

# SCOTTISH EUROPEAN STRUCTURAL FUNDS FORUM



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**SCOTTISH ENTERPRISE BOARDROOM  
ATLANTIC QUAY, GLASGOW  
MONDAY 6 DECEMBER 2004 AT 10 AM**

## **AGENDA**

Coffee available from 9.30 am

- 1. Welcome**
- 2. Apologies**
- 3. Minutes of 24 May meeting and matters arising**
- 4. Financial performance and implementation of the 2000-2006 Scottish Structural Funds Programmes (Paper 1)**
- 5. Presentation by Scottish Enterprise: the added value of Structural Funds to SEN projects**
- 6. Future of the Funds – Revised report from the Analytical Working Group (Paper 2)**
- 7. Update on the 2007-13 Structural Funds negotiations and partner engagement (Paper 3)**
- 8. Date of next meeting**

Scottish Executive  
November 2004

Meeting Date: 6 December 2004

Paper Number:

1

Agenda Item Number:

4

For Discussion

Agenda Item:

Programme implementation

## **SCOTTISH EUROPEAN STRUCTURAL FUNDS FORUM**

### **FINANCIAL PERFORMANCE OF THE 2000-2006 SCOTTISH EUROPEAN STRUCTURAL FUND PROGRAMMES**

#### **Purpose**

1 The following paper will inform Forum members of the current progress towards the N+2 targets for the Structural Funds programmes for 2004. As members will recall, similar progress papers have been presented at previous Forum meetings. With the December meeting scheduled so close to the final deadline for this year's target, more up-to-date figures will be presented at the meeting itself.

#### **The N+2 rule**

2 The de-commitment rule (N+2) is set out in Article 31 of Council Regulation 1260/1999 and is a financial control designed to encourage sound management of the programmes and avoid end loading of activity. It requires de-commitment of any funds not spent by the end of the second year following the year to which they were allocated. The practical effect of this rule is that failure to meet the annual spending targets means that money will be returned to the Commission budget and therefore lost to the Programmes in Scotland. The annual targets relate to payment of Structural Funds by the Commission to Member States as reimbursement of expenditure. In order to meet the targets therefore, project development, delivery, spend and claims are all essential throughout the programming period.

#### **Effect of exchange rate variations**

3 A significant factor influencing progress towards N+2 targets has been the volatility of the sterling/euro exchange rate. As N+2 targets are set in euros, exchange rate fluctuations alter the value of the sterling equivalent required to meet the targets. Over the life of the programmes so far, sterling has moved between €1.51 and €1.42 to the £. These changes increased the sterling value of the Programmes, but therefore also of the targets, by £17.5m since December 2003.

#### **Overall position**

4 Overall progress towards targets is better than at this time last year, though it has still been unsatisfactory in some areas. Two programmes (Objective 3 and South of Scotland Objective 2) have now met their targets.

5 However, spend has been disappointing in two programmes – the Western Scotland Objective 2 Programme (both ERDF and ESF, which is administered by SEP Ltd, and the Highlands and Islands Special Transitional Programme (ERDF), which is administered by HIPP. Both these Programmes have spent only 85% of the available resources at the time of analysis (19 November), and both need to spend more than £10m over the next month if they are not to lose the resources permanently. These programmes have been further handicapped by the unfavourable exchange rate fluctuations, which have had the effect of increasing the sterling value of the euro N+2 targets. The target for ERDF in Western Scotland rose by £2.8 million between October and November, while the target for ERDF in the Highlands and Islands rose by £1.2 million over the same period. Figures 1 and 2 in Annex 1 illustrate the overall position.

6 A relatively small Programme, URBAN II (also administered by SEP Ltd) is in difficulties as well, having so far spent less than 75% of the resources available to it. We are therefore in a less secure position than we anticipated earlier in the year when, on the basis of projections from Programme Management Executives and public sector partners, we expressed greater confidence about meeting this year's targets. The detailed position is set out in the following paragraphs.

- **Highlands and Islands**

- The **ESF** target has already been achieved.
- The **ERDF** programme is currently £11.4 (€16.4) million short of its target. There is a risk that this programme could fall short of target.
- The **EAGGF** and **FIFG** programmes are currently £1.7 (€2.4) and £3.2 (€4.5) million, respectively, short of their N+2 targets. The Scottish Executive Environment & Rural Affairs Department is confident that these targets can be met.

- **Objective 3**

- The N+2 target has already been achieved.

- **South of Scotland**

- The N+2 target has already been achieved.

- **West of Scotland**

- We anticipate receipt of the £2.6 (€4.8) million worth of claims needed to meet the **ESF** target.
- There is currently a shortfall of £16.7 (€24) million, and a significant risk that the **ERDF** programme may not meet its N+2 target.

- **East of Scotland**

- The East **ERDF** programme is currently £500,000 short of its target. We are confident that we shall receive sufficient funding to meet the target.

- **URBAN II**

- This Community Initiative is currently £540,000 (€780,000) short of target. We are confident that Ministerial action will ensure receipt of sufficient claims to meet the target.

- **EQUAL**

- The N+2 target has been achieved in respect of the Scottish proportion of the programme.

## **7 General action taken to address N+2 issues**

- **Highlands and Islands**

- The Highlands and Islands programme met its N+2 target last year and is experiencing difficulties for the first time this year. Of the four funds it administers, **ESF** has already met its target. For the **ERDF** component of the Programme, measures have been put in place to accelerate spend and to bridge the gap between current performance and the target. These include:

- applying pressure to existing projects,
- accepting increased costs as eligible for grant,
- increasing grant rates,
- identifying a limited number of retrospective projects based around a small package of business development projects in fragile and island locations, and
- approving a loan fund for renewable energy projects

We are also working with partners to establish how far retentions on capital projects might be paid early and release more grant. The 'shortfall' currently stands at some £9.5 million. Taken together these initiatives have the potential to produce claims worth around £11.275 million.

**EAGGF** and **FIFG** are both largely the responsibility of SEERAD. Scope here is rather more limited but pressure is being applied to applicants to bring forward spend and claim grant. We have however been able to identify up to £700,000 of EAGGF grant that can be claimed through adjusting arrangements for claims and accepting a retrospective project.

- **West of Scotland**

- The Deputy Minister for Enterprise & Lifelong Learning, his officials and Strathclyde European Partnership Ltd have undertaken a number of urgent actions to ensure that the level of claims made by project sponsors improves.

- On 15 October, the PME issued follow up letters to all projects that failed to meet claim projections to 30 September. This was supported by subsequent telephone calls by members of the PME's senior management team to either Chief Executive or Finance Director level to reinforce the consequences of failing to improve spend levels. This effort was concentrated on, but not restricted to, 13 large projects whose expenditure has lagged behind profile and included visits from PME staff to reinforce the N+2 message.
- Additional claims of £3.34 million can be expected from projects that were successful in securing retrospective awards last year. These projects have now submitted claims for increased grant based on spend up to 30 September 2004.
- West of Scotland advisory group meetings scheduled for December 2004 have been postponed to January to maximise effort on claims processing.
- These considerable efforts will make a difference to the level of shortfall, but given the initially high level of underspend, it remains the case that the Western Scotland Programme may yet be unable to amass the £12 million of claims needed to avoid de-commitment this year.

- **URBAN II**

- The URBAN II community initiative is administered by Strathclyde European Partnership, and has been the focus of similar actions to the ERDF Programme, including Ministerial letters to 3 key project sponsors, and visits from SEP officials.

### **Further specific action undertaken by the Scottish Executive**

8 In 2003, targets were met in the Western Scotland and East of Scotland Programmes by retrospective approval of projects (subject to conditions agreed with the European Commission). The Scottish Executive is currently working with HIPP and project sponsors in their area to investigate how retrospective approval of eligible projects could assist meeting the N+2 target in the Highlands and Islands. Conditions would be similar to 2003, including requirements that the opportunity to apply retrospectively should be offered equally to all programme partners, and that resources freed by any award of ERDF would have to show to have been applied to work consistent with the objectives of the Programme.

9 European Structural Funds Division is also working with other policy divisions in ETLLD to identify areas of possible spend in Western Scotland and the Highlands and Islands that could be declared by the end of the year. It may be possible to realise spend in relation to the SMART and SPUR grant schemes, and possibly other areas of work.

10 The programmes at risk – Western Scotland Objective 2, Highlands and Islands Special Transitional Programme, and URBAN II – remain the subject of constant monitoring by the European Structural Funds Division. SEERAD is similarly monitoring progress on EAGGF and FIFG. All practical actions to assist these programmes in meeting their targets will be taken.

## **N+2 in 2005**

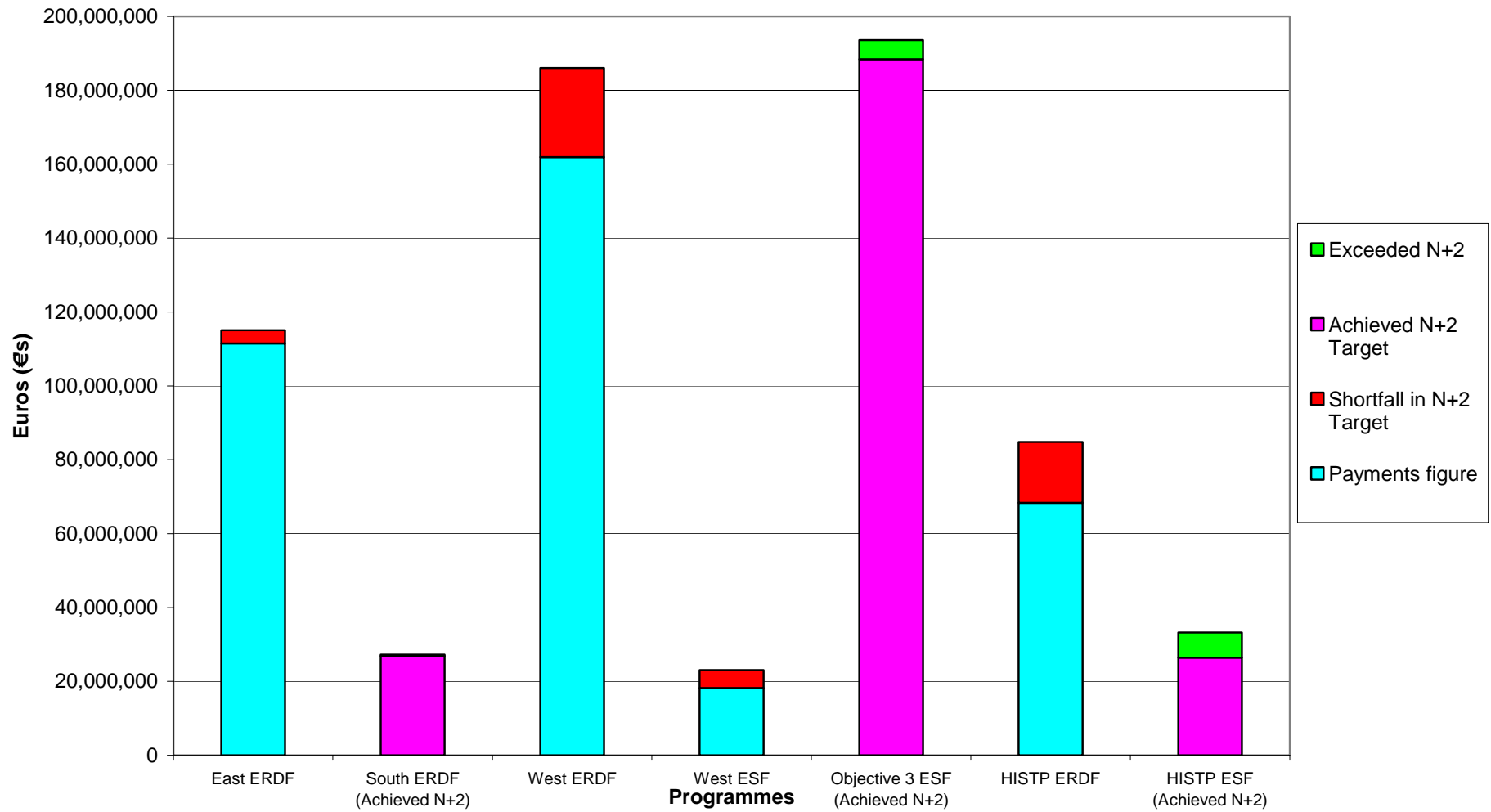
11 It is generally considered that 2005 will be the most difficult year of the current programmes in terms of meeting N+2 targets. This is because resources in the most popular priorities are now almost fully committed and the only scope for increasing spend is by converting commitment to spend at a faster rate than hitherto, or by increasing commitment and spend in priorities that have so far proved less attractive to project sponsors.

12 It has been evident over the past two years that the projections of spend made by PMEs and project sponsors at the mid-point of the year have later proved to be over-optimistic. Starting to plan for N+2 at the beginning of the calendar year and reviewing plans in midsummer has not proved to be an adequate basis for managing N+2 effectively. Annex 2 gives an example of how uneven claims pattern in a programme – with most claims concentrated late in the year – can cause difficulties. Early planning for N+2 will help to ensure more even and predictable claims performance, and therefore make targets easier to attain. We have therefore urged the PMEs to run their N+2 Action Plans from October in the previous year to September.

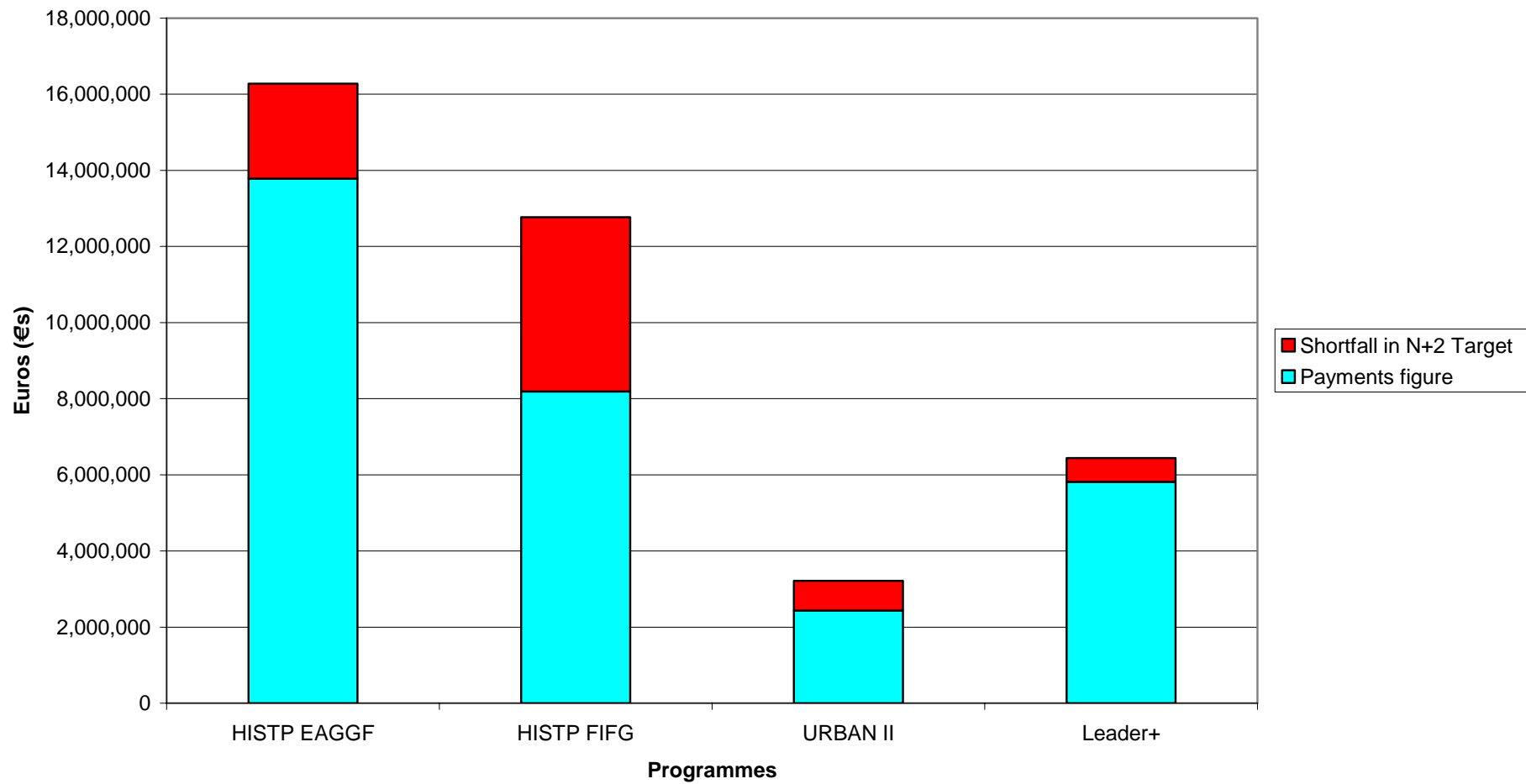
**Scottish Executive  
European Structural Funds Division  
December 2004**

## Annex 1: Figures

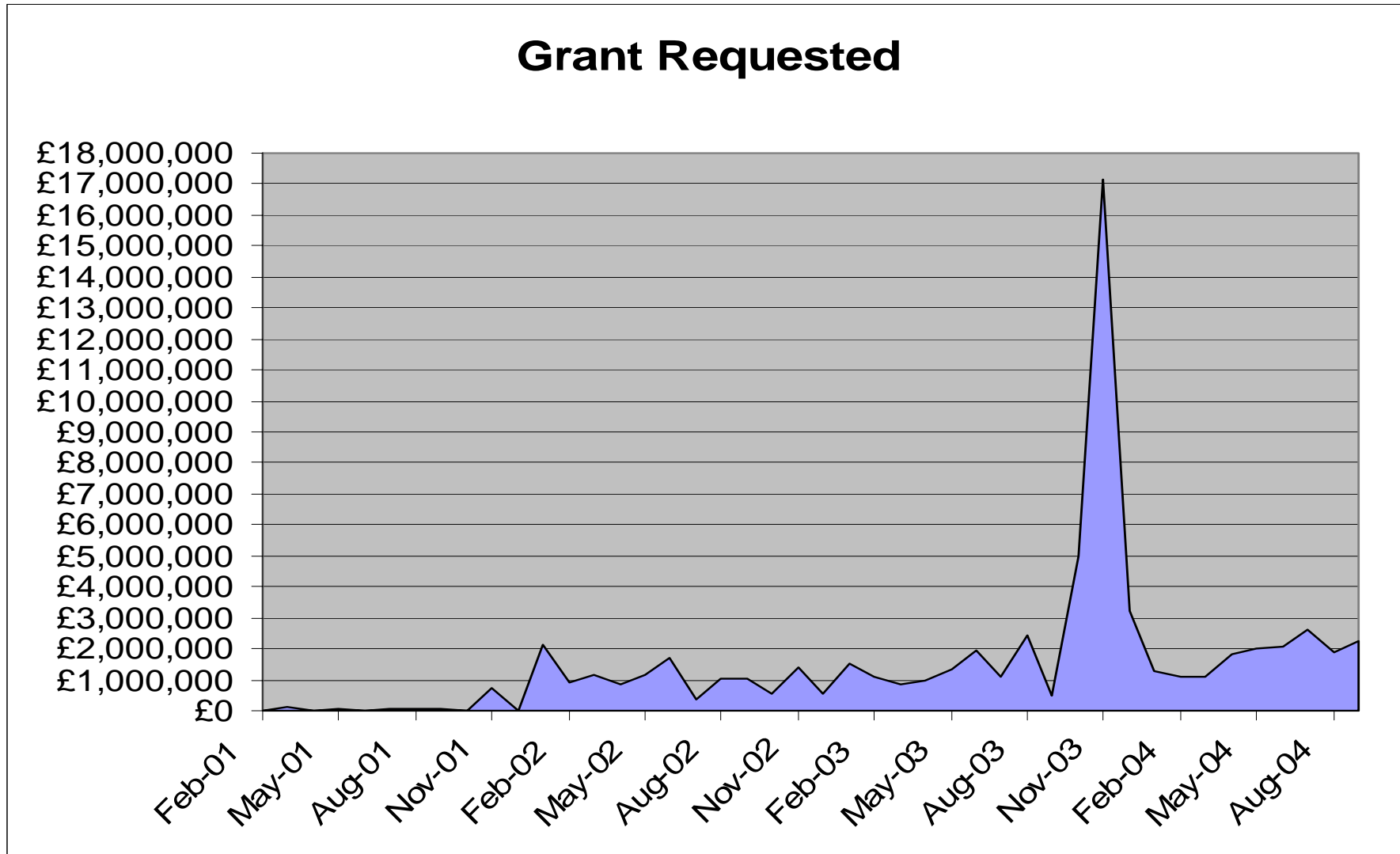
### EURO Progress towards N+2 targets (as at November Exchange Rates)



### Community Initiatives and SEERAD - Euro Progress towards N+2 (as at November Exchange Rates)



Annex 2: Claims profile



Meeting Date: 6 December 2004

Paper Number:

2

Agenda Item Number:

6

For Information

Agenda Item: Update on Analytical Working Group report

## **SCOTTISH EUROPEAN STRUCTURAL FUNDS FORUM**

### **UPDATE TO THE ANALYTICAL WORKING GROUP'S INITIAL REPORT ON THE EUROPEAN COMMISSION'S PROPOSALS FOR STRUCTURAL FUNDS REFORM: IMPLICATIONS FOR SCOTLAND**

#### **Introduction**

1. This paper updates the Analytical Working Group's initial report (of May 2004) to take account of more recent developments relating to the European Commission's proposals for Structural Funds after 2006. The Analytical Working Group was set up by the Structural Funds Forum to report on the financial implications of the Commission's proposals for Scotland. The emphasis of this paper, like that of the initial report, continues to be on the implications for Scotland of these proposals. It does not repeat the sections of the initial report that summarised the Commission's 3<sup>rd</sup> Cohesion Report's account of recent Cohesion trends, the rationale for the Commission's proposed regime, or issues arising from the 3<sup>rd</sup> Cohesion Report that were identified by the Analytical Group. Nor does it examine the connection between the proposals for EU regional policy and regional State Aids. Rather, it updates the sections dealing with the proposals for a new regime and the associated modelling of financial implications.

#### **The Commission's proposals**

2. The Commission's proposals for Structural and Cohesion Funds 2007-13 have been refined since the Analytical Group initially reported. In the intervening period, the Commission has given more detail on its initial proposals in the Third Cohesion Report, though the proposals themselves have not changed substantially. There have been two major developments since the Analytical Working Group's initial report. First, the Commission published its draft General Council Regulation on 14<sup>th</sup> July 2004 along with four other regulations on the Structural Funds. This has been supplemented by documents outlining the Commission's methodology for calculating different funding allocations through Fiche Nos 15 (Convergence), 17 (Capping of Resources), 26 (Regional Competitiveness and Employment), and 28 (Cooperation). The key elements are described below, and Annex C gives a graphical summary.

3. The total budget over the period 2007-13 is set at €36.2 billion (2004 prices). This total budget is still the subject of debate between Member States; the Commission's proposed budget is at the upper end of the spectrum of views on what the total budget should be. Any final agreement on the total budget could, clearly, affect the breakdown of funding for different elements and the forecasts that are made later in this report.

### **Convergence objective (€264.0 billion) comprising:**

➤ *Full Convergence: €177.88 billion*

4. Distributed between NUTS II regions that have GDP per head below 75% of the EU25 average. Fiche No 15 sets out the allocation method, including the relative weights of the different criteria: eligible population, regional GDP per head, national GNI per head, and regional unemployment.

➤ *Statistical Phasing-Out (so-called 'Statistical Effect'): €22.11 billion*

5. Distributed between NUTS II regions which are below 75% of EU15 average GDP per head but above 75% of the EU25 average GDP per head (i.e. they narrowly fail to qualify for full Convergence funding). As above, allocations to Member States would take account of the eligible population, regional and national GDP per head, and regional unemployment. Fiche No 15 states that "a similar approach" would be used for Statistical Phasing-Out as for Convergence regions. However the Fiche gives less detail about the allocation method than it does for full Convergence regions.

6. The Fiche states that, as a general rule, the aid intensity for each Statistical Phasing-Out region in 2007 should not be higher than 85% of the aid intensity received in 2006 under Objective 1. For regions that do not receive Objective 1 funding in 2006 and for regions of the new Member States there would be "a specific and fair treatment". The Fiche does not say what constitutes a specific and fair treatment, although more detail on this issue is currently being sought from the Commission. Aid intensity would be the same in 2008 as in 2007 and then fall by 5% each year.

➤ *Cohesion funding: €63.00 billion*

7. This would go to Member States that have GNI per head below 90% of the EU25 average. Allocations would take account of eligible population, the level of GNI per head, change in GNI per head over a previous period, and the area of the Member State. There is no indication yet of the relative weights for these factors.

8. €1.11 billion is earmarked for the Outermost Regions, (Guadeloupe, French Guiana, Martinique, Reunion, Azores, Madeira and the Canary Islands).

### **Regional Competitiveness and Employment objective (€57.9 billion) comprising:**

➤ *Mainstream Competitiveness: €48.33 billion*

9. All NUTS I or II regions that do not qualify for Full Convergence, Statistical Phasing-Out or Competitiveness Phasing-In funding (see paragraph 10) would be eligible for mainstream Competitiveness funding. Fiche No 26 sets out the allocation criteria: eligible population, unemployment (which, unlike the other regional criteria, would be measured at NUTS III level), regional employment rate, regional low educational attainment, regional population density, and regional GDP per head. The Fiche gives weights for each of the criteria.

➤ *Competitiveness Phasing-In: €9.66 billion*

10. This would go to NUTS II regions that currently receive Objective 1 funding but which would not be eligible for Full Convergence or Statistical Phasing-Out funding in the new programme, i.e. their level of prosperity has grown appreciably. Fiche No 15 states that “a similar approach” would be used for Phasing-In regions as for mainstream Competitiveness regions, but it does not spell this out.

11. As with Statistical Phasing-Out regions there would be limits to the level of funding that Phasing-In regions could receive, but there are some differences. For each Phasing-In region the level of aid in 2007 cannot, as a general rule, be more than 75% of the level of aid it receives in 2006 from Objective 1. For regions of the new Member States which do not receive Objective 1 in 2006 the treatment would be “specific and fair” but this is not spelt out. From 2008 the level of aid would fall linearly so that, in 2011, it reaches the level of mainstream Competitiveness support, and this level would continue in 2012 and 2013.

**European Territorial Cooperation objective (€13.2 billion) comprising:**

➤ *Cross-Border Cooperation (€4.7 billion) and ERDF contribution to the cross-border strand of the European Neighbourhood and Partnership Instrument and of the Instrument for Pre-Accession (€1.6 billion)*

12. Eligible population would be the population of NUTS III regions along internal or external borders of the EU or in maritime border areas (internal or external) separated by not more than 150 kms to ensure the coherence and continuity of existing cooperation areas.

➤ *Transnational Cooperation (€6.3 billion):* The allocation criterion would be the population of Member States. All NUTS II regions would be eligible.

➤ *Cooperation Networks (€0.6 billion)*

**Technical Assistance**

13. €0.8 billion would be allocated for Commission expenditure on Technical Assistance.

**Absorption Limit**

14. An absorption limit is set on Structural and Cohesion Funds (including the relevant parts of the European Agricultural Fund for Rural Development and the European Fund for Fisheries): they should not exceed 4% of a Member State’s GDP as estimated when agreement is reached on the EU budget. If the financial allocation exceeds 4%, then proportional reductions are made to the allocations for each Objective (Convergence, Competitiveness, etc). Fiche No 17 makes it clear that funding withheld by the absorption rule is not redistributed among Member States.

15. Annex C provides a summary graph of the key elements of the Convergence, Competitiveness and Cooperation objectives.

## Summary of Changes

16. It is helpful to summarise the key refinements that have been made in the Commission's proposals since the Analytical Working Group last reported.

17. The total budget is unchanged and there have been only slight adjustments to its distribution between the 3 main strands, but much more detail is given on how it would be apportioned to different funding elements within the strands.

18. The proposals are now more specific about indicators (and their weights) that would be taken into account in apportioning the budget for certain funding elements:

- Previously the proposals simply said that the allocation of funding for mainstream Competitiveness would be on the basis of "economic, social and territorial criteria". As noted in the previous section, these are now specified as (in addition to eligible population) regional GDP per head, regional employment, regional unemployment, regional low educational attainment, and regional population density.
- Previously the proposals did not mention any indicators for the allocation of Statistical Phasing-Out funding other than eligible population. Now, as noted in paragraph 5, these are now specified as national and regional GDP per head and regional unemployment, in addition to eligible population.
- It is now made clear that the allocation of funding for Phasing-In regions would be based on eligible population, regional and national prosperity, and regional unemployment, as noted in paragraph 10.
- The basis of allocations for full Convergence funding is now fully specified. As well as eligible population, account would be taken of regional and national prosperity, and regional unemployment, as noted in paragraph 4.
- The basis of allocation of the Cohesion Fund is more fully specified. As well as eligible population, it is now proposed that account would be taken of the level and change of national GNI per head, and of the area of the Member State. However the weights for these different factors are not yet known, as noted in paragraph 7.

## Implications for Scotland

19. The bullet points below set out which parts of the proposed regime would be relevant to Scotland:

- **Cohesion:** The UK would not qualify for the Cohesion Fund.
- **Convergence Funding:** None of the Scottish NUTS II regions are expected to qualify for full Convergence funding.

- **Statistical Phasing-Out:** The Highlands & Islands NUTS II region could qualify for Statistical Phasing-Out funding (although this is not certain until the precise time when eligibility is determined). Because the Highlands & Islands would not receive full Objective 1 funding in 2006, should it qualify for Statistical Phasing-Out funding it would be one of the regions for which the allocation in 2007 would be “objective and fair” rather than simply lower than the level of funding anticipated for 2006 (see paragraph 6 above).
- In the initial report the possibility of the South of Scotland (which has similar levels of GDP per head to the Highlands & Islands) qualifying for Statistical Phasing-Out funding was considered. However, the Commission’s Financial Framework of July 2004 clearly specifies that entitlement for Statistical Phasing-Out funding would be calculated at NUTS II level. The South of Scotland consists of two NUTS III areas which separately form part of the Eastern Scotland NUTS II area and the South Western Scotland NUTS II area. Consequently, the South of Scotland would consequently not receive Statistical Phasing-Out funding. A review of NUTS II boundaries will not be completed before the end of 2007 so, in this report, it is assumed that the South of Scotland would, instead, potentially qualify for Competitiveness funding.
- **Competitiveness Phasing-In funding:** No Scottish region would qualify for Competitiveness Phasing-In funding because none currently receives Objective 1 funding. With the exception of the Highlands & Islands, however, all would be eligible for mainstream Competitiveness funding, though it is still not clear how programmes would be defined within lowlands Scotland.
- **Cooperation funding:** Scotland would have an interest in funding of the Trans-national and Network strands of the Cooperation theme.

### **Revision to Estimated Funding Receipts for Scotland**

20. Based on the developments reported above, we have calculated a revised set of Scottish funding estimates. The Commission proposes that financial envelopes would be allocated to Member States. These allocations would largely be based on eligibility for different funding elements at regional intra-Member State level. However, the Member States would themselves decide on the final allocation of their national envelopes within their territories. In order to forecast what the implications of the Commission’s proposals would be for Scotland, we have assumed that the value of allocations would be passed **directly** from the EU to Scottish regions and we have used the methods which the Commission has proposed for determining the national envelopes. In reality though, the allocation criteria used by the UK government would be an important influence on the level of Structural Funds received by Scotland. **It should be emphasised that there are still many uncertainties in these forecasts.**

- The estimates are based on 2001 data, whereas the final allocations would be based on the latest data available.
- In the previous Scottish funding estimates the indicators were not fully specified and we had to make assumptions about their relative weights. The indicators and relevant weights are now generally available, although there are still some uncertainties remaining. Pending further information about how it would be determined, we have not applied a ceiling to the estimate of Statistical Phasing-Out funding for the Highlands & Islands. We have also made an assumption about Scottish eligibility for Cooperation funds (detailed in paragraph 19). These estimates are presented under two scenarios now, rather than the original three: newly-defined ‘high’ and ‘low’ scenarios.
- When calculating the Cooperation funding in the initial report, forecasts were based upon a straight population allocation and used for the entire EU25 population, giving a funding per head figure of €4 per annum. However, with the additional information on this funding programme (as described in paragraph 12) for the purpose of these calculations we expect that Scotland would not qualify for the cross-border element of Cooperation funding, but it may be eligible for the trans-national and Cooperation Network elements. Thus calculations are now based on a straight population allocation from these funding strands only.

### *Estimated Scottish Structural Funding*

21. Using the method described in Annex A, the following estimated funding totals are calculated:

**Table 1.1. Scottish Funding Estimates**

<b>Funding Strand</b>	<b>High Scenario (per annum)</b>	<b>High Scenario (2007-13)</b>	<b>Low Scenario (per annum)</b>	<b>Low Scenario (2007-13)</b>
<i>Statistical Phasing Out</i>	€65.8m	€460.6m	€0 m	€0 m
<i>Mainstream Competitiveness</i>	€103.1m	€721.4m	€111.3m	€779.1m
<i>Cooperation</i>	€10m	€70.3m	€10m	€70.3m
<b>Total</b>	€178.9m	€1,252.3m	€121.3m	€849.4m

### **High Scenario**

22. The high scenario now assumes only the Highlands & Islands **would** qualify for Statistical Phasing Out funding. The estimated total funding figure for Scotland (2007-13) of €1.3 billion at 2004 prices would be about a 15% reduction in real terms compared to the level of funding in the 2000-06 period.

## Low Scenario

23. The low scenario assumes the Highlands & Islands **would not** qualify for Statistical Phasing Out funding, thus being eligible only for mainstream Competitiveness funding. The estimated total funding figure for Scotland (2007-13) of around €849 million at 2004 prices would be about a 50% reduction in real terms compared to the level of funding in the 2000-06 period.

24. The change in forecast funding levels compared to the May report (shown in Table 1.2 below) can be attributed to the following factors;

- Estimated Statistical Phasing-Out funding per head has increased from €184 to €189 p.a, due to a change in the percentage allocation detailed in the Commission's Financial Framework (July).
- The indicator adjustments, which were not made in the previous report but are made in the present estimates, increase the total funding estimates by around 5% for the High Scenario and 16% for the Low Scenario. These increases are partly offset by other factors.
- Cooperation funding is now allocated using different assumptions to the previous calculations. Scotland is now assumed to be eligible for only part of the Cooperation budget (see paragraph 19).

25. The updated High Scenario estimates are about 10% higher than those in the Analytical group's initial report, i.e. the decrease compared to funding in 2000-06 is about 10% less. The Low scenario estimates remain broadly similar.

**Table 1.2. Comparison of Initial and Updated Estimates**

Previous Report (May)	Update Report
MIDDLE SCENARIO	HIGH SCENARIO
2007-13 = €1.2 bn	2007-13 = €1.3 bn
Approx 25% decrease	Approx 15% decrease
LOW SCENARIO	LOW SCENARIO
2007-13 = €844 m	2007-13 = €849 m
Approx 50% decrease	Approx 50% decrease

Note: The Middle Scenario is used from the May report because, like the High Scenario in this report, it assumed that the South of Scotland would not qualify for Statistical Phasing-Out funding.

26. Both the May and the updated estimates point to a potentially smaller decrease in Structural funding to Scotland than has been widely anticipated. This can, in part, be attributed to the substantial increase in the EU budget which the Commission proposes, and partly to the fact that, in the high scenario, the Highlands & Islands is assumed to qualify for generous Phasing-Out funding without, at present, any ceiling applied, rather than general Competitiveness funding.

## **Indicators for Allocation of Structural Funds within the UK**

27. The estimates given above assume that all elements of funding would be allocated directly from the EU to Scotland. This is not realistic. For Competitiveness funding, while the Commission proposals calculate indicative funding envelopes on a regional basis, the Commission is clear that it is up to the Member States to develop their own methodologies for determining programmes and allocating funding between the different Competitiveness programmes. Allocations for Convergence funding would pass directly to the regional programmes concerned. As for Cooperation funding, Member States would have flexibility at the margin in how they distribute the allocations between the cross-border and the transnational components.

28. The way the UK decides to allocate Competitiveness funding would therefore be important for Scotland. Different criteria may affect Scotland's share of the UK total. The Scotland-rest of UK comparison of various indicators (which was included in the Analytical Group's initial report) is therefore repeated as Annex B in this paper. It shows which indicators would be more, and which less, favourable to Scotland. Work on this is unlikely to begin until 2005 at a UK level, although the Scottish Executive would be closely involved.

29. The indicators shown are mostly taken from Eurostat. Other possibly relevant indicators would be available for Scotland-rest of UK comparisons using sources other than Eurostat.

## **Summary and Conclusions**

30. The Commission's proposed regime for Structural Funds 2007-13 has become clearer since the Analytical Group's initial report in May 2004. Our best estimate is that, under the Commission's current proposals, and assuming for operational purposes that funds were allocated directly to Scotland, Scotland would receive about 15% less funds in real terms in the 2007-13 period than in 2000-06.

31. This estimate would be affected by any reduction to the overall budget for Structural Funds proposed by the Commission or by a redistribution of the total budget between the 3 different strands. It would also be significantly reduced if the Highlands & Islands were not in fact to qualify for Statistical Phasing-Out funding but, instead, only for general Competitiveness funding.

32. If the Commission's proposed regime is adopted, then the choice of criteria used by the UK government to allocate Structural Funds within the UK could have a significant effect on Scotland.

33. Finally, with the updating of this report, the Analytical Working Group's immediate tasks are now complete. As discussed in paper 3 for the 6 December meeting of the Forum, the Structural Funds negotiations are at an early stage and it is not clear whether – and when – any counter proposals may be made by the Commission or other Member States. When such concrete proposals are put forward, the Group will make appropriate analysis and report to the Forum.

**Scottish European Structural Funds Analytical Working Group  
November 2004**

## ANNEX A

### COMMISSION PROPOSALS: FUNDING 2007-13 FORECASTING THE IMPLICATIONS FOR SCOTLAND

The following annex outlines how the Commission's methodology for calculating allocations under the three proposed strands can be applied to Scotland. It draws heavily on the methodology described in the Commission's supplementary Fiches, but also makes assumptions in the continuing absence of critical information for making fully robust estimates.

#### Step 1: Funding of different strands

1. Use the budgets given in the Financial Framework:

Total Budget: €336.2 bn

➤ **Convergence: €264.1 bn**

Mainstream Convergence	€177.88 bn
Statistical Phasing Out	€22.11bn
Cohesion Fund	€63.00 bn
Outermost Regions	€1.11 bn

➤ **Competitiveness: €57.9 bn**

Mainstream Competitiveness	€48.3 bn
Competitiveness Phasing-In	€9.6 bn

➤ **Cooperation: €13.2 bn**

Cross-border	€6.3 bn
Transnational	€6.3 bn
Networks	€0.6 bn

#### Step 2: Statistical Phasing-Out

1. Calculate the “development gap” between the GDP per head of each Statistical Phasing-Out region and 75% of the average GDP per head of EU15. Fiche No 15 says that the level of prosperity of these regions “is assimilated to that of a region whose per capita GDP is 75% of the Community average”. We assume that the Community average in fact means EU15 average; EU25 would not make sense given that all Statistical Phasing-Out regions have GDP per head above 75% of the EU25 average.

2. From the scale given in Fiche No 15, apply the appropriate % assistance rate (3% in the case of the UK) to the development gap of each relevant region to give funding per head per year.

3. Compare the unemployment rate of each relevant region with the average for the group as a whole and calculate the numbers of any “excess unemployed” in individual relevant regions.
4. Multiply any excess unemployed by €100 per person to give additional funding per year. (We assume that the same rate applies to Statistical Phasing-Out funding as Fiche No 15 indicates for Convergence funding).
5. For each relevant region add development gap funding and excess unemployment funding and multiply the sum by 7 to give funding for the whole Programme period.
6. Compare the total forecast funding with the budget of €22.1 bn, and make any uniform adjustment that is necessary for funding to match budget.
7. The level of funding in 2007 should be subject to a ceiling based on a “specific and fair treatment”. We do not yet know what the nature of this would be and have therefore not applied a ceiling.

### **Step 3: General Competitiveness**

1. NUTS II regions eligible for General Competitiveness are those not eligible for (a) Full Convergence funding, or (b) Statistical Phasing-Out, or (c) Competitiveness Phasing-In funding. We assume that regions within Member States qualifying for the Cohesion Fund remain eligible for general Competitiveness funding providing they do not qualify for (a), (b), or (c).
2. Allocation of the budget for general Competitiveness funding is based on each relevant region’s weighted population. The factors and their weights are specified in Fiche No 26.
  - Simple total population is weighted 0.6.
  - The numbers of excess unemployed in the NUTS III areas making up the NUTS II region are weighted 0.15. Excess unemployed should be calculated by comparing the unemployment rate in each NUTS III area with the average for all NUTS iii areas in relevant NUTS II regions. However Eurostat has yet to make available unemployment data at NUTS III level. We have therefore calculated excess unemployment at NUTS II level.
  - The numbers of additional employed people in the NUTS II region that would be required to achieve an employment rate of 70% are weighted 0.1. This applies only to regions that have an employment rate below 70%. The employment rate data we have relates to the population aged 15-64. The same age group should be used in the calculation of deficit numbers of employed people. However Eurostat is not currently making available data on population age groups at NUTS II level. In order to calculate deficit numbers of employed people, we have therefore resorted to using the total population.

- The excess number of employed people in the NUTS II region that have low education are weighted 0.1. The % of people with low educational attainment in the region are compared with the average % for all Competitiveness regions. Fiche No 26 does not define the variable “Number of employed people with low education”. We have used data on the % of persons aged 25-64 whose educational attainment is “low”. As for the employment rate we have had to use total population to calculate excess numbers rather than population aged 25-64 (which is not yet available at NUTS II level from Eurostat).
- The numbers of additional people in the NUTS II region required to reach the average density of population are weighted 0.05. Population density in the region is compared with the average for all Competitiveness regions.

3. Using the method set out above, the total weighted populations attributable to the different indicators do not correspond to the weights set out in Fiche No 26 (deficit population density accounts for nearly all the total weighted population). At this stage, therefore, we impose the weights set by the EC: eg if simple population is to have a weight of 0.6, then the weighted population attributable to excess unemployment should amount to a quarter of this (because its weight within the total is 0.15).

4. Finally, after the set relative weights have been imposed, the weighted population of each region is increased by 5% if the NUTS II region’s GDP per head is below the average GDP per head of all relevant regions; or it is reduced by 5% if the region’s GDP per head is above the average. There is no scale to this adjustment: the adjustment is +5%, -5%, or 0 (if the region exactly matches the average).

5. The total budget for general Competitiveness is allocated to relevant NUTS II regions according to their shares of total weighted population.

#### **Step 4: Cooperation**

1. It is not expected that Scotland would qualify for the cross-border element of Cooperation funding, but it would be eligible for the trans-national and Cooperation Network elements. The total budget for these 2 elements amounts to €6.9 billion, equivalent to €15.18 per head of EU25 population over the Programme period..

2. Forecast allocation to Scotland over the Programme period is €15.18 x Scotland’s population.

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**N.B.** The steps detailed above are sufficient to estimate funding receipts for Scotland *if allocations were made direct to Scotland rather than via the UK.*

Other regions require estimates to be made also for elements of funding for which Scotland is not expected to be eligible: Cohesion Fund, Convergence Fund, Competitiveness Phasing-In funding, and the Absorption Limit to be applied where necessary.

## ANNEX B

### INDICATORS: SCOTLAND vs UK COMPARISON

1. The attached potential Indicator Chart (which is repeated from the Analytical Group's report) compares Scotland with the rest of the UK on various indicators taken from Eurostat. For most of the indicators any regions expected to qualify for full Convergence or for Statistical Phasing-Out funding are excluded from the rest of the UK figures. The Scottish figures do, however, include the Highlands & Islands.

2. These exclusions are made because it is assumed that Member States would pass on the allocation for Convergence funding determined by the EC, whereas they would have more discretion about the allocation of non-Convergence funding determined by the EC. In the case of Scotland this would relate principally to mainstream Competitiveness funding.

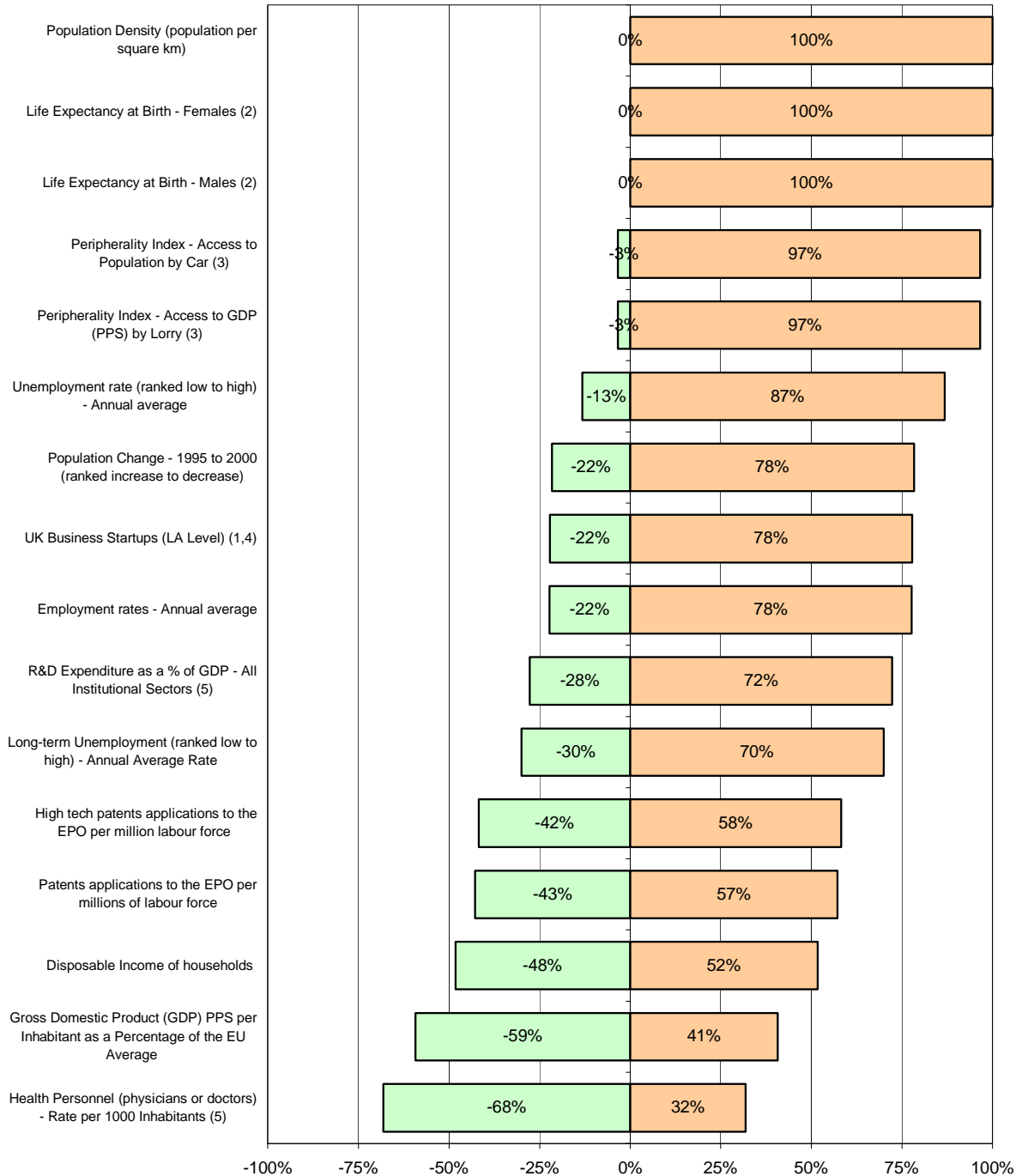
3. The indicators are ranked by the degree to which they would be favourable to Scotland, in an intra-UK allocation.

- Thus population density appears at the top: if allowance were made for population sparsity, this would be very much to the favour of Scotland because 100% of Scotland's population live in NUTS II regions which are more sparsely populated than any of the non-Convergence NUTS II regions in the rest of the UK.
- At the other end of the scale, making allowance for the level of provision of health personnel (in relation to size of population) would not be to Scotland's advantage: 68% of the population in the rest of the UK live in regions where the level of health personnel provision is lower than the levels in Scottish regions.

4. In brief, any indicator with more than 50% shown to the right of the vertical line would be favourable to Scotland, and the higher the figure is the more favourable it would be. It should be noted, though, that a high value to the right of the vertical line does not mean that Scotland has a high value of that indicator. It all depends on what the indicator is and whether having a high value of it is likely to attract more allocation of funds.

- For example Scotland has a relatively low rate of business start-ups, which is a disadvantage for Scotland's economy but would mean that Scotland's allocation would be increased if account were taken of it. Thus more of the horizontal bar for this indicator is shown to the right of the vertical line: 78% of the population in the rest of the UK live in regions where the rate of business start-ups is higher than the levels in Scottish regions.

**CHART 2: Eurostat Regional Indicators - Percentage of Population in UK NUTS2 Areas Ranking Above and Below Scotland (excludes possible convergence regions)**



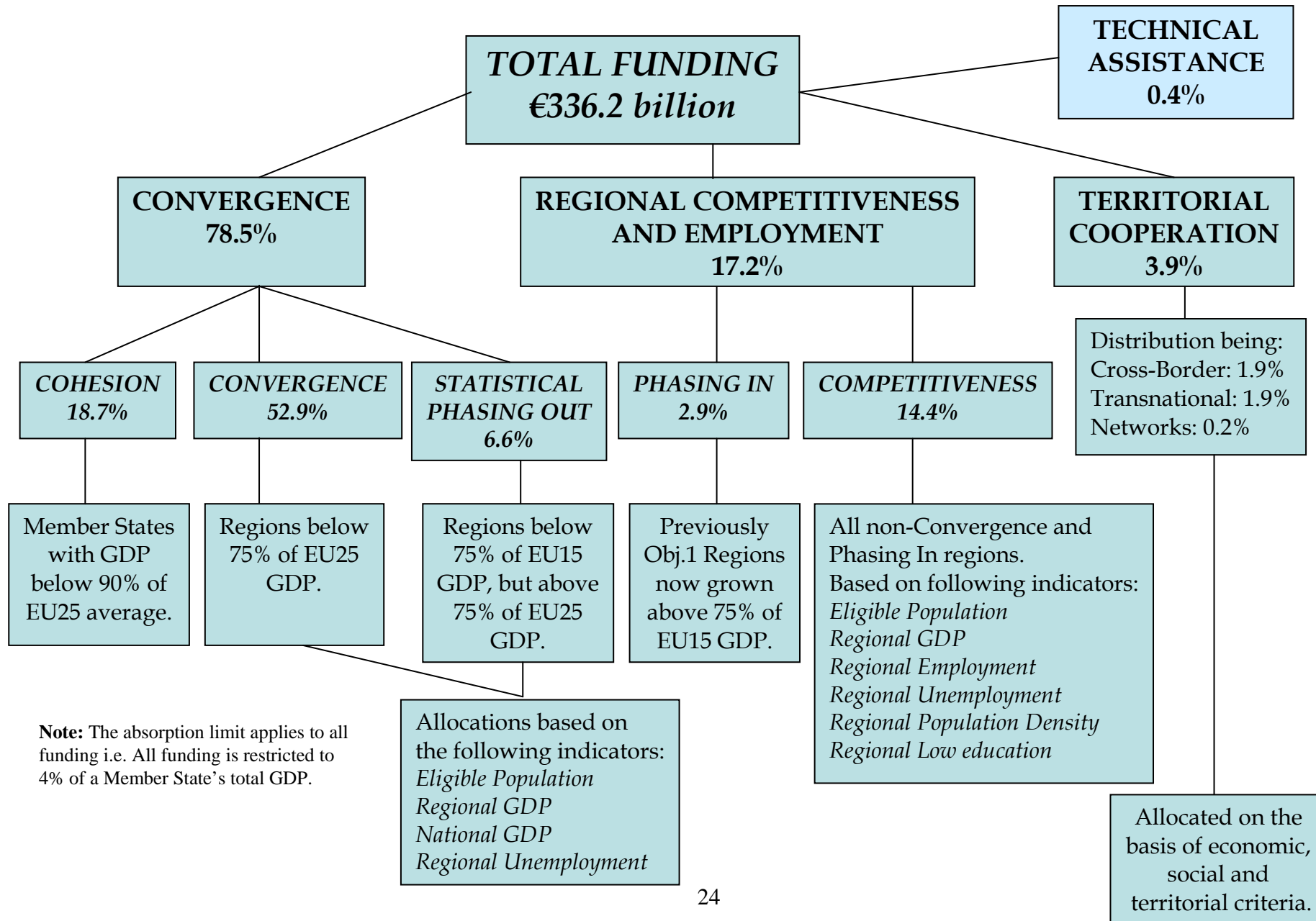
(1) Convergence regions cannot be removed  
 (2) Data from World Health Organisation and Government Actuary's Dept  
 (3) Data from Copus 1999 (research for 2nd cohesion report)  
 (4) Data from ONS small business service  
 (5) Calculated at the NUTS1 level  
 All other data from Eurostat and populations calculated at the NUTS2 level

**Percent of population in UK NUTS2 areas ranking:**  
 <==== Below | Above ====>  
**Scotland**

ANNEX C

EUROPEAN COMMISSION PROPOSALS

EUROPEAN STRUCTURAL FUNDING 2007-13



Meeting Date: 6 December 2004

Paper Number:

3

Agenda Item Number:

7

For Information

Agenda Item:

Update on SF negotiations

## **SCOTTISH EUROPEAN STRUCTURAL FUNDS FORUM**

### **UPDATE ON THE 2007-13 STRUCTURAL FUNDS NEGOTIATIONS AND PARTNER ENGAGEMENT**

#### **Purpose**

1 To inform Forum members of recent developments in the negotiations of the 2007-13 Structural Funds and on engagement with Structural Funds partners in Scotland on preparations for the future.

#### **Structural Funds negotiations**

2 Since the Forum met in May, the Commission has provided more detail on its Structural Funds proposals, originally presented in the 3<sup>rd</sup> Cohesion Report on 18 February, with the publication of the draft regulations on 14 July. Five proposed regulations for the 2007-13 period were set out: general (the main regulation); European Regional Development Fund (ERDF); European Social Fund (ESF); Cohesion Fund; and cross-border co-operation.

3 The regulations form the basis of the negotiations which have begun under the Dutch Council Presidency through the Structural Actions Working Group (SAWG). SAWG is the Council working group involving representation from all Member States which is examining the regulations at weekly meetings in Brussels. As the negotiations are a reserved matter, the DTI is the lead department for the UK in SAWG. However, the DTI discusses the UK line for each meeting through a Core Negotiating Group, which comprises representatives from UK departments and the Devolved Administrations. In addition, the Executive attends SAWG meetings in rotation with other Departments sharing the UK places in the delegation.

4 On 16 September, Patricia Hewitt wrote to UK Ministers and the Devolved Administrations, setting out the lines that the DTI proposed to take in SAWG. The letter restated the UK position, which has not changed since the publication of the regulations and which has been reported to the Forum at past meetings. The UK position has not altered throughout the Dutch Presidency and there is no indication from DTI or Treasury colleagues that it will do so in the near future.

5 In parallel with SAWG, financial and budgetary issues are being discussed in the Ad Hoc Financial Working Group under the Dutch Presidency. The Treasury is the UK representative on the Group. The Presidency decided that matters relating to the contentious issues of the overall size of the EU budget and the allocations under different budget headings – such as the Structural Funds – would be discussed through this Group. By the end of November, the Group will set out a series of budgetary options – or ‘building blocks’ – which will be discussed by Member States at the General Affairs Council in December. It is unlikely that this Council will resolve any of the key differences between Member States on financial issues.

6 The Presidency will also report on progress in SAWG at the December Council meeting. Overall, the negotiations to date have seen Member States setting out their views in relation to the Commission's proposals, with the focus on exploring rather than resolving the main differences of opinion. While there is consensus among Member States on a number of issues – particularly the lack of simplification promised by the Commission in the General Regulation and the drafting of the ESF Regulation – considerable work remains to be done, particularly on the focus of expenditure and the operation of the Co-operation objective.

7 The negotiations will continue into the Luxembourg Presidency. While significant resolution of many of the technical issues in the regulations is expected by the middle of 2005, it is unlikely that there will be any agreement on financial and budgetary issues until the end of the UK Presidency.

### **Scottish partner engagement**

8 While the negotiations have continued at UK and EU levels, Executive officials have been holding a series of meetings with Scottish Structural Funds partners between September and December. The meetings have had several objectives: they have enabled partners to be brought up to date on progress in the negotiations, and have allowed the Executive to get feedback from partners on key concerns in the draft regulations. These concerns have informed the UK negotiating line through the weekly Core Negotiating Group meetings. Moreover, it has been an opportunity to alert partners to the likely reduction in Structural Funds resources and the need to start consideration early of what the priorities should be for any potential future programmes, whatever their source of funding.

9 At the same time, within the Executive, the European Structural Funds Division has been holding meetings with other Divisions with a Structural Funds policy interest. This has involved close cooperation with SEERAD colleagues on the parallel developments in the negotiations of the Rural Development and Fisheries Fund Regulations, ensuring that any emerging Rural Development, Fisheries and Structural Funds programmes are complementary.

10 With the completion of the initial round of engagement meetings, it is becoming clear that preparations need to begin for possible future programmes. In the current round, programmes required 18 months to be developed and to secure Commission approval. A similar timescale will be needed this time around. The challenges for future programme development are significant, given the considerable uncertainty that surrounds the final shape of any Structural Funds settlement at EU level. As a result, the Executive may have to initiate the preparation of programmes in advance of any clear resolution of key issues, such as whether the UK would secure significant Structural Funds support.

11 The Executive intends to begin such programming in co-operation with partners in the second quarter of 2005.

**Scottish Executive  
European Structural Funds Division  
December 2004**