Highland and Islands retaining their Objective 1 status on the basis of their sparse population. The Special Adviser to the Trade & Industry Committee, Professor Iain Begg of South Bank University, pointed out that no region of Sweden currently has a GDP per capita of less than 92 per cent of the European average, but it will qualify on the basis of the sparsity of its population. He also emphasised that the Highlands of Scotland have a lower GDP per capita when analysed separately from the Islands (the Shetlands in particular boost the GDP of the region because of oil activities). The Convention of Scottish Local Authorities also argued in favour of the Highlands and Islands retaining Objective 1 status on the basis of the sparsity of its population.

The Highlands and Islands of Scotland European Partnership explained the situation regarding sparsity of population in its examination of the case for continued Objective 1 status:[26]

> Until the accession of Finland and Sweden to the European union, the Highlands and Islands was the most sparsely populated region of Europe. Its population density of 9 persons per square kilometre is significantly lower than the next most sparsely populated areas, Alentejo in Portugal (20 persons per square kilometre), and the Spanish regions of Castilla la Mancha (21 people per square kilometre), and Castilla y Leon (27 people per square kilometre). Sparsity of population also varies within the NUTS II region, as presently constituted, such that in the NUTS III areas of Lochaber and in Skye and Lochalsh there are only 4 persons per square kilometre. Indeed, if the main settlement of Inverness - four times larger than the next largest settlement - is excluded, the population density falls to 8 persons per square kilometre, the threshold for Objective 6.

4. Northern Ireland

The difficulty that Northern Ireland faces is that Objective 1 status for the 1994 to 1999 programming round was conferred for by virtue of the special political circumstances faced by the Province, rather than on a strict application of the 75 per cent of GDP per capita criterion.

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[25] Scottish Affairs Committee, Evidence, 29 April 1998, HC 714 1997-98, Q12

[26] Highlands and Islands of Scotland European Partnership, *The case for EU Structural Funds support after 1999* (DEP 98/160)

The draft Regulations published by the Commission emphasise that the 75 per cent of EU GDP per capita criterion will be applied **strictly**, implying that the exceptions allowed for the current programming period will no longer be permitted. Latest figures from Eurostat show the GDP per capita of Northern Ireland to be 78% of the EU average in 1995, or 79% of the EU average over the period 1993 to 1995. In a parliamentary answer earlier this year, the Northern Ireland Minister, Paul Murphy MP, emphasised the importance of substantial and continuing assistance from the Structural Funds for Northern Ireland:[27]

> **Mr. Ben Chapman:** To ask the Secretary of State for Northern Ireland what assessment she has made of the future European Structural Funds regime for Northern Ireland.
>
> **Mr. Paul Murphy:** Under the proposed post-1999 reforms, qualifying for Objective 1 status will be more difficult because Northern Ireland's GDP will exceed the 75 per cent. maximum proposed by the Commission. Northern Ireland's Objective 1 status has been vital over the past years and there is a continuing need for substantial EU support after 1999, commensurate with the region's special circumstances, to help in adapting the region's economy to peace.

Mrs Roche (the Minister for Regional Policy) reiterated this when giving evidence to the Trade & Industry Select Committee. She said:[28]

> As far as Northern Ireland is concerned, that is where our concerns are, about the rigidity of using 75 per cent, because, certainly on the latest Eurostat figures, Northern Ireland would not fall into that. As far as that is concerned, we do talk very much about the special political circumstances in Northern Ireland. What I have to say to you on that, Mr Cunningham, and to the Committee as well, is, I have taken the opportunity, in the last few months, of not only speaking about this issue to the Commission and the Commissioners but also to the other Member States, and, I have to say, there is certainly an understanding of the special situation there, the efforts the Government are making at this present time, and we will be continuing to press this case very strongly indeed.

Both the Trade & Industry Committee and the Lords Select Committee were strongly in favour of retaining Objective 1 status for Northern Ireland. If the 75 per cent criterion is to be applied without exception then the best hopes for Northern Ireland would perhaps lie in (a) ensuring that it receives a generous allocation of transitional assistance as a former Objective 1 region (b) that it lobbies for Objective 2 status on the basis of having a number of industries (such as shipbuilding) that are affected by decline and (c) that it lobbies for retention of the PEACE Initiative.

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27 HC Deb 5 March 1998 c726W

28 Trade & Industry Committee, Evidence, page 30

D. Objective 2

The United Kingdom could well see a significant decline in the areas covered by the new Objective 2, in comparison the present Objectives 2 and 5(b). For this reason the safety net, limiting reductions in coverage to a third of the current eligible population, will be important to the United Kingdom.

The Commission's emphasis on unemployment as a key criteria in assessing the eligibility of regions for funding under the new Objective 2 is to be expected, particularly in the context of recent statements from European summits that refer to unemployment as a major social problem facing Europe. The United Kingdom has supported these statements wholeheartedly; this merely reflects the importance that the current Government attaches to unemployment and social exclusion more generally.

From the UK perspective, the concerns over the reliance on unemployment as a key criterion are two-fold. First, using a three-year assessment of unemployment takes no account of the differing economic cycles prevailing in each Member State. Taking a longer term view - over the whole economic cycle - would allow an accurate assessment of **structural** unemployment as opposed to that which is merely **cyclical**. (This would also help the UK's claim for Objective 2 assistance, since unemployment in the UK is relatively low in comparison to other Member States.)

The other argument concerns the definition of unemployment used. The United Kingdom's claimant count measure of unemployment has been widely discredited in recent years, and does not have any directly comparable measure in other Member States. The lack of comparability with other Member States means that the European Commission would not use the claimant count definition for assessing eligibility anyway. Instead, the International Labour Organisation (ILO) definition of unemployment would be utilised. This definition is not based on individuals' eligibility for social security benefits, and is internationally comparable (all Member States have had to use this definition in their annual Labour Force Surveys for many years).

The Alliance for Regional Aid is concerned over the use of the ILO definition of unemployment, claiming in its evidence to the Lords Committee that whilst on the surface it purports not to be dependent on eligibility for social security benefits, it does in fact remain so.[29] It refers to research undertaken by the Institute of Employment Research at Warwick University, which has shown that the degree of "hidden" unemployment (defined as those people who have transferred to sickness benefits and are therefore no longer actively seeking work) is much higher in the United Kingdom - and particularly in the in older industrial areas - than in other Member States. The Alliance advocates the use of GDP per capita as a better indicator than unemployment. It also suggests using

[29] Lords Select Committee, Evidence, page 48

areas smaller than NUTS level 3 regions as proposed by the Commission, so as to maximise the opportunity of targeting funds to the most needy areas.

There have been suggestions from many quarters that the eligibility for Objective 2 should be based on a wider range of criteria. There is certainly a strong view in the United Kingdom, shared by other Member States, that there should be a substantial degree of latitude given to Member States in determining the areas eligible for Objective 2.

The argument advocated by bodies as diverse as the Alliance for Regional Aid and the Confederation for British Industry (CBI) is that since the scope of Objective 2 is now wider than it was previously, a wide range of indicators should be used in assessing eligibility. Both of these organisations have proposed the use of GDP per capita as a better indicator of competitiveness in local areas than unemployment alone. Other indicators, measuring social deprivation, dereliction, variations in productivity and changes in employment were also suggested by the CBI. It in its written evidence to the Lords Select Committee the CBI said that if unemployment is to be used, then long-term unemployment should be examined closely, since this was a better indicator of the underlying problems of local areas.[30]

There is a strong consensus within the United Kingdom for using GDP per capita as an indicator for assessing the eligibility of regions for Objective 2 status. Both the Committees were in favour of this; the Government has made a commitment that it will lobby for this criterion to be adopted. In its written submission to the Trade & Industry Committee the DTI said that:[31]

> …GDP is a fairer criterion between Member States than unemployment. Below the national criterion, subsidiarity should apply; it should be for Member States to use their own more sophisticated national and regional criteria to target the Funds.

This view would appear not to be shared by all the Member States though. In evidence to the Lords Select Committee, Dr Wilhelm Schönfelder, the Director General for European Affairs in the Federal Foreign Office of the Republic of Germany, said:[32]

> We think that EU assistance should be based on regional, not national prosperity. National prosperity is already taken into account in calculating the contributions which the EU Member States make to the budget - the so-called fourth resource of income of the European Union.

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30 Lords Select Committee, Evidence, page 99
31 Trade & Industry Committee, Evidence, page 27
32 Lords Select Committee, Evidence, page 89

E. The Community Initiatives

1. The PEACE Initiative

The Community Initiative PEACE was agreed in 1995, a little after the other Initiatives were established. It is aimed at reinforcing the peace and reconciliation process in Northern Ireland and the six border counties of the Irish Republic. The main objectives of the Initiative are:

- actions for employment and improved quality and accessibility in training, education and recruitment;
- urban and rural regeneration;
- cross-border development, through setting up business and cultural links, the improvement of infrastructure and co-operation between public bodies;
- social inclusion, particularly of women, children, young people and vulnerable social groups, moves to combat exclusion and actions to encourage reconciliation;
- productive investment and industrial development;
- in Northern Ireland, a special sub-programme aimed at encouraging the creation of local partnerships, which will have an important role to play in the programme's realisation.

On the face of it, the draft Regulations would seem to suggest that Northern Ireland would not be eligible for objective 1 funding after 1999 because of the strict application of the GDP per capita threshold. Furthermore, the rationalisation of Community Initiatives from the existing thirteen to just three would indicate that the PEACE Initiative is unlikely to continue in its present form after 1999. Following the assurances given by the Minister Paul Murphy MP in March 1998 (see page 27), Mrs Roche said in answer to a parliamentary question:[33]

> The special circumstances of Northern Ireland and the ongoing political developments there should be recognised. Northern Ireland should certainly receive treatment at least as good as the richer Republic of Ireland.

The Trade & Industry Committee concluded in its Report:[34]

[33] HC Deb 21 May 1998 c541W
[34] Trade & Industry Committee, Report, page xix

> It would be a blow to the European cohesion policy if, of all the EU's regions, the plug were to be pulled on Northern Ireland.

The Lords Select Committee included a similarly robust conclusion in relation to the case for Northern Ireland:[35]

> Cutting the Peace and Reconciliation programme at this critical stage of the Peace Process could be little short of disastrous. Whenever the Structural Funds package is finally agreed, the Peace and Reconciliation programme should be part of it.

2. The URBAN Initiative

The draft Regulations make no room for the continuation of the URBAN Initiative (the proposed new Objective 2 will, however, embrace urban areas explicitly). While some have criticised the Community Initiatives as being time-consuming to administer in relation to the funding available,[36] others have advocated the continuance of certain Initiatives. The Local Government Association in particular has voiced support for the URBAN Initiative. In its evidence to the Trade & Industry Committee, it said:[37]

> The LGA wish to see the continuance of the URBAN Community Initiative. URBAN has been extremely important in generating local involvement in economic development activity and in combating social exclusion. CIs have been valuable in promoting innovation and experimentation. In areas such as Kilburn in Greater London, Brighton and Hove in West Sussex, or Netherton in Merseyside, URBAN has led to the creation of strong links between agencies and local residents to enhance employment and economic opportunities.

3. A New "RESTRUCT" Initiative

The European Regions of Industrial Technology (RETI) group has proposed that there should be another Community Initiative, in addition to those advocated by the Commission, to help industrial areas in difficulty. This would in essence take forward the work undertaken by the existing Initiatives RECHAR (coal), RESIDER (steel), RETEX (textiles) and KONVER (defence). This proposal is supported by the Alliance for Regional Aid, which stated in its evidence to the Trade & Industry Committee that:[38]

> RESTRUCT is designed to meet the needs of regions suffering from significant plant closures and undergoing industrial restructuring in car manufacturing, the

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35 Lords Select Committee, Report, page 28

36 See, for instance, the evidence submitted to the Lords Select Committee by the Northern Ireland Department for Economic Development and comments from the Scottish Office referred to in the Trade & Industry Committee's report.

37 Trade & Industry Committee, Evidence, page 11

38 Trade & Industry Committee, Evidence, page 49

> coal, steel and textile industries, and other industrial sectors during the 2000-06 time frame. It would provide an extra layer of aid, in addition to Objectives 1 and 2. The Initiative would be designed to be fast, flexible and responsive so that it can be targeted at areas where there are large unexpected job losses or the need for major industrial restructuring. Importantly, it would be available to areas regardless of their eligibility for Objective 1 or Objective 2 status.

F. State Aids

The Commission's proposal for a 'consistency' between areas covered by Objectives 1 and 2 and Member States' own programmes of regional assistance has met with a considerable degree of resistance within the United Kingdom.

The DTI's consultation paper on reviewing the Assisted Areas map states that "the proportion of Great Britain's working population covered by the Assisted Areas, currently some 34%, must be significantly reduced, perhaps by as much as a quarter."[39] Depending on the outcome of the negotiations, this could prove to be a rather lower threshold than that applying to the areas eligible under the Structural Funds (the limit being 35 per cent of the total - not working - population). It would therefore seem difficult to for there to be a precise overlap between the two. In the United Kingdom, there are many areas eligible for assistance under the Structural Funds but not designated as Assisted Areas for the purposes of the UK's own system of regional assistance. Likewise, there are other parts of the country designated as Assisted Areas but which are not eligible for Structural Fund assistance.

The Government is "strongly against" the Assisted Areas map and the areas eligible for Structural Funds assistance being made coterminous. Barbara Roche MP, giving evidence to the Trade & Industry Committee on behalf of the DTI, acknowledged that there was likely to be a degree of coherence between the two, and that there may even be a relationship between them. She described the Commission's proposals as effectively merging the two maps, which "made no sense at all".[40] The Trade & Industry Committee itself stated:[41]

> The objectives of the two policies are different. There may be very good reasons to concentrate Regional Selective Assistance in areas which do not, and should not, qualify for EU Structural Funds, and vice versa.

The Committee concluded that harmonisation of state aid and Structural Fund maps was "wholly unnecessary". Much the same view was echoed by the Lords Select Committee, which said that there was "no justification" for the proposal. The Convention of Scottish

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[39] *Review of the Assisted Areas Map of Great Britain*, Consultation Paper, DTI (DEP 98/869)
[40] Trade & Industry Committee, Evidence, page 38
[41] Trade & Industry Committee, Report, page xvii

Local Authorities and the Welsh Development Agency have both supported this viewpoint.

IV The Cohesion Fund

A. Background

One of the themes running through many European Union policies is that of promoting and strengthening economic and social cohesion. It has set itself the objective of gradually removing the differences in living standards between the Member States as well as between the regions. The Single European Act of 1987 first introduced economic and social cohesion as a key policy in its own right. The Maastricht Treaty of 1993 created an explicit link between economic and social cohesion and the establishment of Economic and Monetary Union.

The prerequisite for the introduction of the single European currency (the Euro) is a high degree of convergence in both the economic performance of the participating Member States and in the economic policies pursued by the Member States. For the poorer Member States, the adjustments required to bring their economies up to the same level of the more affluent countries are significant.

This poses a conflict of objectives for the Member States concerned. On the one hand, they need to invest heavily to increase their capacity for growth and prosperity. This implies a considerable increase in expenditure on investment: for instance in the development of new productive capacity and the improvement and expansion of infrastructures. On the other hand, Member States joining the single currency are required to reduce their budget deficits and keep public debt under control; this implies a very tight control of public expenditure rather than an expansion.

The solution to this dilemma was provided in the Maastricht Treaty by the establishment of the Cohesion Fund, by which financial assistance could be channelled to the least prosperous Member States. The Fund was established by a Regulation, which became effective in May 1994.[42] The eligibility threshold was defined in the Regulation as those Member States who had a Gross National Product per capita of below 90 per cent of the European average **and** who were willing to follow economic strategies leading towards convergence. The four beneficiaries of the Cohesion Fund are Greece, Ireland, Spain and Portugal. The table below shows the financial allocations for each country over the programming period:

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[42] Council Regulation (EEC) No 1164/94 provided for the formal establishment of the Cohesion Fund. This superseded a temporary measure to establish a cohesion instrument, Regulation (EEC) No 792/93.

Table 3

Cohesion Fund Allocations, 1994 - 1999
million ECU, 1998 prices

Greece	2,737
Spain	8,443
Ireland	1,294
Portugal	2,737
Total	15,211

Source: Trade & Industry Select Committee Report, HC 697 1997/98

Within these totals, the annual allocations are structured in such a way as to ensure that the amounts received by each Member State each year increase by the rate of inflation, so that the value of assistance is maintained in real terms. Up to 80 per cent of the cost of each project can be funded by the Cohesion Fund.

Cohesion Fund support is conditional upon Member States not running excessive deficits; if the Member State does run an excessive deficit, then no new projects are approved until the deficit has been brought back under control. Projects must comply with EU legislation, in particular the rules relating to competition policy, environmental protection and public procurement. All projects are subject to regular monitoring by the Member States and by the European Commission.

Two main types of project are funded by the Cohesion Fund: environmental projects and transport infrastructure projects, on an approximate fifty-fifty split. Environmental projects must help to achieve the objectives of the EU's environmental policy:

- Preserving, protecting and improving the quality of the environment;
- Protecting human health;
- Assuring prudent and rational use of natural resources.

The Cohesion Fund gives priority to schemes concerned with water supply and waste water treatment; however, other schemes such as reafforestation and erosion control are also eligible.

Transport infrastructure projects must help to establish or improve infrastructure within the Trans-European Network (TEN) or else to provide access to the TEN.

B. Proposals for reform of the Cohesion Fund

A draft Regulation proposing changes to the operation of the Cohesion Fund was also published on 17 March 1998 along with those covering the Structural Funds.[43] This contains a number of proposals for the beneficiaries of the Cohesion Fund:

- For those Member States participating in the single currency, there is a requirement for them to continue to meet the convergence criteria as one of the conditions of eligibility for the Cohesion Fund;
- A series of enhanced financial management provisions, together with a greater use of private sector matching funds;
- An application of the 'polluter pays' principle;
- Greater responsibility for financial management will now be placed on the Member States.

The Commission proposes that, regardless of whether the existing beneficiaries join the third stage of EMU, they should continue to be eligible for the Cohesion Fund, for as long as their GNP per capita remains below the 90 per cent threshold. This would suggest that Spain, Portugal and Greece would remain eligible for assistance for the foreseeable future, but places a serious question-mark over Ireland (on the basis that its GNP per capita would soon exceed the threshold).[44]

C. Issues and Arguments

The key issue in considering the future of the Cohesion Fund is whether Member States should continue to benefit once they have joined the single currency. The unequivocal aim of the Cohesion Fund is to promote economic convergence. Some countries - Germany, the UK and Sweden in particular but with a considerable degree of sympathy from other non-Cohesion Fund recipients - advocate the view that assistance from the Cohesion Fund should end when a Member State joins the single currency. In evidence to the Lords Select Committee, Dr Wilhelm Schönfelder said:[45]

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43 COM(98)130: Proposal for a Council Regulation amending Regulation (EC) No. 1164/94 establishing a Cohesion Fund.

44 An important distinction should be made here between **GNP** per capita (the basis of assessment for Cohesion Fund eligibility and **GDP** per capita (the criterion for Objective 1 funding under the Structural Funds). In the case of Ireland, its GNP per capita as a percentage of the EU average is several points lower than its GDP per capita. This is because the profits of foreign-owned companies in Ireland count towards GDP but not GNP.

45 Lords Select Committee, Evidence, page 90

> The German Government is of the view that the Cohesion Fund was introduced in Edinburgh in 1992 with the intention of easing the rapprochement of the economically weaker states to EMU without endangering important investments in the areas of transport and the environment in these countries. The assistance from the Cohesion Fund should, therefore end when a country joins EMU. The Cohesion Fund should not become a permanent, second instrument of assistance in addition to the Structural Funds. This is something which is seen by our Spanish friends from quite a different point of view.

The UK Government has expressed similar views. In its written submission to the Lords Select Committee, the DTI said:[46]

> The Government considers continued Cohesion Fund receipts for Member States joining the single currency (EMU) difficult to reconcile with the original Cohesion Fund Objectives, particularly its required convergence programme.

The Committee was of the same opinion, saying in its conclusions:[47]

> We consider that those Member States which have joined the single currency should no longer be eligible for Cohesion Fund receipts, although we would recommend that these should be phased out in the period up to 2006, as should the Fund itself.

Only those countries currently in receipt of assistance from the Cohesion Fund have argued for its retention within the Council of Ministers.

46 Lords Select Committee, Evidence, page 15
47 Lords Select Committee, Report, Page 25