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# Grant for Business Investment

Guidelines



Commissioned by

**BERR**

Department for Business  
Enterprise & Regulatory Reform

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# Preface

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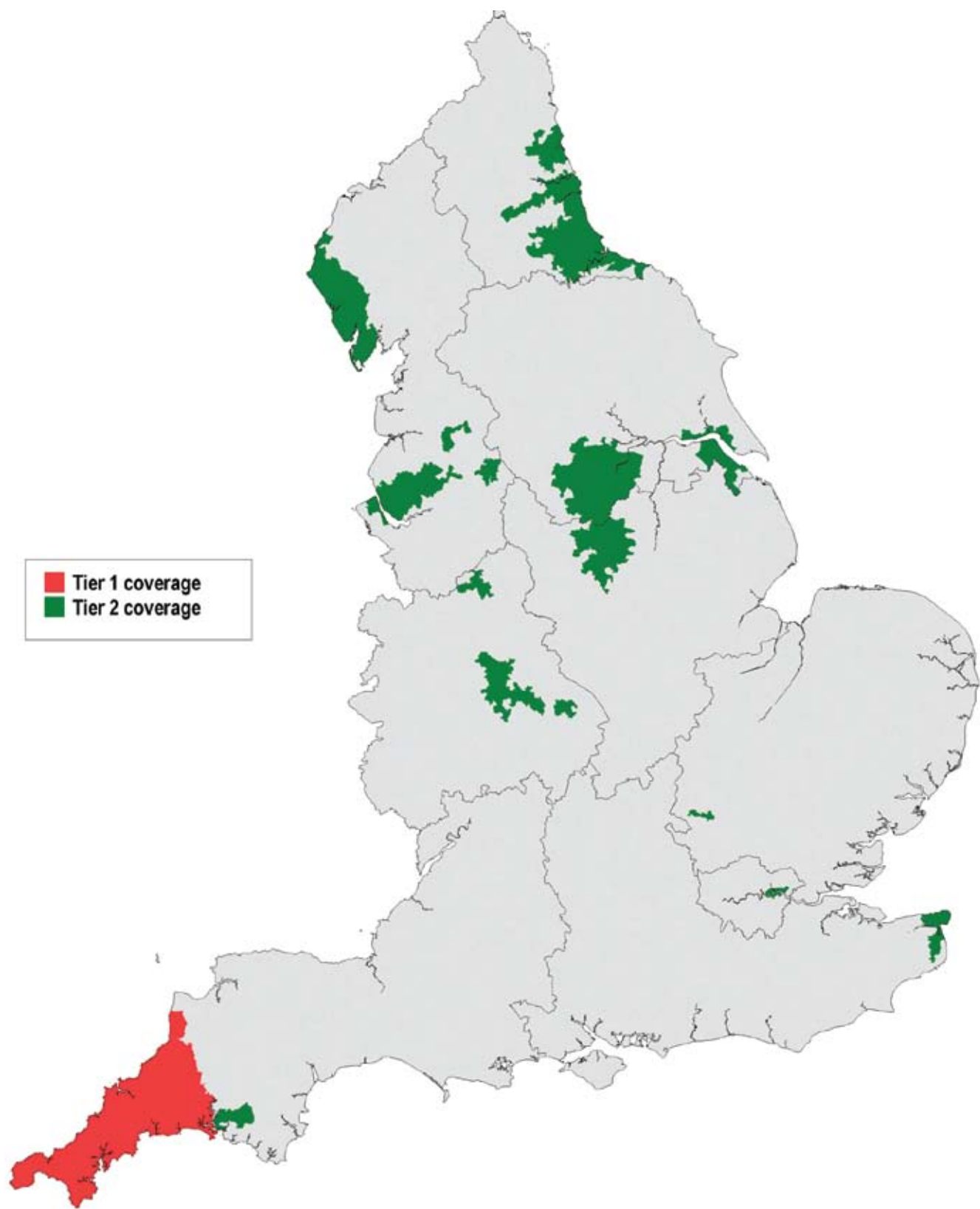
The European Commission ("the Commission") regulates State Aid across the EU to avoid distortion of competition within the common market. State Aid granted to promote the economic development of certain disadvantaged areas within the EU is considered by the Commission to be compatible with the common market. This kind of aid is known as national regional aid, and generally consists of aid for investment granted to large companies targeted on specific regions in order to redress regional disparities, or increased investment to small and medium-sized companies ("SMEs") in those regions over and above what is allowed in other areas. These specific regions are known as Assisted Areas.

The Assisted Areas Order 2007 defines the Assisted Areas of Great Britain between 2007-2013 (see Figure 1). The main forms of regional aid in Great Britain are Grant for Business Investment (GBI) in England and Regional Selective Assistance ("RSA") in Scotland and Wales, through which grants are paid to firms in support of capital investment projects.

Within the Assisted Areas GBI support may be given to large companies and SMEs as long as the scheme operates within the rules set out in the National Regional Aid Guidelines (OJ 2006/C54/08) and the Commission General Block Exemption Regulation (Regulation (EC) 800/2008).

Outside of the Assisted Areas in "Tier 3" regions GBI(SME) support may be given to SMEs providing that the support complies with the provisions set out in the Commission General Block Exemption Regulation (Regulation (EC) 800/2008).

This Commission Regulation also provides the EC with powers of scrutiny and the ability to adopt a decision stating that all or part of the future aid measures to which this Commission Regulation applies are to be notified to the Commission in accordance with Article 88(3) of the EC Treaty.



**Figure 1:** Assisted Areas in England, 2007-13

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# Part I:

## Scope of GBI scheme

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- 1** Grant for Business Investment (GBI) is a national business support scheme. Its objective is to assist the development of the most disadvantaged regions in England by supporting sustainable investment and job creation. It promotes the expansion, rationalisation, modernisation and diversification of economic activities of businesses located in the Assisted Areas, in particular by encouraging firms to set up new establishments there. GBI can also be used to address some of the market failures that limit the development of SMEs. Specifically, GBI may be used to offset the difficulty that SMEs have obtaining capital given the risk-averse nature of certain financial markets and the limited collateral that small businesses may be able to offer.
- 2** These Guidelines set out the rules for the operation of the GBI scheme. They are built upon the European State Aid law provisions set out in the General Block Exemption Regulation ((Regulation EC) 800/2008) and Treasury Green Book guidance designed to promote the efficient and proper use of public resources. Sections **1** to **3** describe the scope of the GBI scheme. They set out:
  - the legal base for the operation of the GBI scheme;
  - European restrictions on the provision of state aid;
  - national restrictions that are designed to ensure that GBI support is directed towards projects that have the greatest likelihood of producing sustainable benefits for the regional and national economies; and
  - sectoral restrictions that are derived directly from EC State Aid rules or flow from the national restrictions.

### 1 Legal base

- 3** Powers to support businesses using GBI are provided by section 7 of the Industrial Development Act 1982. Section 7(1) of the Act provides for financial assistance to be given on a discretionary basis in order to provide, maintain or safeguard employment in the Assisted Areas. Offers of assistance in England are subject to the consent of HM Treasury (HMT).
- 4** Powers to grant GBI in England to SMEs (GBI (SME)) outside of the Assisted Areas are provided by section 8 of the Industrial Development Act 1982.



- 5 In England GBI is delivered by the Department for Business, Enterprise & Regulatory Reform (BERR) for grants where the amount of support requested is £2m or greater. Grants of amounts less than £2m are delivered by the Regional Development Agencies (RDAs) and the London Development Agency. Potential applicants should note that all elements of the scheme are provided at the discretion of the relevant RDA or BERR, as appropriate. HMT approval is required for any grant over £7m or where the cost per job is greater than the delegated ceiling. In Scotland and Wales, Regional Selective Assistance (RSA) is delivered under devolved powers by the Scottish Executive (SE) and the Welsh Assembly Government (WAG).
- 6 Under the concordat on Financial Assistance to Industry (the Concordat), both BERR and the devolved administrations recognise that they have inherited common guidelines on financial assistance to industry. Separate but comparable arrangements apply to Northern Ireland. All parties to the Concordat commit to mutual consultation in adequate detail and reasonable timescale when it is proposed to change GBI policy and practice from the methodology set out in these Guidelines. Where a consensus cannot be reached among officials, differences should be resolved by Ministers.

## 2 European rules related to GBI

### 2.1 Scope

- 7 The Commission has been informed that GBI provides the following types of aid:
  - a) regional aid;
  - b) SME investment and employment aid; and
  - c) aid for the creation of enterprises by female entrepreneurs.
- 8 EC State Aid rules provide that GBI may not be used to:
  - a) provide aid to export-related activities namely aid directly linked to the quantities exported, to the establishment and operation of a distribution network or to other current costs linked to the export activity;
  - b) provide aid contingent upon the use of domestic over imported goods.

### 2.2 EC sectoral restrictions

- 9 GBI aid may be used to support businesses in most sectors of the economy.<sup>1</sup> However, State Aid rules mean that GBI cannot be used to provide aid that favours undertakings active in:
  - a) the fisheries and aquaculture sectors, as covered by Council Regulation (EC) No 104/2000 of 17 December 1999 on the common organisation of the markets in fishery and aquaculture products as amended by Regulation (EC) No 1759/2006;
  - b) the primary production of agricultural products (as defined in Annex A);

<sup>1</sup> EC State Aid rules specify that business support schemes such as GBI may not be restricted to specific types of economic activity within the manufacturing or service sectors. Tourism activities are not considered as being targeted at specific sectors.

- c) the processing and marketing of agricultural products (as defined in Annex A), in the following cases:
  - a. when the amount of the aid is fixed on the basis of the price or quantity of such products purchased from primary producers or put on the market by the undertakings concerned, or
  - b. when the aid is conditional on being partly or entirely passed on to primary producers;
- d) the coal sector as defined in Annex A;
- e) the steel sector as defined in Annex A;
- f) the shipbuilding sector as defined in Annex A;
- g) the synthetic fibres sector as defined in Annex A.

### **Firms in difficulties**

- 10** GBI cannot be used to support undertakings or firms in difficulty (see Annex A). Aid may only be granted to firms in difficulties in accordance with the Rescue and Restructuring Framework. In particular, aid granted to large or medium-sized enterprises during the restructuring period must always be notified individually to the Commission, even if it is granted as part of an approved scheme.
- 11** The power to grant rescue and restructuring assistance has not been delegated to RDAs and GBI assistance must not be used for this purpose.

### **2.3 Gross grant equivalent aid intensity**

- 12** For the purposes of calculating aid intensity, all figures used shall be taken before any deduction of tax or other charge. Where aid is awarded in a form other than a grant, the aid amount shall be the grant equivalent of the aid. Aid payable in several instalments shall be discounted to its value at the moment of granting. The interest rate to be used for discounting purposes shall be the reference rate applicable at the time of grant.

### **2.4 Prior notification**

- 13** GBI awarded in favour of large investment projects (see paragraph 29) shall be notified to the Commission if the total amount of aid from all sources exceeds 75% of the maximum amount of aid an investment with eligible costs of €100m could receive at the location of the project adjusted on the basis of the scale set out in paragraph 29.
- 14** This notification ceiling is equivalent to:

$$\text{Notification ceiling} = \text{€0.75m} \times \text{Intervention Rate (\%)}$$

and it is summarised for some of the most commonly encountered intervention rates in the table below:

Intervention Rate	10%	15%	20%	30%	40%
Notification threshold	€7.5m	€11.25m	€15.0m	€22.5m	€30.0m

### ***Notification of other large investment projects***

- 15** Whenever regional aid is granted to a non-notifiable large investment project, the operating department must notify the Commission within 20 working days of the granting of the aid and provide the Commission with the information requested in the form presented in Annex III of the Commission Guidelines on National Regional Aid (OJ 2006/C54/08).

### **2.5 Cumulation**

- 16** In determining whether the individual notification thresholds laid down in Section [2.4](#) and the maximum aid intensities laid down in Sections [2.8](#) and [2.9](#) are respected, the total amount of public support measures for the aided activity or project shall be taken into account, regardless of whether that support is financed from local, regional, national or Community sources.
- 17** GBI may be cumulated with any other aid granted under an EC notified scheme (for example training aid and aid for research and development) as long as those aid measures concern different identifiable eligible costs.
- 18** Training aid and research and development aid not granted under an EC notified scheme but that is used only to supplement GBI granted to companies operating in Tier 1 or Tier 2 regions shall be exempt from the notification requirement of Article 88(3) of the Treaty provided that the supplementary aid does not exceed 50% of the total aid to be granted to the investment and directly fulfils all of the conditions of the General Block Exemption Regulation (EC) No 800/2008) declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty as set out in Annexes [D](#) and [E](#).
- 19** GBI shall not be cumulated with any other aid exempted under the General Block Exemption Regulation or de minimis aid fulfilling the conditions laid down in Commission Regulation (EC) No 1998/2006 (as last amended by Decision of the EEA Joint Committee No 27/2007) on the application of Article 87 and 88 of the Treaty to the minimis aid or with other Community funding in relation to the same - partly or fully overlapping - eligible costs if such cumulation would result in exceeding the highest aid intensity or aid amount applicable to this aid under the General Block Exemption Regulation.

### **2.6 Incentive effect**

- 20** It is a requirement of EC State Aid law that GBI may only be awarded when it produces an incentive effect. GBI and GBI (SME) are considered to have an incentive effect if they enable the beneficiary to carry out activities or projects which would not have been carried out as such in the absence of the aid.
- 21** GBI is also considered to have an incentive effect if, in the absence of the aid, the investment project would not have been carried out in the Assisted Area concerned.
- 22** GBI may only be awarded if it has an incentive effect. GBI shall be considered to have an incentive effect if, before work on the project has begun, the awarding authority has verified that documentation prepared by the beneficiary establishes one or more of the following criteria:
- a) material increase in the size of the project due to the aid;
  - b) a material increase in the scope of the project due to the aid;

- c) a material increase in the total amount spent by the beneficiary on the project due to the aid;
- d) a material increase in the speed of completion of the project concerned; or
- e) that the project would not have been carried out as such in the deprived area concerned in the absence of the aid.

## **2.7 Investment aid**

**23** GBI to companies operating in Assisted Areas and GBI (SME) support to SMEs operating in Tier 3 areas are both considered to be investment aid schemes by the Commission. In order to be considered an eligible cost for the purposes of GBI, investments shall consist of the following:

- a) an investment in tangible and/or intangible assets relating to the setting-up of a new establishment, the extension of an existing establishment, diversification of the output of an establishment into new additional products or a fundamental change in the overall production process of an existing establishment, or
- b) the acquisition of the capital assets directly linked to an establishment, where the establishment has closed or would have closed had it not been purchased, and the assets are bought by an independent investor. In the case of business succession of a small business in favour of family of the original owner(s) or in favour of former employees, or in the case of a management buyout under market conditions of a business of any size, the condition that the assets be bought by an independent investor shall be waived.

The sole acquisition of the shares of an undertaking does not constitute investment.

### ***Expenditure associated with tangible and intangible assets***

**24** In order to be considered eligible costs for the purposes of GBI tangible or intangible assets must be purchased from third parties under market conditions, without the acquirer being in a position to exercise control, within the meaning of Article 3 of Council Regulation (EC) No 139/2004 on the control of concentrations between undertakings (the EC merger Regulation, see Annex A), on the seller or vice versa. Self built assets, or tangible assets acquired from other companies within the same group are considered to fulfil the conditions of this paragraph if the assets are independently valued.

**25** The investment must be maintained in the recipient region for at least five years, or three years in the case of SMEs, after the whole investment has been completed. This shall not prevent the replacement of plant or equipment that has become out-dated due to rapid technological change, provided that the economic activity is retained in the region for the minimum period.

**26** In order to be considered eligible costs for the purposes of GBI, intangible assets shall fulfil the following additional conditions:

- a) they must be used exclusively in the establishment receiving the aid; and
- b) they must be regarded as amortizable assets.

**27** Expenditure on the purchase of transport equipment (movable assets) is not eligible for GBI support.

**Expenditure associated with job creation**

- 28** In order to be considered an eligible cost for the purposes of GBI, employment must be directly created by an investment project and fulfil the following conditions:
- a) employment shall be created within three years of completion of the investment;
  - b) the investment project shall lead to a net increase in the number of employees in the establishment concerned, compared with the average over the previous twelve months; and
  - c) the employment created shall be maintained during a minimum period of five years in case of large enterprise and a minimum period of three years in case of SMEs.

**Large investment projects**

- 29** Regional investment aid for a large investment project (see Annex A) is subject to an adjusted regional aid ceiling on the basis of the scale set out in Table A. Thus, the aid ceiling for a project with eligible expenditure of €125m located in an Assisted Area with a 15% intervention rate would be:

$$\begin{aligned}\text{Aid ceiling} &= 15\% \times (\text{€}50\text{m} + (0.5 \times \text{€}50\text{m}) + (0.34 \times \text{€}25\text{m})) \\ &= \text{€}12.525\text{m}\end{aligned}$$

**Table A:** Regional aid ceiling adjustments for large investment projects

Eligible expenditure	Adjusted aid ceiling
Up to €50m	No reduction 100% of regional aid ceiling
For the part between €50m and €100m	50% of regional aid ceiling
For the part exceeding €100m	34% of regional aid ceiling

- 30** The adjusted regional aid ceiling must be calculated on the basis of official exchange rates on the date of the grant of aid. These can be found at:

[http://ec.europa.eu/unitedkingdom/work\\_with\\_eu/rates/index\\_en.htm](http://ec.europa.eu/unitedkingdom/work_with_eu/rates/index_en.htm)  
[http://ec.europa.eu/unitedkingdom/work\\_with\\_eu/rates/index\\_en.htm](http://ec.europa.eu/unitedkingdom/work_with_eu/rates/index_en.htm)

- 31** In order to prevent a large investment being artificially divided into sub-projects, a large investment project will be considered to be a single investment project when the investment is undertaken in a period of three years by the same undertaking or undertakings and consists of fixed assets combined in an economically indivisible way.<sup>2</sup>

**2.8 GBI in Tier 1 and Tier 2 areas**

- 32** GBI support may only be granted in regions eligible for regional aid, as set out in the regional Assisted Areas aid map for the period 2007 – 2013.
- 33** The aid intensity in present gross grant equivalent shall not exceed the regional aid threshold which is in force at the time the aid is granted as set out in the regional Assisted Areas aid map for the period 2007 – 2013.
- 34** With the exception of aid granted in favour of large investment projects and regional aid for the transport sector, the thresholds fixed in paragraph 33 may be increased by 20% for aid awarded to small enterprises and by 10% for aid awarded to medium-sized enterprises.

<sup>2</sup> Technical, functional and strategic links and the immediate geographical proximity are factors that will be taken into account to assess whether an initial investment is economically indivisible.

### ***Aid intensity for projects with investment and employment***

- 35** The thresholds fixed in paragraph [33](#) shall apply to the intensity of the aid calculated either as a percentage of the investment's eligible tangible and intangible costs or as a percentage of the estimated wage costs of the person hired, calculated over a period of two years, for employment directly created by the investment project or a combination thereof, provided that the aid does not exceed the most favourable amount resulting from the application of either calculation.

### ***Acquisition of an establishment***

- 36** In the case of acquisition of an establishment, only the costs of buying assets from third parties shall be taken into consideration, and only where the transaction has taken place under market conditions, without the acquirer being in a position to exercise control (see Annex A) on the seller, or vice versa. Where the acquisition is accompanied by other investment, the costs relating to the latter shall be added to the cost of the purchase.
- 37** Costs related to the acquisition of assets under lease, other than land and buildings, shall only be taken into consideration if the lease takes the form of financial leasing and contains an obligation to purchase the asset at the expiry of the term of the lease. For the lease of land and buildings, the lease must continue for at least five years after the anticipated date of the completion of the investment project or three years in the case of SMEs.
- 38** Except in the case of SMEs and takeovers, the assets acquired shall be new<sup>3</sup>. In the case of takeovers, assets for the acquisition of which aid has already been granted prior to the purchase shall be deducted. Where the asset is land and/or buildings that have not been acquired but leased, previously granted state aid does not have to be deducted for the expired part of the period over which the lease was capitalised for the purpose of calculating eligible expenditure.
- 39** For SMEs, the full costs of investments in intangible assets may also be taken into consideration. For large enterprises, such costs are eligible only up to a limit of 50% of the total eligible investment costs for the project.

### ***Aid for the processing and marketing of agricultural products***

- 40** By way of derogation from paragraphs [33](#) and [34](#), the maximum aid intensities for investments in the processing and marketing of agricultural products listed in Annex I of the EC Treaty (see Annex C) are:
- a) 50% of eligible investments in Tier 1 regions and 40% of eligible investments in Tier 2 regions, if the beneficiary is a SME; and
  - b) 25% of eligible investments in Tier 1 regions and 20% of eligible investments in Tier 2 regions, if the beneficiary has less than 750 employees and/or less than €200m turnover, calculated in accordance with Annex [B](#).

### ***GBI aid for newly created small enterprises***

- 41** GBI aid in favour of newly created small enterprises may be provided at the aid intensities set out in paragraph 45 and in relation to a broader range of eligible costs if the provisions in paragraphs [42](#) to [45](#) of these Guidelines are fulfilled.
- 42** The beneficiary shall be a small enterprise.

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<sup>3</sup> Assets must be new to the company and must not replace existing assets.

- 43** The aid amount shall not exceed:
- a) €2 million for small enterprises located in Tier 1 regions;
  - b) €1 million for small enterprises located in Tier 2 regions.
- 44** Annual amounts of aid per undertaking shall not exceed 33% of the amounts of aid laid down in paragraph 43.
- 45** The aid intensity shall not exceed:
- a) in Tier 1 regions 35% of eligible costs incurred in the first three years after the creation of the undertaking, and 25% in the two years thereafter;
  - b) in Tier 2 regions 25% of eligible costs incurred in the first three years after the creation of the undertaking, and 15% in the two years thereafter.
- 46** The eligible costs shall be legal, advisory, consultancy and administrative costs directly related to the creation of the small enterprise, as well as the following costs, insofar as they are actually incurred within the first five years after the creation of the undertaking:
- a) interest on external finance and a dividend on own capital employed not exceeding the reference rate;
  - b) fees for renting production facilities/equipment;
  - c) energy, water, heating, taxes (other than VAT and corporate taxes on business income) and administrative charges;
  - d) depreciation, fees for leasing production facilities/equipment as well as wage costs, provided that the underlying investments or job creation and recruitment measures have not benefited from other aid.
- 47** Small enterprises controlled by shareholders of undertakings that have closed down in the previous 12 months cannot benefit from aid of this type if the enterprises concerned are active in the same relevant market or in adjacent markets.

## **2.9 GBI in Tier 3 areas**

- 48** GBI (SME) investment aid in favour of small and medium-sized enterprises operating in Tier 3 areas shall be compatible with EC State Aid rules, provided that the conditions laid down in paragraphs 49 to 51 are fulfilled.
- 49** The gross aid intensity shall not exceed:
- a) 20% in the case of small enterprises;
  - b) 10% in the case of medium-sized enterprises.
- 50** The eligible costs for the purposes of determining the aid ceiling for the investment project shall be the following:
- a) the cost of investment in tangible and intangible assets; or
  - b) the estimated wage costs of employment directly created by the investment project, calculated over a period of two years.
- 51** By way of derogation from paragraph 50 the maximum aid intensity for investments concerned with the processing or marketing of agricultural products shall be 40% of the eligible costs.
- 52** SME investment and employment aid is limited to €7.5m per undertaking per investment project.



## **2.10 GBI aid for small enterprises newly created by female entrepreneurs**

- 53** GBI aid in favour of small enterprises newly created by female entrepreneurs shall be compatible with EC State Aid rules provided that the conditions laid down in paragraphs [54](#) to 58 are fulfilled.
- 54** The beneficiaries shall be small enterprises newly created by female entrepreneurs (see Annex [A](#)).
- 55** The aid amount shall not exceed €1 million per undertaking.
- 56** Annual amounts of aid per undertaking shall not exceed 33% of the amounts of aid laid down in paragraph [55](#).
- 57** The aid intensity shall not exceed 15% of eligible costs incurred in the first five years after the creation of the undertaking.
- 58** The eligible costs shall be legal, advisory, consultancy and administrative costs directly related to the creation of the small enterprise, as well as the following costs, insofar as they are actually incurred within the first five years of the creation of the undertaking:
- a) interest on external finance and a dividend on own capital employed not exceeding the reference rate;
  - b) fees for renting production facilities/equipment;
  - c) energy, water, heating, taxes (other than VAT and corporate taxes on business income) and administrative charges;
  - d) depreciation, fees for leasing production facilities/equipment as well as wage costs, provided that the underlying investments or job creation and recruitment measures have not benefited from other aid;
  - e) child care and parent care costs including, where applicable, costs relating to parental leave.
- 59** Small enterprises controlled by shareholders of undertakings that have closed down in the previous 12 months cannot benefit from aid under this Article if the enterprises concerned are active in the same relevant market or in adjacent markets.

## **3 National criteria related to GBI**

### **3.1 Policy restrictions**

- 60** GBI is a discretionary programme. Sections 7 and 8 of the Industrial Development Act 1982 do not provide automatic qualifying criteria. In order for a project to be eligible for a GBI grant it must comply with all of the following national criteria in addition to the EC rules described in Section [2](#).
- 61** In addition operating departments must make an assessment of the overall quality of the project in order to provide a basis for judging the level of assistance that will deliver value for money for the UK. In principle, the higher the quality of the project the more assistance can be offered (according to need). The quality factors that should be considered include: the number of jobs created or safeguarded; the salaries and skill levels of these jobs; the value of research and development and training, and the amount of productivity improvement.



- 62** GBI support can be awarded to companies, partnerships or sole traders. In these Guidelines the term “company” includes all legal vehicles for carrying on business (including partnerships, limited liability partnerships, sole traders and companies registered in other jurisdictions as well as limited liability companies registered in Great Britain) unless the context dictates otherwise

### ***Additionality***

- 63** The applicant must be able to demonstrate convincingly that without GBI assistance the project would not go ahead at all in the disadvantaged area, or in exceptional cases, would go ahead on a smaller scale.

### ***No prior start***

- 64** If work on a project has started then it is ineligible for GBI support. An application for assistance must be submitted and an offer made before work on the project is started. “Start of work” is defined in Annex [A](#).

### ***Jobs***

- 65** All investment projects must create or safeguard sustainable jobs.<sup>4</sup> Projects which are likely to create over-capacity and/or displace jobs from another Assisted Area elsewhere in the UK do not qualify for aid. Relocation projects will not normally qualify for GBI support unless the relocation involves a significant increase in net employment.
- 66** The ratio of grant to jobs created/safeguarded must be below the delegated cost per job threshold.
- 67** Where aid is calculated on the basis of the investment cost of a project the fixed capital and/or jobs created/safeguarded by the project (depending upon the type of offer) must be maintained for a minimum of 5 years (3 years for SMEs) after the first payment or 18 months after the last payment whichever is longer.
- 68** Where aid is calculated on the basis of wage costs EC State Aid rules (paragraph [28](#)) specify that the job creation associated with the project must occur within three years of project completion (see Annex [A](#)) and each job must be maintained for a minimum period of five years in the case of employment by a large company and three years in the case of employment by a SME.

### ***Productivity & Skills***

- 69** An investment project must deliver an improvement in productivity, based on the growth of gross value added (GVA) per full-time equivalent (FTE) employee against the sector and national averages; in addition the majority of the jobs must be at NVQ level 2 (or equivalent) or above.

### ***Viability***

- 70** The company undertaking the investment project must be viable and the project must have a good chance of being self-sustaining by the completion of the investment.

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<sup>4</sup> The only exception to this rule is in the case of a grant of less than £100,000 to a SME. In this situation the jobs requirement can be waived at the discretion of the relevant RDA.

### ***Funding***

- 71** GBI is funding of last resort. The applicant should normally have exhausted all alternative sources of funding before applying for a GBI grant. In England the minimum amount of GBI support is £10,000.

### ***National and regional benefit (efficiency)***

- 72** All projects should contribute positive benefits to both the regional and national economy. The impact of the proposed investment on existing businesses must be considered during the assessment of any application for GBI support.

### **3.2 National sector restrictions**

- 73** In addition to the EC sectoral restrictions set out in Section [2.2](#) the national restrictions set out in Section [3](#), may limit the provision of GBI in certain sectors.
- 74** In situations where there is an inconsistency between EC restrictions and the objectives of the GBI scheme the EC restrictions take precedence.
- 75** National sectoral restrictions should not be interpreted in a mechanistic way. Rather they should be read within the context of the policy objectives of the GBI scheme. For example, a company with an investment project to produce bio-fuel from waste material should be able to apply for GBI support even though the energy market is regulated and the project is unlikely to have any impact on end users (i.e. the price of energy will not change). This is because the project is not primarily concerned with energy generation but waste disposal. In this type of situation case officers must determine what market need the project is addressing, with the test being what type of business would step in if the project did not go ahead. In the example above: an energy generation business or a waste disposal business?
- 76** In all cases, to qualify as a commercial activity at least 50% of income or profits must be derived from business trading.

### ***Local consumer-type service activities***

- 77** Projects that involve retailing or other local consumer-type activities will not normally qualify for assistance. This is because local consumer-type projects are not mobile, involve primarily routine low risk investment and do not provide significant regional or national benefit.

### ***Mining and construction***

- 78** Special care needs to be taken over the permanence of employment in mining and construction projects. Individual construction projects should not normally be assisted but a project to expand the workforce of a construction company on a permanent basis would be eligible.

### ***Tourism***

- 79** Tourism projects, for example B&B projects, hotels etc may qualify but displacement considerations will frequently lead to ineligibility. Projects would not normally qualify where finance is still available under section 4 of the Development of Tourism Act 1969. Applications should be referred to the appropriate Tourist Board for market advice.

### ***Charitable organisations***

- 80** Activities undertaken by charitable organisations and other similar bodies may qualify providing they are of a commercial nature.

### ***Franchise operations***

- 81** By their nature franchise operations will not normally qualify. The length of the franchise, viability, control over the business and displacement are among the issues which need careful scrutiny. Legal advice should be sought if there is any uncertainty about the terms of the franchise agreement being compatible with the national policy objectives of the GBI scheme.

### ***Health service***

- 82** Applications involving hospital or medical services and residential care are ineligible for assistance. The primary health care sector is considered to be fully supplied by the National Health Service and its relationships with, and other funding for, private sector providers.

### ***Defence***

- 83** Applications for projects in the defence sector are normally ineligible for assistance. The defence sector is considered to be fully supplied by the Armed Services and their associated private sector providers.

### ***Educational***

- 84** Projects by schools or colleges are unlikely to qualify. The schools sector is considered to be fully supplied by the Department for Children, Schools and Families and its relationships with, and other funding for, private sector providers. Universities should be treated as private sector organisations.

### ***Energy generation***

- 85** These projects are unlikely to satisfy national GBI criteria. Energy markets are regulated and projects often serve only regional/local markets. There are also separate, substantial funding schemes for some segments, for example off-shore wind farms.

### ***Tobacco***

- 86** The projects involving the manufacture of tobacco related products are unlikely to qualify for GBI support as this market is considered to be fully supplied in Great Britain.

## **3.3 Companies controlled by the public sector**

- 87** Projects undertaken by nationalised industries and companies where the public sector has full or majority ownership (for example: the Post Office, British Nuclear Fuels Ltd, London Transport and the Civil Aviation Authority) may be eligible for assistance. HMT approval must be sought on a case by case basis where the project involves mainstream activities, or the statutory duties of the applicant in question.

- 88 In deciding a particular case, HMT will have regard to the extent to which the applicant is dependent on Government for day-to-day financial support, the degree of privatisation envisaged or achieved, and whether or not the mainstream activities involve trading on a commercial basis in competition with the private sector.
- 89 Applications where HMT approval does not have to be sought are those relating to projects involving non-mainstream activities or joint ventures, and projects with minority public sector share. These will be considered on the same basis as applications from private sector firms.

# Part II:

## Project appraisal

- 90** The purpose of project appraisal is to ensure that investment aid is provided only to projects that, for example, would not have gone ahead in a disadvantaged area without the aid, that have a good chance of becoming sustainable, and that provide a net benefit to the wider economy.
- 91** Sections [4](#) to [9](#) describe how GBI applications should be appraised. These sections set out:
- the operational requirements associated with the appraisal process;
  - procedures for processing applications for GBI support;
  - advice on how applications should be assessed against the policy objectives of the GBI scheme and other factors; and
  - guidance with regard to determining the level and form of GBI assistance.

### 4 Operational requirements

- 92** There are a number of operational requirements associated with the appraisal of GBI applications. These are designed to ensure that the appraisal is fair, auditable and transparent.
- 93** GBI applications must be assessed on a case by case basis against the criteria set out in these Guidelines. Operating departments and RDAs should note that:
- a) a case officer must be assigned to lead on each assessment. The case officer must be an official directly employed by the operating authority. Case appraisals must not be contracted out to a private sector body;
  - b) the assessment of GBI applications involves matters of judgement and therefore case officers should not be mechanistic in their application of these Guidelines;
  - c) the assessment should provide the minimum depth of appraisal and impose the lightest possible burden on the applicant company consistent with reasonable administration, taking into account the public expenditure at risk;

- d) before starting an appraisal, case officers must establish whether there are any EC or other restrictions which may preclude or restrict the offer of assistance to firms in the sector concerned.

#### 4.1 Cases less than £250,000

- 94** Case officers are expected to negotiate on all cases, regardless of size, in order to establish the minimum necessary assistance. However, case officers should take account of the level of assistance requested in these negotiations. The efficiency test also should normally be satisfied on a qualitative test. Similarly, the depth of assessment of viability can be reduced, omitting the need for accountancy advice. Where the business has no track record, the forecasts in the application form should be scrutinised more carefully.

#### 4.2 Cases over £250,000

- 95** Where the application is for an amount greater or equal to £250,000 it is mandatory for the case officer to seek:
- market advice from BERR and, if relevant, other departments;
  - accountancy advice from an internal or external adviser, the latter subject to the normal rules on public appointments, including safeguards on conflicts of interest;
  - the advice of the relevant Regional Industrial Development Board (RIDB)<sup>5</sup>.

#### 4.3 Cases over £2m

- 96** Applications for grants of £2m or more must be assessed by the Corporate Finance Practice (CFP) at BERR.
- 97** In order to provide an efficient service to applicant companies, RDAs should inform CFP at the earliest possible opportunity if the application is likely to exceed £2m. CFP will work with the applicant companies and other public sector interests from as early a point as possible. In the event of direct receipt of an application for £2m or over, CFP will advise the relevant RDA and seek their involvement as soon as possible, eg in providing the regional perspective for the appraisal.
- 98** Ministerial approval is required for all cases appraised by CFP, following their consideration by the Industrial Development Advisory Board. Approval is sought from the Minister of State for cases where the amount of support is less than £5m, and from the Secretary of State where the amount of support is greater than £5m.

#### 4.4 Time to appraise applications

- 99** Where the application is for less than £250,000 it should be appraised within 20 working days of receipt of a fully documented application.
- 100** Where the application is for £250,000 or more the case papers for the relevant Industrial Development Board should be prepared within 30 working days of receipt of a fully documented application. Applications should normally be considered by the relevant Industrial Development Board at the first scheduled meeting after the preparation of the case papers.

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<sup>5</sup> Or an equivalent successor body, if appropriate.

- 101** A fully documented application is an application that includes all information relevant to the appraisal of the project. If the case officer has to seek information from the applicant company that should have been included the application the appraisal period should be restarted.
- 102** When a fully documented application is received, written confirmation should be sent to the applicant referring to a named individual, normally the case officer, who will be responsible for the case. If the application is not fully documented the applicant should be informed quickly that the appraisal procedures will not begin until the missing information is provided.

#### **4.5 Record keeping and Freedom of Information**

- 103** In order to meet the requirements of the Freedom of Information Act 2000 reasons for decisions about applications and claims must be recorded properly on file at all stages. This record keeping will also ensure that there is a clear audit trail for all applications. Administrative records should be maintained for all applications irrespective of whether they were successful.
- 104** Guidance for case officers on the Freedom of Information Act can be found at:
- <http://www.foi.gov.uk/practitioner/index.htm>

#### **4.6 Non-disclosure and tripartite agreements**

- 105** Case officers are sometimes asked to sign non-disclosure agreements or tripartite agreements regarding commercially sensitive information contained in applications for GBI support.
- 106** Case officers should not sign non-disclosure or tripartite agreements.
- 107** If necessary case officers should inform applicant companies that information provided in confidence is exempt information under the terms Article 41 of the Freedom of Information Act 2000, and that the operating department will respect its confidentiality.

#### **4.7 Publicity and disclosure of information**

- 108** Operating departments and RDAs are responsible for electronically publishing information on GBI grant offers greater than £75,000. Publication should occur in the quarter following the payment of the first instalment of the grant. The published information should contain the name and location of the recipient of the GBI grant, the size of the grant offered, and the following caveat should be appended to the table:

*The grants listed here represent offers of discretionary financial support linked to specific investment projects. Payment of these grants is dependent upon agreed investment and/or employment milestones being achieved by the recipient.*

- 109** Aggregated information on GBI grants is also presented in the Industrial Development Act 1982 Annual Report to Parliament published by The Stationery Office.

- 110** Other requests for the disclosure of information should be dealt with under the provisions of the Freedom of Information Act.

### ***Early publicity***

- 111** It may be appropriate or desirable to publicise a GBI project before payment of the first instalment of a grant, for example at acceptance of a grant offer. Such publicity should only take place with the agreement of the applicant company. In England cases where the grant awarded is £2m or more should not be publicised without the prior agreement of BERR.
- 112** Case officers may come under pressure from Members of Parliament to release information on the latest offers in their area in advance of the agreed procedure for publication after the first payment. It is acceptable to provide information on offers in advance of payment in summary form providing there are a sufficient number of cases to conceal information relating to individual companies.

### ***Information on payments***

- 113** Exceptionally, if there is a strong case on grounds of public accountability, information on payments may also be published. Information received from applicants is to be treated as commercially confidential but the operating departments reserve the right to disclose details to other government departments if the applicant also applies for assistance from another department.

## **5 Processing GBI applications**

### **5.1 Application stage**

- 114** The application form and its appendices request the following information:
- a) a description of the project outlining its purpose and rationale, the product, the manufacturing process to be used, market objectives, its relationship to the company's existing operations, and employment projections for up to five years;
  - b) a breakdown of the capital costs by year in which they are likely to arise;
  - c) audited accounts (if appropriate) for the last two/three years, more recent management or unaudited accounts if available and group accounts if appropriate;
  - d) cash flow and forward trading estimates compared with an alternative;
  - e) details of how the project is to be financed;
  - f) the rate of inflation assumed in future years; and
  - g) curricula vitae for all directors and other key personnel;
  - h) information on the company's markets and on the identity and location of competing firms.

### ***Financial appendices***

- 115** To help reduce delay and aid appraisal, standard financial appendices should be supplied to all applicants. Applicants do not have to complete these appendices if they can provide equivalent information in a different form. The underlying principle is to make the minimum demand on the company consistent with a fully reasoned judgement on the application.



- 116** Where the amount of GBI assistance requested is £2 million or above the following additional information covering year by year, the expected life of the project (up to a maximum of 10 years) is required to enable a Full Economic Appraisal (FEA) to be carried out:
- a) the additional sales associated with the project (indicating whether they are on an accrual or payments basis). Sales should be split between exports and the domestic market;
  - b) the labour costs of the project (including employers' national insurance and any pension fund contributions);
  - c) the value of bought-in goods and raw materials (if possible, net of VAT and import duties) indicating the proportion of imports;
  - d) the value of any other current expenditure, for example administrative and management charges, insurance premiums, rates, or utility costs; and
  - e) the value of any increase or decrease in working capital.
- 117** The fixed capital expenditure data should be broken down (as far as possible), year by year, into land, work on existing buildings, new buildings, UK plant and machinery, foreign plant and machinery vehicles and any other fixed capital expenditure. The figures should state the full cost of the asset. Wherever possible, the company's provisions for depreciation should also be provided.
- 118** The inflation factors used in preparing the above forecasts should also be clearly stated.
- 119** Where comprehensive forecasts cannot be given about the later years of the project, the analysis should be based on figures for a representative year when the project is fully on stream and there is a stable cash flow.

### ***Projects replacing undertakings destroyed by fire or other disaster***

- 120** Where a project is a replacement of an undertaking destroyed by fire or some other disaster it is important to ensure that assistance is not provided for the same jobs or costs twice. Guidance related to case appraisal in these circumstances is presented in Annex F.

## **5.2 Case handling**

- 121** The default approach to handling applications for GBI assistance should favour simplicity and clarity. Case officers should strive to maintain clear lines of communication with the applicant company. It is appropriate for case officers to indicate the approximate level of assistance that might be available for a project as soon as the case officer has enough information to make a judgement. The normal approach should be to quote a range of assistance (the historical average is 5-15% of fixed project costs) and average historic cost per job for the types of jobs associated with the project.
- 122** At an early stage case officers should stress that support will only be available if the project satisfies the GBI criteria, that GBI support is normally underwritten by, for example, a parental or bank guarantee, that any grant will be phased, and that payment will only be made when specific audited milestones are reached.
- 123** Case officers should assess applications against the criteria set out in Section 3. Section 6 provides guidance on applying these criteria in practice.

**Third party advice to applicants**

- 124** It is not uncommon for third parties such as consultants to advise companies with regard to GBI applications, or even provide information on behalf of the applicant. If the third party continues to play an active role in the application after the application form has been submitted the case officers should request that the applicant company designate an in-house point of contact. All correspondence regarding the appraisal of the GBI case should then be copied to this company contact. It is the responsibility of the applicant to ensure that any information submitted on its behalf is accurate and complete. It may be difficult to incorporate changes late in the appraisal process.
- 125** If the case officer believes that information provided by third parties is not a true and fair reflection of the business plan of the company then the case officer has a duty to:
- request confirmation from the applicant company that the data presented in the application form and financial appendices is accurate and reflects their business model; and
  - ensure that the final recommendation regarding the application records these concerns.

**5.3 Accountancy advice**

- 126** Where a case officer obtains advice from an accountant there must be a clear understanding about the respective roles. The case officer must continue to retain the leading responsibility for the case and, in the main, accountancy input will relate to the financial appraisal and consideration of the applicant company's viability. However, accountants can make a valuable input on additionality issues and negotiations with applicants on assistance levels. Where possible they should be encouraged to do so but final responsibility for assessing additionality and reaching a judgement on the case as a whole must remain the responsibility of the case officer.

**5.4 Consultation on the market aspects of applications**

- 127** Market advice must be sought for all applications for £250,000 and over and/or applications of any size where EC restrictions may apply. Case officers should take a robust line in dealing with applications from sensitive sectors. Market advice should be demonstrably fact based and should:
- comment on the present and prospective market for the products and services expected to arise from the project; this analysis should be at the industry sub-class (4-digit SIC code<sup>6</sup>) level and at the sector level;
  - comment on the applicant's forecasts (as set out in the GVA spreadsheet; and the impact on the market (or markets) of absorbing the forecast output;
  - consider whether or not the project appears viable and well-based and whether the processes, equipment, material/component supplies, sales channels, customer profile, and the like, are appropriate to the proposition;
  - consider the implications for displacement of jobs in other companies as a result of the project proceeding; and
  - comment on any wider benefits that are likely to accrue to the economy from the project, both up and down the supply chain.

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<sup>6</sup> Standard Industrial Classification (SIC 2003) of economic activity (see Annex G).

- 128** The case papers prepared for the Industrial Development Board must reflect the market advice received. If a case officer proposes a course of action which differs substantially from recommendations made by the market analyst, the latter should be given the opportunity to comment on the wording of the case papers before they are presented to the Industrial Development Board and to attend the Board meeting.

### **Feedback**

- 129** Market advisers should be informed of the decisions taken in all cases where they have provided advice. The information is invaluable to future assessments and for maintaining a sector database.

## **5.5 Indicative offers**

- 130** It is not good practice to provide indicative offer letters. Exceptionally, because of timing or competitive pressures it may be necessary to provide an indicative offer of support before full appraisal of an application has taken place. RDAs must consult with BERR before an indicative offer letter is issued. Ministerial agreement will be required if the quantum of grant in an indicative offer is greater than £2m.
- 131** Where the use of an indicative offer is approved a letter should be sent to the applicant making clear that the offer is subject to a full appraisal to establish that the project justifies the indicated level of support. Reference should also be made to Ministerial and Industrial Development Board approval if appropriate.
- 132** Before issuing an indicative offer the operating department must gather enough information about the project and applicant company to make a judgement about how likely it is for the application to be supported. Indicative offers must not be issued where there is significant doubt about whether the application will be successful.
- 133** In addition to a broad assessment of the project against the normal criteria the value of an indicative offer should take into account the following:
- location of the project and average levels of support;
  - comparable similar projects in terms of size of company, size of project product;
  - early indications about the quality aspects of the project; and
  - the total funding package including the level of other public sector support.

## **5.6 Other government and public sector assistance**

- 134** GBI support is provided as assistance of last resort. In theory this means that all other sources of funding (including public sector funding) should be exhausted before a GBI application is made. In practice a “package” of public funding that includes an element of GBI may be co-ordinated according to the specific needs of the applicant company.

### **Cumulation**

- 135** The Government provides assistance to business through a wide range of programmes and care must be taken to ensure there is no unintentional dual funding of projects. In almost all cases where aid is offered in

combination with other public sector assistance the total assistance must be cumulated to ensure that aid package is consistent with EU State Aid rules (see Section 2.5). Other public sector assistance will also have a bearing in calculating the minimum amount of GBI support required to win the project.

- 136** If a project receives Launch Investment under the Civil Aviation Act 1982 it will not normally be eligible for GBI except where the case officer is satisfied that the project has a genuine choice of location for the manufacturing stage of the project. In such cases assistance may be provided towards the additional costs to the company associated with the Assisted Area location. In all cases care must be taken not to assist the same costs twice.
- 137** EC funded assistance from the Structural Funds, Objectives 1 and 2, must be cumulated within the relevant regional aid ceiling.
- 138** Where GBI is given to a project involving research and development, the research and development expenditure may not be eligible for a research and development tax credit.

### ***Assistance from local authorities***

- 139** Local authorities have a range of powers under which they provide assistance to industry. This assistance can take a variety of forms, including soft loans, wage subsidies, rent concessions and guarantees, rate holidays and grants for conversion, extensions and new buildings. Where an applicant is seeking such assistance, the amount and nature of that assistance should always be taken into account in determining the minimum level of GBI necessary to secure the benefits associated with the project.

### ***Government financial involvement in companies***

- 140** The involvement of Government (whether by way of a grant, loan, equity or guarantee) in a limited liability company does not alter the position of creditors. Those doing business with such a company have been advised through Parliament that they must act on the assumption that liability for the company's debts will be determined solely in accordance with the normal rules applicable to a limited liability company under the Companies Acts except where the Government undertakes or has undertaken a specific commitment in relation to debts.

## **6 Criteria for assessment**

### **6.1 Location**

- 141** If an application is for GBI support the associated project must be located within a Tier 1 or Tier 2 Assisted Area. The postcode check available on BERR's website<sup>7</sup> will indicate if a particular address falls within a Tier 1 or Tier 2 area and the relevant intervention rate. If an application is for GBI (SME) the company must be a SME located in a Tier 3 area; these are determined by the relevant RDA.

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<sup>7</sup> <http://www.dtistats.net/regional-aa/aa2007.asp>

## 6.2 Additionality

**142** The aim of the additionality criterion is to establish whether assistance is necessary for the project to go ahead at all or whether its quality, scale, timing or location (or any combination of these factors) would justify the provision of assistance.

**143** Analysing the additionality of a potential GBI award is the most important condition for determining whether it would be value for money. The additionality test is an assessment of whether the proposed award will induce undertakings to pursue an investment in a disadvantaged area which they would not otherwise have pursued. In testing the additionality of a GBI award case officers should take into consideration the following elements:

- **Counterfactual analysis:** the change of behaviour has to be identified by counterfactual analysis: what would be the level of intended activity with and without GBI support? The difference of the two scenarios is considered to be the impact of the GBI award and describes the incentive effect.
- **Level of profitability:** if a project would be more profitable at an alternative location outside of a disadvantaged area it is more likely that the GBI will have an incentive effect. Standard financial methodologies should be used to evaluate the overall profitability (or lack thereof) of a project – these may include calculating the Net Present Value (the sum of the discounted expected cash flow resulting from the investment minus the investment cost), the internal rate of return (IRR) or the return of capital employed (ROCE) for the project. Financial reports and internal business plans containing information on demand forecasts; cost forecasts; financial forecasts, documents that are submitted to an internal investment committee and which elaborate on various investment scenarios, or documents provided to the financial markets should be used as evidence.
- **Amount of investment and time path of cash flows:** high start-up investment costs, limited appropriable cash flows and a significant fraction of cash flows arising in the very far future should be considered positive elements in assessing the additionality of a GBI award.
- **Level of risk involved in the project:** GBI will not be additional where a project is low risk (unless there is an alternative location – usually overseas - for the project outside of the disadvantaged area). Project risk should be assessed, drawing on feasibility studies and expert opinions where these are available, and in particular take into account the irreversibility of the investment, the probability of commercial failure, the risk that the project will be less productive than expected, the risk that conducting the project would undermine other activities and the risk that the project costs undermine the undertaking's financial viability.

**144** In assessing additionality the case officer should:

- a) identify what precisely GBI will cause to happen which would not happen without assistance;
- b) challenge why the company considers that GBI is required; and
- c) make a judgement about whether the additionality case is convincing.

- 145** The burden of proof in demonstrating that additionality is satisfied rests on the applicant. Companies should be made aware at the application stage that the project will have to pass an additionality test. Case officers must assess whether the case is convincing and challenge it where appropriate. For example in the case of a large firm which claims that although it has sufficient funds, a project would not go ahead without assistance because it does not meet the firm's internal criteria. Evidence of the implementation of this criterion will be required.
- 146** It is acceptable for companies to base their need for grant on the additional cost of doing business in an Assisted Area. However, case officers have an obligation to test this type of argument.
- 147** If the amount of assistance in prospect is small in relation to project costs, the case officer should consider whether it is credible a grant would make the difference between a positive and negative decision on the project.
- 148** Appraisal should be stringent where subsidiaries claim to be unable to proceed because of internal decision rules, particularly when subsidiaries of large, cash rich companies are involved.
- 149** Finally, case officers should directly address the following questions when appraising an application:
- a) is there evidence that the applicant has explored alternative sources of finance?
  - b) has the applicant company produced a convincing rationale for needing the assistance?
  - c) is the case for any alternative project location credible? Annex H provides guidance for evaluating the credibility of alternative project location claims.

### **6.3 Prior start**

- 150** If work on a project has started then it is ineligible for GBI support. An application for assistance must be submitted and an offer made before work on the project is started.
- 151** If, during the course of an appraisal, it becomes clear that an applicant has incurred, or wishes to incur, expenditure on a project before the operating department has decided whether assistance is justified this would normally nullify the additionality case. However, there are exceptions to the "no prior expenditure" rule, for example research and feasibility work undertaken or planned to help identify the options or secure the possibility of an option.
- 152** A more serious difficulty may arise if the applicant incurs significant expenditure on physical assets associated with the project, for example, on land and buildings or plant and machinery, before the appraisal has been completed. Whilst each application must be treated on its merits, in most cases such commitments or expenditures demonstrate the intention to carry out the project irrespective of assistance and should result in the application being rejected.

### **6.4 Jobs**

- 153** A key objective of regional policy is the creation of sustainable jobs - normally this means jobs that last for at least five years.

- 154** Employment estimates provided by companies should be critically examined. Case officers should satisfy themselves that the number and timing of jobs forecast accords with the investment proposed and the company's existing staffing arrangements or with the normal employment densities for the industry in question. Only jobs created or safeguarded by the applicant company as a direct consequence of the project should be taken into consideration. Indirect employment on the project through sub-contracting of support activities permanently based on site such as maintenance engineers, security and catering staff may sometimes qualify under this standard.
- 155** On occasions staffing of an establishment may be wholly contracted to an independent agency that supplies staff on an individual contractual basis. Providing that the contracts are for a fixed term with the applicant business, such arrangements may qualify for assistance. However, in England such cases must be cleared with BERR. Amongst other things it will be necessary to show that the jobs created will be an integral and permanent part of the project. Temporary employment cannot be considered (although seasonal jobs and jobs that involve distance working may be eligible - see Annex I). Jobs which involve the transfer and/or retraining of existing employees are safeguarded jobs and cannot be considered to be new.
- 156** It is important to specify the exact nature and location of safeguarded jobs within the plant or premises. This should form part of the schedules to the offer letter. Where site or company employment totals are included, case officers should also make clear whether such base employment totals are expected to be preserved as part of the offer.

## 6.5 Productivity and Skills

- 157** The investment project must deliver an improvement in productivity, based on the growth of gross valued added (GVA) per FTE employee against the sector and national averages; in addition the majority of the jobs must be at NVQ level 2 (or equivalent) or above.
- 158** Details of the GVA productivity test are presented in Annex [G](#), and details of the skills test are presented in Annex [L](#).

## 6.6 Viability and sustainability

- 159** Viability means that after receiving assistance, the project/business will become sufficiently profitable for the associated employment to be sustained without further subsidies.
- 160** It is important to establish that a project has a good chance of being viable. However, if public funds can be protected by a bank guarantee or a robust parental guarantee then case officers should consider these in a favourable way.
- 161** Properly analysed financial and commercial data are the foundation of the viability assessment. However, other factors should also be taken into account. These include:
- **Market prospects**  
A realistic appraisal of the market for the applicant company's products, at home and overseas, and of the company's ability to sell in those markets, is essential. GBI support will rarely be justified for projects that only serve declining markets (because it is unlikely that the project would be sustainable) or markets which are over-supplied by existing UK suppliers.



- **Management**

An assessment of the quality of the management of the applicant company is important. An investment project is more likely to succeed and be sustainable if the management of the company are of good quality. Case officers should examine the project plan for the investment project, and probe the company with regard to contingency planning. Curricula Vitae should be obtained for all directors and other key personnel and these should be examined for evidence of successful past project management.

- **Costs**

If the applicant company operates in a sector that is facing or expected to face considerable import penetration the long-term running costs of the project should be analysed critically.

- 162** Ultimately the case officer must make a judgement as to whether the applicant company will be capable of paying its debts as they fall due for the foreseeable future. In many cases this decision will not be clear cut. However, the case officer's view is that there is at least a 50:50 chance that the business will survive in both the short-term, and will be able to deliver sufficient profits to embed the business and related jobs in the region, then support can be offered.

## **6.7 Funding**

- 163** GBI is funding of last resort. The applicant should normally have exhausted all alternative sources of funding before applying for a GBI grant. However, there are some circumstances where it might be appropriate to relax this requirement. Specifically these are:

- where it is necessary to present a package of state support in order to win an investment project for the UK; or
- where the project involves a start-up company.

In the case of a start-up company if there is a question as to whether all alternative sources of funding have been exhausted it may be appropriate to provide GBI support only on a repayable basis and on quasi-commercial terms.

### ***Low risk projects***

- 164** A project that is low risk for the company will not normally justify assistance unless the rationale for support is based on an alternative project location outside of the Assisted Areas. For example, GBI should not be used to support a project to simply acquire land or general purpose buildings, since these assets could be readily realised and therefore involve the company in little risk.

### ***Routine investment***

- 165** GBI should not be provided for routine investment, including routine upgrading of products with a short life span, unless there is convincing evidence that the alternative is to relocate. There should also be a presumption against giving assistance in response to repeated applications relating to one establishment.

### ***Contract bids***

- 166** Assistance should not be offered to underpin a contract bid under the rules of a competitive tender. In addition to the potential distortion of price, the benefit could also be to the detriment of other Assisted Area bidders. Projects based on single contracts also carry more risk with regard to sustainability.



## 6.8 National and regional benefit (efficiency)

- 167** All projects should contribute positive benefits to both the regional and national economy. The impact of the proposed investment on existing businesses must be considered during the assessment of any application for GBI support.
- 168** Assistance must be concentrated on projects which will strengthen the national and regional economy. The factors taken into consideration include the income generated directly by a project, the displacement effects on firms both in and outside the Assisted Areas and the wider benefits to the competitiveness of the economy at large.
- 169** As far as possible the net economic benefits of the project should be quantified. Generally, the depth of appraisal should be related to the size of the project. Annex J sets out procedures for assessing the economic efficiency depending on the size of the potential assistance. These procedures should be applied in all cases where the assistance sought is greater than £250,000. A pass of the efficiency test or the full economic evaluation is a necessary condition before cases can be offered assistance. However, if a case fails the efficiency test it may still pass the full economic evaluation as this will more effectively capture any wider economic benefits associated with the project.

## *Research and development projects*

- 170** Research and development projects involving new capital investment can qualify for assistance even where the nature of their relationship to the parent organisation may mean that an income stream is not readily identifiable for the purposes of the normal viability test. For example the facility may not involve trading. Research and development projects may be either stand-alone operations or part of a wider project. They generally involve quality jobs and offer wider benefits making them attractive proposals for the national economy. Research and development projects that fail the commercial efficiency test should be subject to a full economic appraisal to ensure that all of the benefits of the project are identified.
- 171** Spend on development and building of prototypes is not an eligible cost for the purpose of calculating investment expenditure.

# 7 Other factors

- 172** In addition to the EU and national criteria case officers should take into account the following additional factors when assessing GBI applications.

## 7.1 Credit checks

- 173** Case officers may consider it necessary to carry out checks on individuals or companies. Case officers should note that credit checks on individuals are subject to the Data Protection Act and can only be carried out with the consent of that individual. When seeking that consent the individual must be informed of the identity of the Data Controller and the operating department's Data Protection Officer, the purpose for which the data is required and any other information to enable the processing to be fair (for example, who else will see the information and how long it will be kept). An individual's consent is not required in order to obtain information held on the Insolvency Service's public register, about County Court Judgments or on disqualified directors.

**174** Annex [K](#) presents details on sources of information about UK companies.

**175** Where a director of a company applying for a grant is known to have been bankrupt but is now discharged or has been given permission by the bankruptcy court to be a director, this would not automatically rule out acceptance of the grant application but it is a factor that would have to be taken into account in considering the viability and probity of the applicant company. Where a director was found to be an undischarged bankrupt who was not entitled to be a director of a company, this would be grounds for considering prosecution of the director and would be likely to lead to rejection of the company's grant application.

## **7.2 Phoenix companies**

**176** Case officers should exercise caution when handling applications from "phoenix" companies. Reasons for failure of the previous business should be investigated and special attention should be paid to the viability of the new operation. Checks should also be made into the financial history of the directors involved in the new business.

## **7.3 Projects rejected by another office**

**177** During the appraisal of an application, checks should be made to establish whether the applicant has made a previous approach to any of the operating departments.

**178** Care should be taken to avoid assistance being given unwittingly to a project already rejected by another region. RDAs should consult BERR and other regions concerned where:

- they believe it is likely that a project for which they have refused assistance will be re-submitted to another region, or
- they receive an application for a project for which there is reason to believe (because of the company's location, other regional connections etc) may have been the subject of an application elsewhere.

**179** An application for assistance for a project which has been rejected for assistance in a very similar form by another office requires careful handling because of its potential sensitivity. This is especially so where that rejection has been endorsed by one of the Regional Industrial Development Boards. It will be most unusual for a case rejected by one office to be taken up by another unless substantial revisions to the project have been made.

**180** Before an application in respect of a project which has been refused assistance by another office is put to an Industrial Development Board every effort must be made to reconcile the conflicting views taken on it. Where this cannot be achieved by discussion between officials in the regions concerned, BERR at the request of the receiving office, will seek to "conciliate". If agreement cannot be reached in this way the case must be referred to Ministers in the relevant department(s) with an agreed statement of the facts and a description of the conflicting views.

**181** Where the advice of a Regional Industrial Development Board is sought on a project previously rejected for assistance in another region the case paper should:

- give a summary of the earlier case and of the reasons for it having been rejected;
- indicate what attempts have been made to reconcile differences of view, and what conclusions (if any) have been reached

#### **7.4 Relocation projects**

**182** Assistance is not available for projects which involve the transfer of jobs from one part of Great Britain to another with no net increase in jobs, unless it involves:

- rationalisation programmes, planned by multi-plant enterprises, which involve substantial investment in new equipment or new production at one site and loss of jobs in another, and where, in the absence of assistance, the loss could fall in an Assisted Area;
- concentration of production in a single location by a multi-plant enterprise, where assistance can influence the choice of location.

**183** For a project to be considered for assistance under these exceptions a firm needs to meet the following criteria:

- a) it is a multi-plant enterprise with plants both inside and outside the Assisted Areas;
- b) its plans involve job losses somewhere whether or not assistance is offered;
- c) the offer of assistance would prevent job losses occurring in an Assisted Area location, at the expense of jobs outside of the Assisted Areas; and
- d) the investment must lead to net economic benefits. For example, by encouraging extra modernisation or minimizing net job losses.

**184** Relocation projects which involve a relatively small increase in jobs should be considered particularly carefully:

- a) where the jobs created in the new location are less than 10% above the jobs lost in the old, assistance should not normally be given;
- b) where the new jobs are between 10% and 100% more than those lost and the relocation is from a non-Assisted to Assisted Area, the amount of assistance offered should be calculated on the basis of the net increase in jobs and kept within the level permitted by internal cost per job limits;
- c) where the increase in jobs is more than 100% the normal cost per job limits apply without qualification: i.e. jobs lost outside the Assisted Areas do not need to be netted off since the project is not primarily about relocation.

**185** A company may seek assistance for the replacement of an existing plant by another in a different location, in circumstances where the existing plant will close without replacement in the UK if no assistance is given. Before advantage can be taken of this provision, the company should normally have a firm plan to close the existing plant come what may, supported by convincing evidence of their need to do so. To protect the operating department's public position, firms can be expected to explain to their workforce, and if necessary publicly, that the existing plant must close. In view of the special sensitivities involved, RDAs in England and operating departments in Scotland, Wales and Northern Ireland should consult BERR in all cases which involve companies moving into or out of England. Scottish Executive, Welsh Assembly Government and Northern Ireland Office should consult each other if the movement is between their areas. In addition, RDAs should consult BERR about moves from one English region to another.

**186** In all cases, the normal section 7 efficiency criteria apply, and assistance should not be used to rescue an ailing firm proposing to move to Assisted Area without a gain in efficiency.

## 8 Level of assistance

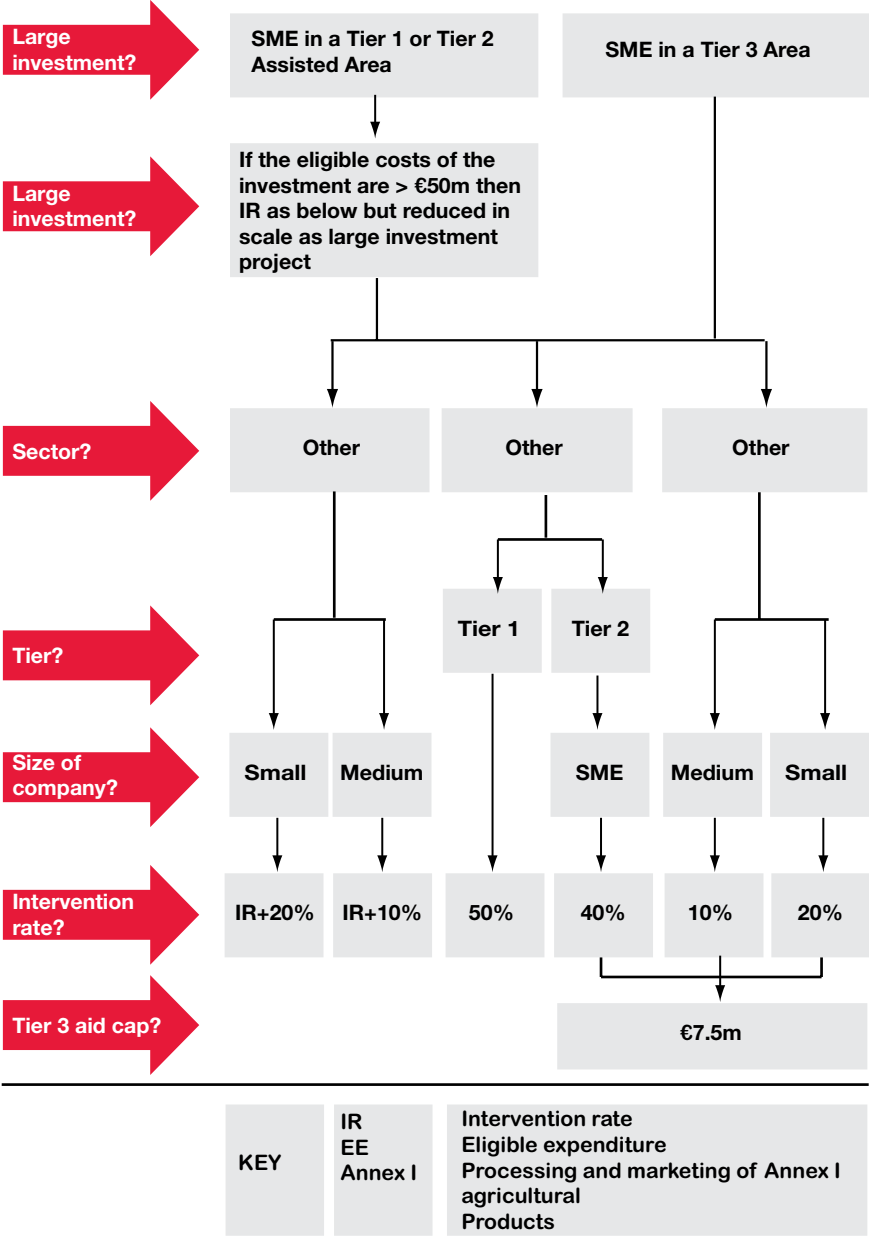
**187** When appraising an investment project the case officer should also make a judgement regarding how much support is appropriate. This amount, which is known as the "quantum", should be the minimum necessary to win the project for the region. Operating departments should note that:

- a) the quantum must not be greater than the maximum permitted by the EU State Aid rules set out in Section 2;
- b) the cost per job for the project must be consistent with the national cost per job ceiling; and
- c) once the level of GBI support has been agreed by the recipient it cannot be revised upwards to reflect increased project expenditure or employment.

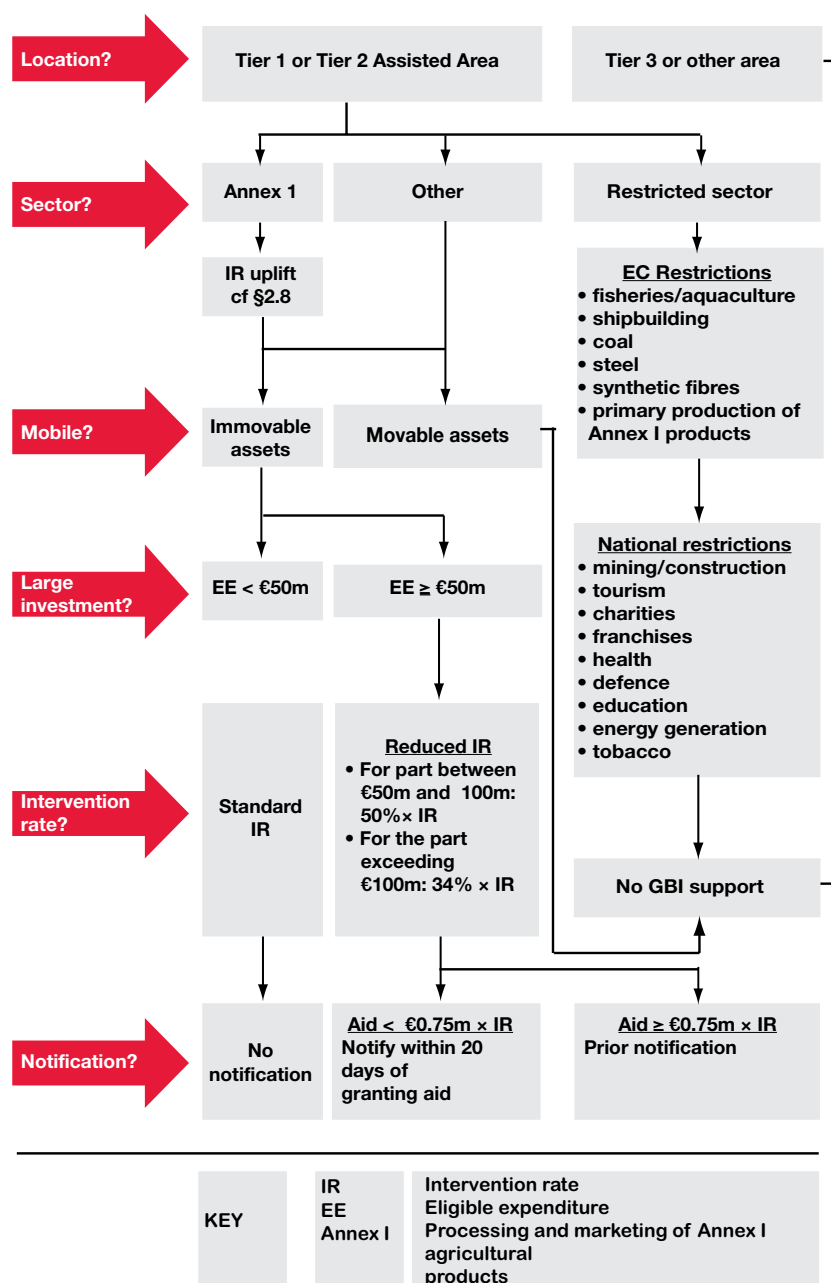
### 8.1 Interpretation of State Aid rules

**188** The flow charts in Figures 2 and 3 simplify the interpretation of State Aid rules with respect to intervention rate, notification threshold and aid ceiling for SMEs and large companies respectively.

**189** These figures should be treated as a guide only, and the text of Sections 2 and 3 and the relevant Commission regulations should be consulted in the case of any uncertainty.



**Figure 2:** Flow chart showing how location, sector, size of company and amount of eligible expenditure affect the amount of GBI support that can be offered to an SME.



**Figure 3:** Flow chart showing how location, sector and amount of eligible expenditure affect the amount of GBI support that can be offered to a large company.

## 8.2 Job quality

**190** Jobs created should be valued more highly than jobs safeguarded on the basis that they represent a genuine addition to existing economic activity. However, this matter is not always clear cut as internationally mobile re-investment, for example upgrading a quality manufacturing process, may deserve the same level of support as a project that creates a similar number of jobs. The judgement needs to fall back on how the project measures against other quality benchmarks.

**191** Wage and skill levels are normally the best measures of job quality. Detailed information on pay scales is obtained at appraisal and this provides a sound basis for assessing job quality. If the level of assistance is not being calculated on the basis of each individual project job, an assessment of average job quality should be made on the basis of the average wage and skill levels for the project compared with historic averages for the sector and the region.

### 8.3 Research and development

- 192** Projects that involve enhanced levels of research and development justify higher levels of GBI support. Where a project involves an in-house research and development facility case officers should estimate the level of research and development expenditure as a proportion of sales over the life of the project and compare this ratio with the average for the sector<sup>8</sup>.
- 193** Similar considerations apply to stand alone research and development centres. In these cases the absence of a direct link to a UK manufacturing base is generally offset by the quality of the work and the pay it attracts. Research and development centres of this kind are very much part of the Knowledge Based Economy and support can be justified even where the project does not satisfy all of the normal scheme criteria. The use of supplemental research and development aid for projects in the Assisted Areas is covered in Annex D.

### 8.4 Training

- 194** New work practices may require a continuous re-skilling of employees. In addition to assessing the quality of work provided by the project, case officers should assess the value of training. This should be done by examining the extent to which a firm is prepared to fund training of employees, thereby adding to the stock of trained labour in the region. The use of supplemental training aid for projects in the Assisted Areas is covered in Annex E.

### 8.5 Other project costs

- 195** Notwithstanding the requirement to secure projects for the minimum quantum, it is important that case officers take into account all additional working capital requirements related to the project and other significant project costs when determining the amount of assistance necessary to support an investment project.
- 196** Once the size of grant has formally been agreed with a company (i.e. the company signs the offer letter) it cannot be revised upwards to reflect additional project costs.

### 8.6 Purchase of assets from a receiver or liquidator

- 197** As Section [2.7](#) indicates, assistance can be provided for the purchase of the assets or, if appropriate, the business of another company in receivership or liquidation where it is clear that there is only one realistic bidder. Such assistance can also be provided if there is a clear and imminent threat to employment even if the firm in question is not in receivership or liquidation. These circumstances apart, assistance should not be provided to one company in order that it might take over another company

## 9 Form of assistance

- 198** GBI has been registered with the European Commission as a “grant only” scheme. GBI support should take the form of a capital grant, payable in instalments triggered by the achievement by the recipient company of specific expenditure and/or job creation milestones that must be set out in the offer letter for the grant.

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<sup>8</sup> The case officer should request sectoral R&D expenditure when requesting market advice.

**199** Although GBI support is delivered via capital grants it is usual for the grant to be recoverable in part or in whole in cases where the project associated with the grant does not satisfy the conditions set out in the offer letter. The prospect of recovery should not influence the assessment of a GBI application.

**200** Alternatively it is acceptable for the grant to be recoverable in part or in whole in cases where the project proves to be particularly profitable for the recipient of the grant. The triggers for this type of royalty payment should be linked to easily observable quantities such as factory output and set out in the offer letter.

## **9.1 Negotiation**

**201** In negotiating the appropriate level of assistance, the case officer should have regard to such factors as the profitability of the project, the degree of risk, the extent to which the project is internationally or nationally mobile and the number of jobs to be created. It is normally helpful to think of the grant in terms of “what it is buying for the UK and for the region.”

**202** Before starting negotiations with a company with regard to the quantum of grant, and the payment triggers, the officer with responsibility for the local GBI budget must approve the maximum level of assistance.

## **9.2 Phasing of grant payments**

**203** Grant payments should be phased in line with capital expenditure and/or job creation. In this way assistance will align with the gross grant equivalent and cost per job targets for the project.

**204** At no time should the amount of grant paid out be greater than the amount of eligible expenditure defrayed by the recipient company.

**205** If the amount of grant is greater than £250,000 then, 20% of the grant should be held back until the completion of the project and the achievement of the productivity target.

## ***Capitalisation of leases related to land and buildings***

**206** EU State Aid rules specify (see paragraph [37](#)) that for a capitalised lease of land and buildings to be regarded as eligible expenditure it must continue for at least five years after the anticipated date of the completion of the investment project or three years in the case of SMEs.

**207** Land and building leases should not normally be capitalised for longer than minimum period specified by State Aid rules, nor should a land and building lease be capitalised over a period where the company has an option to terminate the lease. In unusual situations where it is desirable to capitalise a land and building lease for longer than the minimum specified by EU State Aid rules then the phasing of grant (and therefore the conditions period) should be extended by an equal amount.

## **9.3 Parent guarantee**

**208** When an offer is accepted by a subsidiary within a Group, the subsidiary undertakes obligations to repay any assistance if it defaults on the conditions set out in the offer letter. Although the obligations in the offer letter are for the subsidiary it is standard practice to obtain a parental guarantee where the grant recipient is a subsidiary company. A parental guarantee is not an absolute requirement, but case officers should seek



equivalent alternative security (for example a bank guarantee) if the parent is not prepared to underwrite the investment grant.

- 209** Where the grant cannot be underwritten by a parent guarantee or alternative security, payment should backloaded.

#### **9.4 The offer letter**

- 210** The payment of grant must be linked to the achievement of specific project milestones. The triggers for payments must be negotiated by the operating department and set out in the offer letter. With aid for investment the triggers must be related to the disbursement of capital expenditure and the creation/safeguarding of jobs. With aid for job creation the schedule should be linked to expenditure on salaries. At no stage of the project should the payment of grant exceed the applicant's actual cash expenditure on project assets.
- 211** The offer letter template provides a standardized structure and text. This text is non-negotiable, although it is frequently necessary to add clauses to ensure that all of the conditions associated with the grant are accurately reflected in the offer letter. Legal clearance should be sought for all additions to the offer letter.
- 212** Applicants can be told on the telephone that their application has been approved prior to the issue of the offer letter. However, the offer letter should be issued as soon as practicable after this conversation. The case officer should indicate the level of assistance and draw attention to the conditions associated with the grant. Officers should bear in mind that if, as a result of inaccurate or misleading advice given by telephone (or in writing), an organisation suffers a financial loss, they may take legal action against the operating department concerned.
- 213** In normal circumstances, no publicity should be given to an offer of assistance before the formal offer letter has been signed by the applicant.
- 214** It is sometimes necessary to amend an offer letter after it has been issued. In this case the changes should be set out in a "letter of variation" that should be legally cleared before issue. The letter of variation signed by the recipient must be attached to the original offer letter and stored by the operating department.

# Part III:

## Monitoring

**215** Under section 7 or section 8 of the Industrial Development Act operating departments have a responsibility to obtain enough information to assess the continuing viability of the company and progress of the project, to ensure that the assistance is being used for the purposes for which it was provided and to confirm that related assets and jobs stay in place in accordance with the terms of the offer letter.

**216** Sections [10](#) to [12](#) present guidance on monitoring GBI supported projects. They set out:

- a) the role of the monitoring officer;
- b) the mechanics of project monitoring;
- c) guidance for dealing with changes in projects.

### 10 Role of the monitoring officer

**217** A monitoring officer should be assigned by the operating department or RDA to monitor each project. Monitoring and payment approval functions should not be carried out by individuals involved in the appraisal process. Where a company has more than one supported project in a particular region then a single monitoring officer should be responsible for all the projects.

**218** The essential tasks of the monitoring officer are:

- a) to ensure that public funds are used for the purpose for which they were provided. In England this will include the achievement of productivity and skills benchmarks in addition to the normal capital expenditure and job creation/safeguarding conditions;
- b) to ensure that the company complies with the terms of the offer letter and to give consent to variations where these are justified;
- c) to consider the factors critical to the success of the project and be satisfied about its continuing viability at each stage. The viability of a project should be checked before payment of each instalment of grant. Monitoring officers should make use of accountancy advice as appropriate. Viability reassessment should not be a purely mechanical process and it should be proportionate to the degree of risk associated with the project;
- d) to check whether the project is proceeding according to plan or whether there are substantial variations in its scale, nature or timing;

- e) if there are changes to the project plan, to assess the impact of these changes with regard to the scheme criteria;
- f) to safeguard the operating department's position wherever necessary either by reducing, delaying or withholding payment or by requiring the repayment of part or all of the assistance already provided; and
- g) where a parental undertaking or guarantee has been obtained to monitor the financial status of the parent with regard to the value of that guarantee.

**219** Monitoring officers should rely as far as possible on the information produced for the company's own management purposes and on audited accounts where available. Furthermore, the complexity of additional information required of the company and the monitoring approach used (for example visits and written requests) should be proportionate to the amount of expenditure at risk.

**220** It is vitally important that all contact with companies and the reasons for decisions taken during monitoring are properly recorded on file by the monitoring officer.

**221** It is not the monitoring officer's role to advise the management of the company, but monitoring officers should recognise that they represent a link between the company and Government. Monitoring officers should be ready to provide information on Government services which may be relevant either to the project or the general operations of the company concerned. The basic objective should be to secure the maximum possible benefit from each project consistent with the observation of these Guidelines and the terms and conditions by which assistance has been provided.

## 11 Mechanics of project monitoring

### 11.1 Legal entitlements and administrative practices

**222** Payment under section 7 or section 8 of the Industrial Development Act is made on the basis of a legally binding agreement between the company and the operating department (the offer letter). The terms of the offer letter, once accepted by the company, impose legally enforceable obligations on both the company and the operating department. Monitoring officers should ensure that the company's rights are properly observed. Similarly, in negotiating any reduction or repayment of assistance with a company in the event of it being in default of its obligations, monitoring officers must make the legal basis for the action clear to the company. It follows that monitoring officers should consider at an early stage whether legal advice is needed. Where an applicant's legal entitlement to some financial or other benefit has been established, that entitlement must be met.

**223** For all cases, appraisal officers have limited discretion to vary the time period between payments. Monitoring officers may seek authority to bring forward or otherwise vary payments where progress on cases justifies it. Where payments are brought forward the changes must be set out in a letter of variation agreed with the recipient company.

### 11.2 Processing of claims for payment

**224** Claims for payment must be made on the claim form provided by the operating department. The information supplied in support of each application for payment should be carefully examined by the monitoring officer against the offer letter in line with local desk instructions.

In England, RDAs also have responsibility for approving, on behalf of BERR, claims where the grant awarded is £2m or more. RDAs are required to forecast impending claims and notify BERR in advance to enable the release of funds.

### **11.3 Monitoring of additionality**

**225** The case paper for the investment project will record the reason why the company applied for GBI, i.e. the grounds for additionality. This is established at the point at which the appraisal is made and there is normally no need to monitor additionality unless specifically asked to do so.

### **11.4 Post completion monitoring**

**226** It is important that monitoring ensures that the assets and jobs are maintained for an appropriate period after completion of the project. This "conditions period" is specified in the offer letter and is project specific. For offers made under the Assisted Area map 2007-13, the minimum applicable conditions periods are set out in paragraphs 227-229.

#### ***Aid for initial investment***

**227** For offers of £250,000 or above the conditions period should cover both assets and jobs for 5 years from the date of the first payment or 18 months from the date of the last payment, whichever is the longer.

**228** For offers below £250,000, the conditions period for assets is 5 years from the date of the first payment or 18 months from the date of the last payment whichever is longer. There is a separate conditions period for jobs of a minimum of 18 months after the last payment.

#### ***Aid for job creation***

**229** For all offers where the grant or part of the grant is for the creation of jobs linked to initial investment the conditions period will be 5 years from the date of the creation of the last job associated with the project, which must be within 3 years of 'project completion' (see paragraph 67). This period can be reduced to 3 years if the project is undertaken by a small or medium-sized enterprise. The extended monitoring period is a requirement of EU State Aid rules.

#### ***Number of cases to monitor***

**230** It is for each operating department to determine the percentage of cases on which active post completion monitoring should be carried out. However, this should not be on less than 10% of projects by number or 60% of projects by value within the region. Where less than 100% post completion monitoring is carried out, cases should be selected with a view to factors such as the size of offer, risk, the company's past performance and nature of the project. In England post completion monitoring would not normally involve site visits unless clawback is being considered.

### **11.5 Action where payment claims are not received**

**231** There is no contractual obligation on monitoring officers to issue reminders where payments fall due and consequently no need for any immediate action if companies fail to submit claims by the due date. However, the reasons for delayed claims should be investigated by monitoring officers. The monitoring officer should write to the recipient company if a claim has

not been received within two months of the due date. With this letter the monitoring officer should seek information about the current state of the project and the reasons for the delay in claiming payment. If no reply is received, the monitoring officer should follow up by telephone or a site visit.

## 11.6 No obligation to pay dates

**232** Late claims arise when a company submits a claim after the “no obligation to pay” date (NOPD). The NOPD, which should be specified in every offer letter, is the deadline after which the operating department is no longer under any contractual obligation to make payments. The main purpose of this date is to avoid an open-ended commitment and thus assist financial control. If a company claims an instalment before the NOPD, it is entitled to receive that payment, provided it satisfies the conditions set out in the offer letter, even if the time taken to process the claim means that payment is not made until after the NOPD date has passed.

### *Reminder letters*

**233** It is essential for monitoring officers to try to identify and resolve potential problems with claimants at an early stage and minimize the number of late claims. Monitoring officers should make certain that a final reminder letter is sent to all companies about 2 months before the NOPD. In addition, where it is clear the company will be unable to claim all the payments before the NOPD, the monitoring officer should take steps to remind the company that the date is approaching. The monitoring officer should explain to the company that an extension will be required and invite it to submit a formal written request setting out the reasons for the delay and the revised schedule for completion of the project. Provided that the circumstances of the case justify it the monitoring officer should grant a formal extension. Extensions beyond 6 months should normally be conditional upon the company providing the operating department with a brief report confirming the progress of the project during the period of the extended NOPD. The circumstances of each case will vary but, for example, an extension would normally be justified where the project had been delayed by major accidents during construction, fire, flood or other reasons clearly outside the company’s control.

### *Late claims*

**234** A claim submitted after the NOPD is known as a “late claim.” There is a presumption against the payment of late claims. In practice this means that payment should not be approved unless the claimant has a particularly good reason. In all cases a project should have been satisfactorily completed and its original objectives achieved. The circumstances listed below are examples of when sympathetic consideration might be given to late claims. They should not be interpreted as definitive criteria but as illustrations of the type of factors that are likely to influence the judgement that has to be made:

- a) the death or serious and protracted illness of the principal or a key member of staff in a small business;
- b) disruptive changes in personnel at small companies with limited staff resources;
- c) claims which have been lost or delayed in the post, or sent to the wrong address;
- d) delays caused by a major accident, fire or other disaster outside the control of the company;
- e) claims relating to lengthy or complex projects which are only slightly late, perhaps due to delays with auditors.

**235** Another factor which should be taken into account is any administrative failure on the part of the operating department, particularly the failure to issue a reminder letter at the appropriate time. Although, in itself, failure to issue a reminder letter is unlikely in itself to be sufficient justification to support a late claim.

**236** If a company makes a claim before the NOPD, but it only becomes apparent after that date that the claim is not fully documented, the claim must be treated as a late claim along the lines of the paragraphs above unless it appears that the missing information is due to an unintentional oversight or clerical error. In such cases, to be treated as a normal claim, the error or oversight needs to be corrected promptly once the company has been made aware of it.

## 12 Changes in projects

**237** It is a requirement of EC State Aid Law that offer letters contain a general provision to allow the recovery of all state support in the event of a grant not being compliant with EC State Aid rules.

**238** This general provision gives operating departments wide ranging powers to withhold, delay, reduce or reclaim (clawback) all or part of the proposed assistance in certain circumstances and in particular in the event of:

- a) a substantial change in the nature or scale of the project;
- b) the disposal of all or a significant part of the assets provided for the project;
- c) an unsatisfactory rate of progress towards project completion;
- d) employment shortfall, in terms of either numbers or skills; or
- e) failure to achieve forecast growth in productivity.

**239** These powers should be used with discretion.

**240** In England, any variation of a project where the level of assistance awarded is greater than £2m must be referred to BERR.

### ***Increase in project costs***

**241** Once the offer has been accepted, no allowance can be given for any subsequent increase in overall project costs.

### ***Clawback***

**242** Careful consideration should be given to the circumstances of the case when determining the level of assistance to be reclaimed. The monitoring officer should consider whether the failure of the company to fulfil the conditions in the offer letter arose from circumstances outside the company's control for example a major change in market conditions or technical problems which the company has made reasonable efforts to overcome. The ability of the company to repay assistance should be taken into account, for example there should be a greater presumption of clawback if a company is in a position to do so.

**Early payment of grant instalment**

- 243** On occasions firms may seek part payment of the planned assistance when the project has not progressed sufficiently to meet the trigger point. This needs to be treated with caution as it can indicate problems with viability. Firms may try to pressure monitoring officers by claiming that without some payment the company will fail losing all the jobs. The implication of this is that the operating department could be blamed for the failure of the business. A number of considerations will apply in such circumstances, for example:
- would a part payment genuinely save the project/business? More often it will be the case that more fundamental re-financing arrangements are required;
  - what action if any is necessary to protect the operating department's position? For example is there risk to previous payment of assistance to the business? Can this be reduced in any way without risk to jobs?
- 244** Normally assistance should not be provided if viability cannot be established, as this would put public funds at unnecessary risk, and is likely to breach EU State Aid rules with regard to providing aid to companies in difficulties.

**12.1 Aid for investment projects reduced in scale**

- 245** Where the scale of the project has been reduced, or the project has underachieved, the level of assistance should normally be reduced pro rata with the reduction in the scale of the project. However, if the monitoring officer considers this justified the grant may be reduced by a different amount.
- 246** In assessing the extent of the reduction in scale, the monitoring officer should take account of the extent to which total project costs are reduced, and the implications of any employment shortfall. This should be assessed in the light of the considerations set out in Section 12.5.
- 247** Asset sales should be regarded as reducing net project costs. If a significant disposal of assets occurs during the post completion period, or there are sales which alter the character of the project, monitoring officers should take account of the proportion of the conditions period for which an asset has been in place when deciding how much assistance should be recovered.
- 248** Changes in scale may impact adversely on productivity and skills mix and both tests should be re-visited to help inform the reduction in grant quantum.
- 249** If a company has failed to perform as well as could reasonably have been expected, or has made a deliberate decision to abandon a project in order to concentrate resources on other investment, or in obtaining assistance has unreasonably withheld information about difficulties being encountered, a greater clawback than indicated by the pro rata calculation should be considered. Operating departments should assess whether all of the paid assistance should be reclaimed in these circumstances.
- 250** If a company is sold or if its ownership is otherwise transferred recovery of monies paid should only take place when the obligations of the offer letter (including all guarantees) cannot be novated to the purchaser.

## 12.2 Changes in the nature of the project

- 251** Where the nature of the project alters to such an extent that it effectively represents a different project from that originally considered, a view will need to be taken as to whether the revised project qualifies for GBI. In such cases advice should be obtained from the appraisal officer responsible for the original offer of assistance. Examples of this situation include a company choosing to manufacture a different product; a company failing to purchase a key piece of equipment as described in the original application; or a company altering the general scale of a project.
- 252** Case officers need to take a view as to whether it is best to address changes in the nature of a project by a revised application. In this case the new application should include a reference to the basis for the original award. New accountancy and market advice should also be sought as appropriate. In considering whether support can be given to the revised project, all the normal criteria should be applied including the minimum level of assistance.
- 253** Alternatively it may more appropriate to negotiate a variation of the original offer letter.

## 12.3 Changes in financing

- 254** In some cases, the project may proceed as planned but the company may decide, after the offer of GBI has been made, to change the basis on which it is financed - i.e. by finance leasing (expenditure under an operating lease is not eligible) or acquiring under hire purchase or extended credit agreements assets which it had intended to purchase outright. In such cases, the monitoring officer should consider the implications of the revised arrangements for the project and the company. For example, the change in financing arrangement may be an indication that the company has cash flow problems which it is attempting to control by spreading capital payments over a longer period. The monitoring officer should determine whether the offer is still the minimum required to secure the project or whether it should be reduced to take account of any benefits to the company arising from the revised arrangements. The standard offer letter contains a provision for such reconsideration.
- 255** At no stage of the project should accrued payments exceed the applicant's actual cash expenditure on the project

## 12.4 Changes in ownership

- 256** As part of the normal post-completion monitoring the recipient company should be asked if its name, ultimate ownership or company registration number has changed. The implications for the project of any change in company ownership must be analysed by the monitoring officer. In particular an assessment of the viability of the project going forward and the value of any parental guarantee should be made and recorded.
- 257** If a GBI grant is to be novated it is normal for the purchasing company to "step into the shoes" of the vendor and take on all the obligations associated with the grant. In these circumstances it is not normally appropriate to withhold assistance to a new owner because they may have, for example, sufficient funds to carry out a project without support, as the value of the grant will have already been reflected in the purchase price.



**258** Legal advice should be sought in any case where a Receiver or Liquidator is seeking to transfer the project as a way of realising assets. As a general rule the monitoring officer should draw attention to the company's obligations set out in the offer letter, and request the potential claim to be noted by the Liquidator/Receiver pending the signing of the novation agreement. If the project is not continued satisfactorily or if a new project owner is unwilling to take over the offer, clawback must be considered.

**259** In certain limited circumstances, it is not necessary to action a novation or transfer agreement:

- a) If the change occurs early in the life of a project, before expenditure on the project has started, the matter may be dealt with by the issue of a new offer letter to the company undertaking the project with parallel withdrawal of the original offer;
- b) If the change occurs in the post-completion monitoring period then:
  - for small cases (less than £100k) in the last 12 months of the conditions period the monitoring officer may choose to forego the issuing of novation agreement if, in his or her considered judgement, it is likely that the project will be taken forward satisfactorily by the new owner; or
  - if the monitoring officer would not recommend the exercise of clawback conditions in the event of failure to achieve a novation agreement. This discretion is likely to be used only in cases where the project achievement, at the point of the transfer, can be said to have justified the assistance paid, or where the cost of recovery action is likely to exceed the amount repayable.

## **12.5 Employment shortfall**

**260** Monitoring of the jobs provided by a project is of paramount importance in ensuring that the purpose for which assistance has been provided is fulfilled. During monitoring, it may become apparent that the company is in fact failing to achieve the level of employment it forecast in its original application for assistance. The monitoring officer should take this up with the company.

### ***Projects given aid for investment***

**261** If the company was simply over optimistic in its original job forecast or if the shortfall is due to substantial change in the scale or nature of the project, for example, because only part of the fixed capital equipment is installed, assistance should be withheld unless it is clear that the changes, had they been known about before, would not have affected the amount of assistance offered.

**262** The skill level of jobs created and safeguarded should be assessed at the time of each claim. Any shortfall in the forecast skill levels should be treated in the same manner as a shortfall in employment.

**263** In England, if the recipient company has achieved the forecast improvement in productivity (and all the assets have been installed) it might be appropriate to pay the assistance in full or to withhold a smaller amount than the job shortfall might appear to warrant.

**264** Generally, when accounting for a job creation shortfall in an investment project the following procedure should be adopted:

- a) calculate the number of full time job-year equivalents required by the terms of the offer letter over the relevant time period<sup>9</sup> for the project ( $\sum t_{\text{target}} \times t_{\text{offer}}$ )
- b) calculate the number of full time job-year equivalents associated with the project over the period from the start of the project<sup>10</sup> and the date at which monitoring officer judges that the project has come to end. This data should be supplied by the company and verified by the monitoring officer ( $\sum t_{\text{actual}} \times t_{\text{actual}}$ )
- c) the ratio of these two quantities:

$$\text{Job fraction} = \frac{\sum t_{\text{actual}} \times t_{\text{actual}}}{\sum t_{\text{offer}} \times t_{\text{offer}}}$$

should then be used as a guide by the monitoring officer in assessing the appropriate amount of clawback.

**265** The above procedure can also be used where employment has been safeguarded rather than created. However, in this circumstance the relevant time period is the full conditions period for the project. Normally with projects that involve the safeguarding of employment it is more appropriate to look at the amount of jobs that had been protected (i.e. safeguarded) at the end of the conditions period.

### ***Projects given aid for jobs linked to initial investment***

**266** Where aid has been given as a “job grant” any employment shortfall must result in the withholding or clawback of assistance in order to ensure that the grant does not breach EU State Aid rules. The procedure set out in paragraph **264** can be used for this calculate the amount of grant to be withheld or clawed back.

## **12.6 Productivity or skills shortfall**

**267** Productivity growth and a minimum level of skills are required for projects to be eligible for GBI assistance. The skill level of jobs created or safeguarded can be monitored over the life of the project. However, it is not normally practical to assess the productivity growth achieved until the end of the project. Nevertheless, the achievement of higher productivity growth in the regions is a priority of the GBI scheme, and there should be a presumption that the total amount of grant payment will be reduced if a company fails to meet the productivity growth target specified in the offer letter.

**268** In cases where a project does not achieve the productivity growth target specified in the offer letter the final 20% instalment of grant should be withheld, in addition to any other clawback associated with other shortfalls in project outputs.

<sup>9</sup> The relevant period is from the job creation trigger specified in the offer letter until the end of the monitoring period.

<sup>10</sup> This must not be earlier than the date that the offer was agreed by the recipient company.

# Part IV:

## Annexes

### Annex A: Definitions

For the purpose of these Guidelines the following definitions shall apply:

- a) “control” has the meaning set out in Article 3 of Council Regulation (EC) No 139/2004. Specifically, control shall be constituted by rights, contracts or any other means which, either separately or in combination and having regard to considerations of fact or law involved, confer the possibility of exercising decisive influence on an undertaking, in particular by:

- ownership or the right to use all or part of the assets of an undertaking;
- rights or contracts which confer decisive influence on the composition, voting or decisions of the organs of an undertaking;

Control is acquired by persons or undertakings which:

- are holders of the rights or entitled to rights under the contracts concerned; or
- while not being holders of such rights or entitled to rights under such contracts, have the power to exercise the rights deriving therefrom;

- b) “tangible assets” means assets relating to land, buildings and plant, machinery and equipment;
- c) “intangible assets” means assets entailed in by transfer of technology by the acquisition of patent rights, licences, know-how or unpatented technical knowledge;
- d) “firm in difficulty” means a firm that fulfils the following conditions:
- i. in the case of a limited liability company, where more than half of its registered capital has disappeared and more than one quarter of that capital has been lost over the preceding 12 months;
  - ii. in the case of a company where at least some members have unlimited liability for the debt of the company, where more than half of its capital as shown in the company accounts has disappeared and more than one quarter of that capital has been lost over the preceding 12 months; or
  - iii. whatever the type of company concerned, where it fulfils the criteria under domestic law for being the subject of collective insolvency proceedings;
- e) “large investment project” means an investment in capital assets with eligible costs above €50m, calculated at prices and exchange rates on the date when the aid is granted;

- f) "number of employees" means the number of annual labour units (ALU) (full time equivalent (FTE) staff), namely the number of persons employed full time in one year, part-time and seasonal work being ALU fractions;
- g) "job creation" means a net increase in the number of employees directly concerned with the activity to which the investment relates, including employment created following an increase in the utilisation rate of the capacity created by the investment. The net increase is the increase in employment compared to the average number of employees over the previous 12 months;
- h) "job safeguarding" is not defined in EC State Aid law. For the purposes of GBI it is taken to mean the average number annual labour units (ALU), directly employed in a particular establishment calculated over the 12 month period to the end of the monitoring period;
- i) "wage cost" means the total amount actually payable by the beneficiary of the aid in respect of the employment concerned, comprising:
  - the gross wage, before tax, and
  - the compulsory contributions, such as social security charges; and
  - child care and parent care costs;
- j) "small and medium-sized enterprises" or "SME" means undertakings fulfilling the criteria laid down in Annex B at the time that the grant is offered;
- k) "large enterprises" means undertakings not fulfilling the criteria laid down in Annex B;
- l) "project completion" is not defined in EC State Aid law. For the purposes of GBI it is taken to mean the date of mechanical completion of the investment project, or the date that the material assets associated with an investment project become operational, whichever is earlier;
- m) "transport sector" is not defined in EC State Aid law. For the purposes of GBI it is taken to mean transport operators or carriers (bus operators, train operators, airlines, ship owners and operators, etc.) and transport network providers (e.g. rail networks, ports and airports). The transport sector includes road haulage (though as a liberated sector it is excluded from benefiting from most forms of State Aid). For the purposes of State Aid the transport sector does not include own transport, for example, where a supermarket carries its own goods by road in its own vehicles. It does not include freight forwarders, who merely organise shipments and warehouse goods, and it does not include vehicle, aircraft, rolling stock, ship, etc. manufacturers;
- n) "start of work" means either the start of construction work or the first legally binding commitment to order equipment, excluding preliminary feasibility studies, whichever is earlier;
- o) "agricultural product" means:
  - i. the products listed in Annex I of the Treaty, except fishery and aquaculture products covered by Regulation (EC) No 104/2000;
  - ii. products falling under Council Note codes 4502, 4503 and 4504 (cork products);
  - iii. products intended to imitate or substitute milk and milk products, as referred to in Council Regulation (EEC) No 1234/2007;

Annex I of the Treaty is reproduced in Annex C.
- p) "processing of agricultural products" means any operation on an agricultural product resulting in a product which is also an agricultural product, except on-farm activities necessary for preparing an animal or plant product for the first sale;

- q) "marketing of agricultural products" means holding or display with a view to sale, offering for sale, delivery or any other manner of placing on the market, except the first sale by a primary producer to resellers or processors and any activity preparing a product for such first sale; a sale by a primary producer to final consumers shall be considered as marketing if it takes place in separate premises reserved for that purpose;
- r) "coal sector" means undertakings which carry out an activity in connection with coal production where 'coal' is defined as high-grade, medium-grade and low-grade category A and B coal within the meaning of the international codification system for coal laid down by the United Nations Economic Commission for Europe;
- s) "shipbuilding sector" means any undertaking which is involved in the building, repair or conversion of ships where 'shipbuilding' means the building, in the Community, of self-propelled seagoing commercial vessels;
- t) "tourism activities" means the following activities in terms of NACE Rev. 2:
  - i. NACE 55: Accommodation;
  - ii. NACE 56: Food and beverage service activities;
  - iii. NACE 79: Travel agency, tour operator reservation service and related activities;
  - iv. NACE 90: Creative, arts and entertainment activities;
  - v. NACE 91: Libraries, archives, museums and other cultural activities;
  - vi. NACE 93: Sports activities and amusement and recreation activities;
- u) "synthetic fibres sector" means:
  - i. extrusion/texturisation of all generic types of fibre and yarn based on polyester, polyamide, acrylic or polypropylene, irrespective of their end-uses; or
  - ii. polymerisation (including polycondensation) where it is integrated with extrusion in terms of the machinery used; or
  - iii. any ancillary process linked to the contemporaneous installation of extrusion/texturisation capacity by the prospective beneficiary or by another company in the group to which it belongs and which, in the specific business activity concerned, is normally integrated with such capacity in terms of the machinery used;
- v) "newly created small enterprise" means a small enterprise which has been created less than five years ago (see footnote 77 to the EC National Regional Aid Guidelines (2006/C 54/08));
- w) "enterprise newly created by female entrepreneurs" means a small enterprise fulfilling the following conditions:
  - i. one or more women own at least 51% of the capital of the small enterprise concerned or are the registered owners of the small enterprise concerned; and
  - ii. a woman is in charge of the management of the small enterprise;
- x) "steel sector" means all activities related to the production of one or more of the following products:
  - i. pig iron and ferro-alloys: pig iron for steelmaking, foundry and other pig iron, spiegeleisen and high-carbon ferro-manganese, not including other ferro-alloys;
  - ii. crude and semi finished products of iron, ordinary steel or special steel: liquid steel cast or not cast into ingots, including ingots for forging semi finished products: blooms, billets and slabs; sheet bars and tinplate bars; hot-rolled wide coils, with the exception of production of liquid steel for castings from small and medium-sized foundries;

- iii. hot finished products of iron, ordinary steel or special steel: rails, sleepers, fishplates, soleplates, joists, heavy sections 80 mm and over, sheet piling, bars and sections of less than 80 mm and flats of less than 150 mm, wire rod, tube rounds and squares, hot-rolled hoop and strip (including tube strip), hot-rolled sheet (coated or uncoated), plates and sheets of 3 mm thickness and over, universal plates of 150 mm and over, with the exception of wire and wire products, bright bars and iron castings;
- iv. cold finished products: tinplate, terneplate, blackplate, galvanized sheets, other coated sheets, cold-rolled sheets, electrical sheets and strip for tinplate, cold-rolled plate, in coil and in strip;
- v. tubes: all seamless steel tubes, welded steel tubes with a diameter of over 406.4 mm.

## Annex B: Definition of micro, small and medium-sized enterprises

- 1 The definitions of micro, small and medium-sized enterprises are summarised in Table B:

**Table B:** SME definitions – thresholds

Category	Headcount	Turnover	or	Balance sheet total
medium-sized	Fewer than 250	Not exceeding €50m		Not exceeding €43m
small	Fewer than 50	Not exceeding €10m		Not exceeding €10m
micro	Fewer than 10	Not exceeding €2m		Not exceeding €2m

- 2 For the purposes of GBI an SME must be an 'autonomous enterprise' within the meaning of paragraph 1 of Article 3 of Annex I to the Commission General Block Exemption Regulation (EC 800/2008 (see below) on the date that the offer of GBI support is made.

*(Annex I to the Commission General Block Exemption Regulation (EC 800/2008)*

### Article 1: Enterprise

An enterprise is considered to be any entity engaged in an economic activity, irrespective of its legal form. This includes, in particular, self-employed persons and family businesses engaged in craft or other activities, and partnerships or associations regularly engaged in an economic activity.

### Article 2: Staff headcount and financial ceilings determining enterprise categories

- 1 The category of micro, small and medium-sized enterprises (SMEs) is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding €50m, and/or an annual balance sheet total not exceeding €43m.
- 2 Within the SME category, a small enterprise is defined as an enterprise which employs fewer than 50 persons and whose annual turnover and/or annual balance sheet total does not exceed €10m.
- 3 Within the SME category, a microenterprise is defined as an enterprise which employs fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed €2m.

### Article 3: Types of enterprise taken into consideration in calculating staff numbers and financial amounts

- 1 An 'autonomous enterprise' is any enterprise which is not classified as a partner enterprise within the meaning of paragraph 2 or as a linked

enterprise within the meaning of paragraph 3.

- 2** 'Partner enterprises' are all enterprises which are not classified as linked enterprises within the meaning of paragraph 3 and between which there is the following relationship: an enterprise (upstream enterprise) holds, either solely or jointly with one or more linked enterprises within the meaning of paragraph 3, 25% or more of the capital or voting rights of another enterprise (downstream enterprise).

However, an enterprise may be ranked as autonomous, and thus as not having any partner enterprises, even if this 25 % threshold is reached or exceeded by the following investors, provided that those investors are not linked, within the meaning of paragraph 3, either individually or jointly to the enterprise in question:

- a) public investment corporations, venture capital companies, individuals or groups of individuals with a regular venture capital investment activity who invest equity capital in unquoted businesses ('business angels'), provided the total investment of those business angels in the same enterprise is less than €1.25m;
- b) universities or non-profit research centres;
- c) institutional investors, including regional development funds;
- d) autonomous local authorities with an annual budget of less than €10m and fewer than 5,000 inhabitants.

- 3** 'Linked enterprises' are enterprises which have any of the following relationships with each other:

- a) an enterprise has a majority of the shareholders' or members' voting rights in another enterprise;
- b) an enterprise has the right to appoint or remove a majority of the members of the administrative, management or supervisory body of another enterprise;
- c) an enterprise has the right to exercise a dominant influence over another enterprise pursuant to a contract entered into with that enterprise or to a provision in its memorandum or articles of association;
- d) an enterprise, which is a shareholder in or member of another enterprise, controls alone, pursuant to an agreement with other shareholders in or members of that enterprise, a majority of shareholders' or members' voting rights in that enterprise.

There is a presumption that no dominant influence exists if the investors listed in the second subparagraph of paragraph 2 are not involving themselves directly or indirectly in the management of the enterprise in question, without prejudice to their rights as stakeholders.

Enterprises having any of the relationships described in the first subparagraph through one or more other enterprises, or any one of the investors mentioned in paragraph 2, are also considered to be linked.

Enterprises which have one or other of such relationships through a natural person or group of natural persons acting jointly are also considered linked enterprises if they engage in their activity or in part of their activity in the same relevant market or in adjacent markets.

An 'adjacent market' is considered to be the market for a product or service situated directly upstream or downstream of the relevant market.

- 4** Except in the cases set out in paragraph 2, second subparagraph, an enterprise cannot be considered an SME if 25 % or more of the capital or



voting rights are directly or indirectly controlled, jointly or individually, by one or more public bodies.

- 5 Enterprises may make a declaration of status as an autonomous enterprise, partner enterprise or linked enterprise, including the data regarding the ceilings set out in Article 2. The declaration may be made even if the capital is spread in such a way that it is not possible to determine exactly by whom it is held, in which case the enterprise may declare in good faith that it can legitimately presume that it is not owned as to 25 % or more by one enterprise or jointly by enterprises linked to one another. Such declarations are made without prejudice to the checks and investigations provided for by national or Community rules.

#### **Article 4: Data used for the staff headcount and the financial amounts and reference period**

- 1 The data to apply to the headcount of staff and the financial amounts are those relating to the latest approved accounting period and calculated on an annual basis. They are taken into account from the date of closure of the accounts. The amount selected for the turnover is calculated excluding value added tax (VAT) and other indirect taxes.
- 2 Where, at the date of closure of the accounts, an enterprise finds that, on an annual basis, it has exceeded or fallen below the headcount or financial ceilings stated in Article 2, this will not result in the loss or acquisition of the status of medium-sized, small or microenterprise unless those ceilings are exceeded over two consecutive accounting periods.
- 3 In the case of newly established enterprises whose accounts have not yet been approved, the data to apply is to be derived from a bona fide estimate made in the course of the financial year.

#### **Article 5: Staff headcount**

The headcount corresponds to the number of annual work units (AWU), i.e. the number of persons who worked full-time within the enterprise in question or on its behalf during the entire reference year under consideration. The work of persons who have not worked the full year, the work of those who have worked part-time, regardless of duration, and the work of seasonal workers are counted as fractions of AWU. The staff consists of:

- a) employees;
- b) persons working for the enterprise being subordinated to it and deemed to be employees under national law;
- c) owner-managers;
- d) partners engaging in a regular activity in the enterprise and benefiting from financial advantages from the enterprise.

Apprentices or students engaged in vocational training with an apprenticeship or vocational training contract are not included as staff. The duration of maternity or parental leaves is not counted.

#### **Article 6: Establishing the data of an enterprise**

- 1 In the case of an autonomous enterprise, the data, including the number of staff, are determined exclusively on the basis of the accounts of that enterprise.
- 2 The data, including the headcount, of an enterprise having partner enterprises or linked enterprises are determined on the basis of the

accounts and other data of the enterprise or, where they exist, the consolidated accounts of the enterprise, or the consolidated accounts in which the enterprise is included through consolidation.

To the data referred to in the first subparagraph are added the data of any partner enterprise of the enterprise in question situated immediately upstream or downstream from it. Aggregation is proportional to the percentage interest in the capital or voting rights (whichever is greater). In the case of cross-holdings, the greater percentage applies.

To the data referred to in the first and second subparagraph are added 100 % of the data of any enterprise, which is linked directly or indirectly to the enterprise in question, where the data were not already included through consolidation in the accounts.

- 3 For the application of paragraph 2, the data of the partner enterprises of the enterprise in question are derived from their accounts and their other data, consolidated if they exist. To these are added 100 % of the data of enterprises which are linked to these partner enterprises, unless their accounts data are already included through consolidation.

For the application of the same paragraph 2, the data of the enterprises which are linked to the enterprise in question are to be derived from their accounts and their other data, consolidated if they exist. To these are added, pro rata, the data of any possible partner enterprise of that linked enterprise, situated immediately upstream or downstream from it, unless it has already been included in the consolidated accounts with a percentage at least proportional to the percentage identified under the second subparagraph of paragraph 2.

- 4 Where in the consolidated accounts no staff data appear for a given enterprise, staff figures are calculated by aggregating proportionally the data from its partner enterprises and by adding the data from the enterprises to which the enterprise in question is linked.

## Annex C: “Annex I” agricultural products

1 The following list contains descriptions of the agricultural products found in Annex I of the European Treaty:

- Live animals
- Meat and edible meat offal
- Fish, crustaceans and molluscs
- Dairy produce; birds’ eggs; natural honey
- Guts, bladders and stomachs of animals (other than fish), whole and pieces thereof
- Animal products not elsewhere specified or included; dead animals of Chapter 1 or Chapter 3, unfit for human consumption
- Live trees and other plants; bulbs, roots and the like; cut flowers and ornamental foliage
- Edible vegetables and certain roots and tubers
- Edible fruit and nuts; peel of melons or citrus fruit
- Coffee, tea and spices, excluding maté (heading No 09.03)
- Cereals
- Products of the milling industry; malt and starches; gluten; inulin
- Oil seeds and oleaginous fruit; miscellaneous grains, seeds and fruit; industrial and medical plants; straw and fodder
- Pectin
- Lard and other rendered pig fat; rendered poultry fat
- Unrendered fats of bovine cattle, sheep or goats; tallow (including ‘premier jus’) produced from those fats
- Lard stearin, oleostearin and tallow stearin; lard oil, oleo-oil and tallow oil, not emulsified or mixed or prepared in any way
- Fats and oil, of fish and marine mammals, whether or not refined
- Fixed vegetable oils, fluid or solid, crude, refined or purified
- Animal or vegetable fats and oils, hydrogenated, whether or not refined, but not further prepared
- Margarine, imitation lard and other prepared edible fats
- Residues resulting from the treatment of fatty substances or animal or vegetable waxes
- Preparations of meat, of fish, of crustaceans or molluscs
- Beet sugar and cane sugar, solid
- Other sugars; sugar syrups; artificial honey (whether or not mixed with natural honey); caramel
- Molasses, whether or not decolourised
- Flavoured or coloured sugars, syrups and molasses, but not including fruit juices containing added sugar in any proportion
- Cocoa beans, whole or broken, raw or roasted
- Cocoa shells, husks, skins and waste

- Preparations of vegetables, fruit or other parts of plants
- Grape must, in fermentation or with fermentation arrested otherwise than by the addition of alcohol
- Wine of fresh grapes; grape must with fermentation arrested by the addition of alcohol
- Other fermented beverages (for example, cider, perry and mead)
- Ethyl alcohol or neutral spirits, whether or not denatured, of any strength, obtained from agricultural products listed in Annex I to the Treaty, excluding liqueurs and other spirituous beverages and compound alcoholic preparations (known as 'concentrated extracts') for the manufacture of beverages
- Vinegar and substitutes for vinegar
- Residues and waste from the food industries; prepared animal fodder
- Unmanufactured tobacco, tobacco refuse
- Natural cork, unworked, crushed, granulated or ground; waste cork
- Flax, raw or processed but not spun; flax tow and waste (including pulled or garnetted rags)
- True hemp (*Cannabis sativa*), raw or processed but not spun; tow and waste of true hemp (including pulled or garnetted rags or ropes)

### Non-“Annex I” products

2 It is not possible to provide an exclusive definition of the term “non-Annex I good” since it represents all goods not listed in Annex I of the Treaty of Rome i.e. those which are made by processing the agricultural products listed in the basic agricultural product Regulations. Thus it covers the vast majority of manufactured foods. As a general guide, the term can be taken to include:

- ready meals
- bakery products
- flavoured yoghurts
- frozen sweet corn
- margarine (some)
- sugar confectionery
- chocolate confectionery
- malt extract
- pasta
- breakfast cereals
- ice cream
- bread
- biscuits
- sandwiches
- snack products
- frozen desserts
- pizzas
- potato crisps

- tinned sweet corn
- peanut butter
- sauces
- soups
- mineral water
- soft drinks
- spirits
- beer

### **Exceptions**

- 3** The following processed foods are specifically excepted from the term “non-Annex I good”:
- goods covered by the processed fruit and vegetable regime (for example, orange juice, tomato paste)
  - first-stage processed products listed in the Annex I regimes (for example, cheese, jam, flour)

## Annex D: Supplemental research and development aid for projects in Tier 1 or Tier 2 areas

- 1 Additional research and development can be used to supplement GBI aid in Tier 1 and Tier 2 areas. This supplemental ad hoc aid does not need to be notified to the European Commission separately provided that it does not exceed 50% of the total aid to be granted for the investment and it directly fulfils all of the conditions of this Annex.

### Definitions

- 2 For the purposes of this Annex, the following definitions shall apply:
  - a) “research organisation” means an entity, such as a university or research institute, irrespective of its legal status (organised under public or private law) or way of financing, whose primary goal is to conduct fundamental research, industrial research or experimental development and to disseminate their its results by way of teaching, publication or technology transfer; all profits must be reinvested in these activities, the dissemination of their results or teaching; undertakings that can exert influence upon such an organisation, for instance in their capacity as shareholders or members of the organisation, shall enjoy no preferential access to the research capacities of such an organisation or to the research results generated by it;
  - b) “fundamental research” means experimental or theoretical work undertaken primarily to acquire new knowledge of the underlying foundations of phenomena and observable facts, without any direct practical application or use in view;
  - c) “industrial research” means the planned research or critical investigation aimed at the acquisition of new knowledge and skills for developing new products, processes or services or for bringing about a significant improvement in existing products, processes or services. It comprises the creation of components parts to complex systems, which is necessary for the industrial research, notably for generic technology validation, to the exclusion of prototypes;
  - d) “experimental” development means the acquiring, combining, shaping and using existing scientific, technological, business and other relevant knowledge and skills for the purpose of producing plans and arrangements or designs for new, altered or improved products, processes or services. These may also include, for instance, other activities aiming at the conceptual definition, planning and documentation of new products, processes or services. Those activities may comprise producing drafts, drawings, plans and other documentation, provided that they are not intended for commercial use;

The development of commercially usable prototypes and pilot projects is also included where the prototype is necessarily the final commercial product and where it is too expensive to produce for it to be used only for demonstration and validation purposes. In case of a subsequent commercial use of demonstration or pilot projects, any revenue generated from such use must be deducted from the eligible costs.

The experimental production and testing of products, processes and services shall also be eligible, provided that these cannot be used or transformed to be used in industrial applications or commercially.

Experimental development shall not include routine or periodic changes made to products, production lines, manufacturing processes, existing services and other operations in progress, even if such changes may represent improvements;

- e) “highly qualified personnel” means researchers, engineers, designers and marketing managers with tertiary education degree and at least 5 years of relevant professional experience; doctoral training may count as relevant professional experience;
- f) “secondment” means temporary employment of personnel by a beneficiary during a period of time, after which the personnel has the right to return to its previous employer.

### **Aid for research and development projects**

**3** Aid linked to research and development activities can be used to supplement GBI provided that it fulfils the conditions laid down in paragraphs 4 to 7 of this Annex are fulfilled.

**4** The aided part of the research and development project shall completely fall within one or more of the following research categories:

- a) fundamental research;
- b) industrial research;
- c) experimental development.

When a project encompasses different tasks, each task shall be qualified as falling under one of the categories listed in the first subparagraph or as not falling under any of those categories.

**5** The aid intensity shall not exceed:

- a) 100 % of the eligible costs for fundamental research;
- b) 50 % of the eligible costs for industrial research;
- c) 25 % of the eligible costs for experimental development.

The aid intensity shall be established for each beneficiary of aid, including in a collaboration project, as provided in paragraph 6(b)(i) of this Annex.

In the case of aid for a research and development project being carried out in collaboration between research organisations and undertakings, the combined aid deriving from direct government support for a specific project and, where they constitute aid, contributions from research organisations to that project may not exceed the applicable aid intensities for each beneficiary undertaking.

**6** The aid intensities set for industrial research and experimental development in paragraph 5 of this Annex may be increased as follows:

- a) where the aid is granted to SMEs, the aid intensity may be increased by 10 percentage points for medium-sized enterprises and by 20 percentage points for small enterprises; and
- b) a bonus of 15 percentage points may be added, up to a maximum aid intensity of 80% of the eligible costs, if:
  - i. the project involves effective collaboration between at least two undertakings which are independent of each other and the following conditions are fulfilled:
    - no single undertaking bears more than 70% of the eligible costs of the collaboration project;
    - the project involves collaboration with at least one SME or is carried out in at least two different Member States, or

- ii. the project involves effective collaboration between an undertaking and a research organisation and the following conditions are fulfilled:
  - the research organisation bears at least 10% of the eligible project costs, and
  - the research organisation has the right to publish the results of the research projects insofar as they stem from research carried out by that organisation, or
- iii. in the case of industrial research, the results of the project are widely disseminated through technical and scientific conferences or through publication in scientific or technical journals or in open access repositories (databases where raw research data can be accessed by anyone), or through free or open source software.

For the purposes of point (b)(i) and (b)(ii) of the first subparagraph, subcontracting shall not be considered to be effective collaboration.

**7** The eligible costs shall be the following:

- a) personnel costs (researchers, technicians and other supporting staff to the extent employed on the research project);
- b) costs of instruments and equipment to the extent and for the period used for the research project; if such instruments and equipment are not used for their full life for the research project, only the depreciation costs corresponding to the life of the research project, as calculated on the basis of good accounting practice, shall be considered eligible;
- c) costs for buildings and land, to the extent and for the duration used for the research project; with regard to buildings, only the depreciation costs corresponding to the life of the research project, as calculated on the basis of good accounting practice shall be considered eligible; for land, costs of commercial transfer or actually incurred capital costs shall be eligible;
- d) cost of contractual research, technical knowledge and patents bought or licensed from outside sources at market prices, where the transaction has been carried out at arm's length and there is no element of collusion involved, as well as costs of consultancy and equivalent services used exclusively for the research activity;
- e) additional overheads incurred directly as a result of the research project;
- f) other operating costs, including costs of materials, supplies and similar products incurred directly as a result of the research activity.

**8** All eligible costs shall be allocated to a specific category of research and development.

**Aid for technical feasibility studies**

**9** Aid for technical feasibility studies preparatory to industrial research or experimental development activities can be used to supplement GBI provided that it fulfils the conditions laid down in paragraphs 10 and 11 of this Annex.

**10** The aid intensity shall not exceed:

- a) for SMEs, 75% of the eligible costs for studies preparatory to industrial research activities and 50% of the eligible costs for studies preparatory to experimental development activities;



- b) for large enterprises, 65% of the eligible costs for studies preparatory to industrial research activities and 40% of the eligible costs for studies preparatory to experimental development activities.

**11** The eligible costs shall be the costs of the study.

#### **Aid for industrial property rights costs for SMEs**

**12** Aid to SMEs for the costs associated with obtaining and validating patents and other industrial property rights can be used to supplement GBI provided that it fulfils the conditions laid down in paragraphs 13 and 14 of this Annex are fulfilled.

**13** The aid intensity shall not exceed the intensity for research and development project aid laid down in paragraphs 5 and 6 of this Annex, in respect of the research activities which first led to the industrial property rights concerned.

**14** The eligible costs shall be the following:

- a) all costs preceding the grant of the right in the first jurisdiction, including costs relating to the preparation, filing and prosecution of the application as well as costs incurred in renewing the application before the right has been granted;
- b) translation and other costs incurred in order to obtain the granting or validation of the right in other legal jurisdictions;
- c) costs incurred in defending the validity of the right during the official prosecution of the application and possible opposition proceedings, even if such costs occur after the right is granted.

#### **Aid to small young innovative enterprises**

**15** Aid to young innovative enterprises can be used to supplement GBI provided that it fulfils the conditions laid down in paragraphs 16 to 19 of this Annex are fulfilled.

**16** The beneficiary shall be a small enterprise that has been in existence for less than 6 years at the time when the aid is granted.

**17** The research and development costs of the beneficiary shall represent at least 15% of its total operating costs in at least one of the three years preceding the granting of the aid or, in the case of a start-up enterprise without any financial history, in the audit of its current fiscal period, as certified by an external auditor.

**18** The supplementary aid amount shall not exceed €1.5 million in Tier 1 regions, and €1.25 million in Tier 2 regions.

**19** The beneficiary may receive the aid only once during the period in which it qualifies as a young innovative enterprise.

#### **Aid for innovation advisory services and for innovation support services for SMEs**

**20** Aid for innovation advisory services and for innovation support services can be used to supplement GBI provided that it fulfils the conditions laid down in this paragraph and in paragraph 21 of this Annex. The conditions laid down in this paragraph are:

- a) The beneficiary shall be an SME;
- b) The aid amount shall not exceed a maximum of €200,000 per beneficiary within any three year period;

- c) The service provider shall benefit from a national or European certification. If the service provider does not benefit from a national or European certification, the aid intensity shall not exceed 75% of the eligible costs;
- d) The beneficiary must use the aid to buy the services at market price, or if the service provider is a non-for-profit entity, at a price which reflects its full costs plus a reasonable margin.

**21** The eligible costs shall be the following:

- a) as regards innovation advisory services, the costs relating to: management consulting, technological assistance, technology transfer services, training, consultancy for acquisition, protection and trade in Intellectual Property Rights and for licensing agreements, consultancy on the use of standards;
- b) as regards innovation support services, the costs relating to: office space, data banks, technical libraries, market research, use of laboratory, quality labelling, testing and certification.

**Aid for the loan of highly qualified personnel**

**22** Aid for the loan of highly qualified personnel seconded from a research organisation or a large enterprise to an SME can be used to supplement GBI provided that it fulfils the conditions laid down in this paragraph and in paragraphs 23 to 25 of this Annex. The conditions laid down in this paragraph are:

- a) The seconded personnel must not be replacing other personnel, but must be employed in a newly created function within the beneficiary undertaking and must have been employed for at least two years in the research organisation or the large enterprise, which is sending the personnel on secondment;
- b) The seconded personnel must work on research and development and innovation activities within the SME receiving the aid.

**23** The aid intensity shall not exceed 50% of the eligible costs, for a maximum of 3 years per undertaking and per person borrowed.

**24** The eligible costs shall be all personnel costs for borrowing and employing highly qualified personnel, including the costs of using a recruitment agency and of paying a mobility allowance for the seconded personnel.

**25** This Annex shall not apply to consultancy costs as referred to in Article 26 of Commission Regulation (EC) No 800/2008 of 6 August 2008 declaring certain categories of aid compatible with the common market in application of Articles 87 and 88 of the Treaty (General block exemption Regulation).

## Annex E: Supplemental training aid for projects in Tier 1 or Tier 2 areas

### Definitions

- 1** For the purposes of this Annex, the following definitions shall apply:
  - a) “specific training” means training involving tuition directly and principally applicable to the employee’s present or future position in the undertaking and providing qualifications which are not or only to a limited extent transferable to other undertakings or fields of work;
  - b) “general training” means training involving tuition which is not applicable only or principally to the employee’s present or future position in the undertaking, but which provides qualifications that are largely transferable to other undertakings or fields of work. Training shall be considered general if, for example:
    - i. it is jointly organised by different independent undertakings or where employees of different undertakings may avail themselves of the training;
    - ii. it is recognised, certified or validated by public authorities or bodies or by other bodies or institutions on which a Member State or the Community has conferred the necessary powers.

### Training aid

- 2** Additional training aid can be used to supplement GBI aid in Tier 1 and Tier 2 areas. This supplemental ad hoc aid does not need to be notified to the European Commission separately provided that it does not exceed 50% of the total aid to be granted for the investment and it directly fulfils conditions laid down in paragraphs 3 to 5 of this Annex.
- 3** The aid intensity shall not exceed:
  - a) 25% of the eligible costs for specific training; and
  - b) 60% of the eligible costs for general training.However, the aid intensity may be increased, up to a maximum aid intensity of 80 % of the eligible costs, as follows:
  - a) by 10 percentage points if the training is given to disabled or disadvantaged workers;
  - b) by 10 percentage points if the aid is awarded to medium-sized enterprises and by 20 percentage points if the aid is awarded to small enterprises.
- 4** In cases where the aid project involves both specific and general training components which cannot be separated for the calculation of the aid intensity, and in cases where the specific or general character of the training aid project cannot be established, the aid intensities applicable to specific training shall apply.
- 5** The eligible costs of a training aid project shall be:
  - a) trainers’ personnel costs;
  - b) trainers’ and trainees’ travel expenses, including accommodation;
  - c) other current expenses such as materials and supplies directly related to the project;

- d) depreciation of tools and equipment, to the extent that they are used exclusively for the training project;
- e) cost of guidance and counselling services with regard to the training project;
- f) trainees' personnel costs and general indirect costs (administrative costs, rent, overheads) up to the amount of the total of the other eligible costs referred to in points (a) to (e). As regards the trainees' personnel costs, only the hours during which the trainees actually participate in the training, after deduction of any productive hours, may be taken into account.

## Annex F: Undertakings destroyed by fire or disaster

- 1 Where a project is a replacement of an undertaking destroyed by fire or some other disaster it is important to ensure that assistance is not provided for the same jobs or costs twice.
- 2 Where GBI support was not previously provided to the undertaking, projects whether at the same location or elsewhere should be treated as wholly new projects. Insurance monies should be treated as resources available for the project and should be taken into account when considering the level, nature and terms of assistance.
- 3 Where grant support was awarded to the original undertaking, and all payments were made, assistance should only be provided to a replacement project in the Assisted Area in respect to jobs and investment in excess of those relating to the original grant. For example, investment associated with the acquisition of new or more modern plant or equipment would not count as eligible investment unless it was also associated with an increase in employment.
- 4 Where a grant was provided for a project and the disaster occurred before all payments were made, further payments should only be made when the project has restarted and the milestones set out in the offer letter are achieved.

## Annex G: Productivity test

- 1 The productivity test calculates projected productivity growth for an undertaking plus the planned project, and compares it with average growth observed nationally in the same industry and in the wider economy.
- 2 The objective of the test is to ensure that projects improve the rate of growth in productivity both in the region and in the country as a whole. If a project is in a sector that is growing above the national average (for either manufacturing or for the whole economy, as relevant), the project is compared with the sectoral average. If a project is in a sector that is performing below the relevant national average, the project is compared with the national average.

### ***What is Gross Value Added (GVA)?***

- 3 Under the UK National Accounts, GVA is defined as:  
  
 “The value generated by any unit engaged in production (of goods and services)...”  
  
 It is measured at basic prices, i.e. it excludes taxes on products (such as Value Added Tax).
- 4 Company accounts do not contain an equivalent measure of GVA. However, the calculation used by the Value Added Scoreboard published by the BERR and accepted nationally and internationally is a good approximation. Applying this definition to the financial information available from the application form, the main components are:
  - gross profit (i.e. before deduction of depreciation of fixed capital); and
  - direct labour costs

### ***Full-time equivalents (FTEs) and employees***

- 5 The GVA calculations are based on the average growth per year in terms of GVA per full-time equivalent employee (defined as “annual labour units” in EC Regulations). As such, where the forecasts for the undertaking with the investment project forecasts a mix of both full-time and part-time positions, the part-time jobs should be expressed as a proportion of full-time hours, and aggregated to provide a total full-time equivalent figure. These calculations should be made before entering employment figures into the applicant spreadsheet. Normally jobs are listed in the standard GBI application form on an FTE basis.
- 6 The GVA calculations only use “employees” (and associated labour costs). Employees are those workers with National Insurance contributions paid by the applicant plant (or by the enterprise in which the applicant belongs).

### ***Assigning an industry code***

- 7 All calculations are based on classifications at industry sub-class (4-digit) level from the Standard Industrial Classification (SIC 2003) of economic activities.
- 8 The applicant will be asked to provide the 4-digit code for the project in the standard application form. However, the case officer may also need to agree with the applicant the 4-digit SIC code that best encompasses the undertaking’s main area of economic activity if this differs from that of the proposed project. It is the SIC code for the undertaking that should be used in the GVA calculation.

### Time Scales

- 9** The applicant GVA per FTE spreadsheet provides options to make a productivity assessment over any time period up to 12 years. Assessment over a short time period will be acceptable only where the grant level is less than £250,000. In general applications should be assessed over at least 6 years.

### Applicant spreadsheet

- 10** The first stage of the GVA assessment is to calculate a projected annual average growth rate in terms of GVA per FTE. This may either be done by the applicant, or by the case officer using the information provided in the Financial Appendices to application form.
- 11** The first year of accounts used in the calculations should be the most current "actual" financial information for the undertaking. All further years should be based on the forecasts provided for the undertaking with the project.

### Entering data

- 12** The applicant spreadsheet is presented in Figure 4. Only figures in green on the spreadsheet should be entered manually - all other figures calculate automatically from these.

**Figure 4:** The applicant spreadsheet for the GVA productivity test.

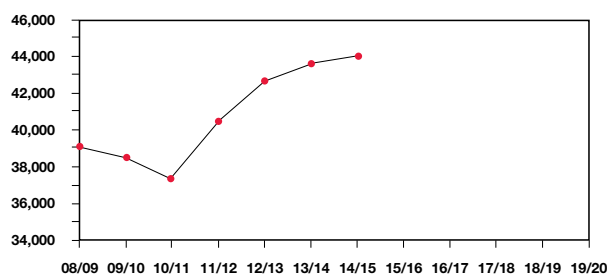
Calculation of GVA per FTE of applicant plant *plus* project

Total number of years **7**  
 Start month for first data point **Apr**  
 Start year for first data point **2008**

	Out-turn	Projections...					
£000s	08/09	09/10	10/11	11/12	12/13	13/14	14/15
Gross profit	110.0	122.0	123.0	142.0	157.0	164.0	165.0
Direct labour	301.0	342.0	352.0	370.0	380.0	385.0	390.0
<b>Subtotal (inputs)</b>	<b>411.0</b>	<b>464.0</b>	<b>475.0</b>	<b>512.0</b>	<b>537.0</b>	<b>549.0</b>	<b>555.0</b>
Indirect materials and services	20.0	22.0	24.0	25.0	25.0	25.0	25.0
Group service charge	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other items	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional items	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Subtotal (costs)</b>	<b>20.0</b>	<b>22.0</b>	<b>24.0</b>	<b>25.0</b>	<b>25.0</b>	<b>25.0</b>	<b>25.0</b>
<b>Total GVA</b>	<b>391.0</b>	<b>442.0</b>	<b>451.0</b>	<b>487.0</b>	<b>512.0</b>	<b>524.0</b>	<b>530.0</b>
<b>FTE jobs</b>	<b>10.0</b>	<b>11.5</b>	<b>12.0</b>	<b>12.0</b>	<b>12.0</b>	<b>12.0</b>	<b>12.0</b>
<b>GVA per FTE (£)</b>	<b>39,100</b>	<b>38,435</b>	<b>37,583</b>	<b>40,538</b>	<b>42,667</b>	<b>43,667</b>	<b>44,167</b>

**GVA per FTE (£)**

Growth rate (%) in GVA/FTE	<b>2.05</b>
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- 13** The case officer should first enter the number of years over which the assessment is to be made, and the month and year of the start of the first data-point (for example, in Figure 4 the first data-point refers to the financial year 06-07, so this is entered as Apr 2006). The table and graph will only display data over the specified time period, and the column headings will show the years for which data is to be entered.
- 14** The elements of the financial information to be entered for each year are:
- Gross profit (turnover less direct materials and direct labour costs);
  - Direct labour costs;
  - Indirect costs associated with materials and services;
  - Group service charge;
  - Costs entered under “Other items” (see note below); and
  - Exceptional items (see note below).

Note - “Other items” and “Exceptional items”, although rarely included in an applicant’s Financial Appendices, may by their very nature include a wide range of costs. If such costs are included an assessment should be made on a case-by-case basis as to whether they should be entered into the spreadsheet and therefore subtracted from the calculation of GVA. BERR will be able to offer advice on this assessment for individual cases if there is any uncertainty.

- 15** Finally the case officer should enter the number of FTE jobs associated with the investment project for each year of the assessment. The spreadsheet will display the average annual growth rate in GVA per FTE. In Figure 4 this value is 2.05% and it is highlighted by a red ellipse. The average annual growth rate is the key output of this spreadsheet.
- 16** The trend GVA and trend FTE used in the previous version of the applicant spreadsheet have been removed for simplicity and to avoid perverse outcomes that had occasionally been observed.
- 17** As the raw data is now used, the spreadsheet automatically plots a graph of GVA per FTE. This is to allow any unusual trends in the growth of GVA per FTE to be identified, for example data that is clearly cyclical or highly erratic. If such a trend is present, case officers should investigate further by examining the inputted data and the assumptions underpinning the forecasts.

### ***Allowing for “lead times” for new start-ups***

- 18** Where a project is a new start-up and exhibits a clear negative return in the first couple of years of coming into being, it is recommended that the early years of the GVA forecast are discarded.
- 19** Calculating growth in GVA per FTE from year 1 of a start-up project can falsely inflate expected growth rates and result in the applicant being set an unrealistic GVA per FTE growth target.
- 20** Alternatively front loaded expenditure by a start-up can give rise to a negative growth rate, which can cause the project (unfairly) to fail the GVA test. Therefore, when dealing with investment projects by start-ups case officers should allow some “lead-time” and use year 2 or 3 of the project as the first year in the GVA applicant spreadsheet.



### Thresholds by SIC code spreadsheet

- 21** The second stage of the GVA assessment is to compare the GVA per FTE growth rate calculated by the applicant spreadsheet with the average observed nationally in the sector or wider economy.
- 22** The thresholds by SIC code spreadsheet, presented in Figure 5 calculates average growth rates observed in each sector and sub-sector of the GB economy in recent years. This calculation is based on data from the Annual Business Inquiry (ABI) for the years 1998 to 2004. The spreadsheet converts the observed average growth rate into thresholds against which the applicant's growth rate can be compared.

**Figure 5:** The thresholds by SIC code spreadsheet

4 digit SIC code	1582	Manufacture of rusks and biscuits; manufacture of preserved pastry goods and cakes
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Inflation assumption	1	Current prices
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0 = zero inflation assumed (ie constant prices), 1 = positive inflation assumed (ie current prices)

Thresholds of annual average growth in GVA per FTE

1 = Good pass	6.75% and above
2 = Pass	2.56% to 6.75%
3 = Qualified pass	1.30% to 2.56%
Fail	less 1.30%

Table based on average for **4-digit sector**

Average growth rates in GVA per FTE

4 digit sector	1582	Manufacture of rusks and biscuits; manufacture of preserved pastry goods and cakes	4.7%
3 digit sector	158	Manufacture of other food products	5.8%
2 digit sector	15	Manufacture of Food Products and Beverages	3.8%
Industry group		Manufacturing	3.5%

Average growth rates in GVA

4 digit sector	1582	Manufacture of rusks and biscuits; manufacture of preserved pastry goods and cakes	-0.2%
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Average growth rates in FTE

4 digit sector	1582	Manufacture of rusks and biscuits; manufacture of preserved pastry goods and cakes	-4.7%
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Latest GVA per FTE level (2003)

4 digit sector	1582	Manufacture of rusks and biscuits; manufacture of preserved pastry goods and cakes	£36,597
Current prices			

- 23** The ABI does not include data for public organisations or the financial intermediation sector, so data for these sectors are not available in this spreadsheet.

### Layout and Content

- 24** As with the applicant sheet, only figures in green on the spreadsheet should be entered manually as all other figures are calculated automatically from these. Specifically, the only information that needs to be entered is:

- the 4-digit SIC code for the undertaking. A full list of the 2003 SIC codes available, and their titles, can be found on a second sheet, by clicking on the "4-digit SIC codes" tab; and

- whether a positive inflation assumption is included in the applicant's forecasts. If no such assumption is made, i.e. zero inflation is assumed, this equates to constant prices, and is coded as 0. If a positive inflation assumption is included, this equates to current prices, and is coded as 1.

This information is highlighted by a red ellipse in Figure 5.

### **Thresholds**

- 25** Growth rates are categorised as: 1 = a good pass; 2 = a pass; 3 = a qualified pass; or a fail. The colour-coded box gives the growth rates for each of these categories for the specified SIC code sector. In Figure 5, the previously calculated growth rate for the undertaking plus project (2.05%) falls into the category of Qualified Pass (1.47% to 2.88%).
- 26** The projected growth rate in GVA per FTE across the undertaking and project must achieve a score of at least 2 in order to gain an automatic pass on the productivity test. However, an undertaking that achieves a score of 3 should not automatically fail the productivity test. In these cases, case officers should check whether the growth rate of the undertaking and project is close to the average for its broader sectors (2-digit or 3-digit) and/or the average rate across the industry group. If the undertaking with project rate of growth is comparable to either of these then the application should be awarded a "qualified pass" against the productivity criteria.

### **Average GVA per FTE growth rates**

- 27** Below the project growth rate thresholds on the spreadsheet are the average GVA per FTE growth rates observed in the 4-digit, 3-digit, and 2-digit sectors, and across the industry group (either manufacturing or whole economy). These allow comparisons to be made in the case of a qualified pass, as described above.
- 28** Due to data quality issues there are a number of cases where growth rates could not be calculated for some sectors and sub-sectors. Also, if the average growth rate in a sector or sub-sector is below that of the industry group, it is not used, reverting instead to the growth rate for a broader sector of the economy. In these cases no growth rate will be displayed for the level in question. The thresholds are always based on the lowest level at which a growth rate is usable, and this level is shown immediately under the table of thresholds.

### **Average growth rates in GVA and in FTE**

- 29** This information is included in order to provide additional background information on which to base decisions concerning the relative productivity improvement of the undertaking and the project. For example, high growth in GVA per FTE can simply result from the number of employee jobs declining more quickly than total GVA. The separate growth rates are included to help identify specific industry sectors where this may be occurring.
- 30** These figures are also based on the lowest level at which a GVA per FTE growth rate is usable, and so match the level used to calculate the project growth rate thresholds.

### **Level of GVA per FTE**

- 31** The final data on the spreadsheet is the latest available level of GVA per FTE, to give further context to the figures for the undertaking plus project.

**Confidential data**

- 32** Data for many sectors and sub-sectors is unavailable as it is considered “disclosive”, i.e. it may be possible to deduce figures for an individual firm responding to the ABI from those figures. In all cases, the lowest level at which figures are available is shown and, within that level, the most recent figure available is used. The level and year used are indicated in the spreadsheet. Note that the level will not necessarily correspond with the level used for the project growth rate thresholds.

**Cautionary points**

- 33** When interpreting the economic information presented in the thresholds by SIC code spreadsheet, and assessing applicant performance against this, the following points should be noted:
- a) All of the figures used in the GVA calculation are estimates based on statistical surveys. Therefore the data outputs have some inherent uncertainty that is difficult to quantify. Limitations on the number of businesses that can be sampled in any given year mean that the estimates for some industries will be of higher quality than others;
  - b) The economic growth rates calculated by this system are based on seven years of data (1998 to 2004). In some cases, these growth rates could reflect short-term movements in certain industry sectors, and not the underlying longer-term growth trends against which we would ideally want applicants to be assessed. Case officers must interpret the GVA per FTE information carefully, and where possible use the full range of outputs available from the spreadsheet (for example, changes in employment and GVA levels, and wider sectoral growth rates). If case officers find clear evidence that a growth rate produced by the GVA spreadsheets has been severely distorted by short-term fluctuations, then the case officer should assess the applicant firm’s growth rate against the manufacturing or whole economy growth rate as appropriate;
  - c) In some cases, an applicant firm may be the most efficient firm operating in its sector. In this situation it is unlikely that the applicant will be able to demonstrate strong productivity growth and as it will have little room for improvements in operational efficiency. The GVA per FTE graph on the applicant spreadsheet may well be flat in these cases. In the case of a large firm (i.e. a non-SME), where the project is internationally mobile and the applicant is more than 40% above its sector average for GVA per FTE, case officers should be flexible in their approach. It is acceptable to set aside the result of the productivity test provided that the projected annual growth in GVA per FTE remains positive over the duration of the project;
  - d) At its lowest level, the GVA system tabulates the rates of growth in GVA per FTE and other information at the SIC 4-digit level. Even at this level the nature of the specific firms within some of the codes can still be very diverse, and there may be considerable scope for variation in, for example price inflation, earnings, and productivity, between all of the types of business that are contained within each grouping. Case officers should be conscious of this variation when benchmarking individual firms against these rates of growth.
  - e) In certain industries, both employment and GVA may be declining, and the average GVA per FTE growth rate may be high simply because employment is declining more quickly than GVA. This could lead to an unrealistic productivity target being set. Additional information encompassing total GVA and employment is provided from the system to help identify sectors or sub-sectors where this may be happening. If this effect is evident, it is preferable to assess a given undertaking or project against the performance of the broader sector in which it is coded (i.e. the performance of the 3-digit or 2-digit sector).

### **Further considerations**

- 34** In addition to using the GVA spreadsheets to assess productivity, it may be useful to compare the rate of growth in GVA per FTE of the project with the rate of growth in regional GVA per head to give an idea of the contribution of a project to regional growth. However, case officers should note that these two measures have different definitions, so straight comparisons need to be treated cautiously.
- 35** Case officers also need to be satisfied that the productivity growth associated with a project is sustainable. To illustrate this point, a relatively poor project in a high performing sector may well improve regional GVA per head but it may not be sustainable in the market.
- 36** Should case officers judge that the project will not contribute to sustainable regional economic growth, including its impact on other regions, it may be appropriate to refuse financial assistance.

### **Updates**

- 37** The information in the GVA assessment system is based on a number of continuous surveys carried out by the Office for National Statistics, with the main one being the Annual Business Inquiry.
- 38** The information in the system and resulting growth rates will be updated every couple of years, and an updated version of the new system will be circulated to operating departments and RDAs. However, any productivity assessments made of applicant companies should not be revised after an updated system is distributed. The GVA assessment and GBI offer will be made on the basis of the best information available at the time of application, and should not be changed retroactively.

### **Confidentiality**

- 39** The criteria for assessment of the productivity test are intended for internal use by operating departments and RDAs. Under no circumstances should any information from the thresholds by SIC code spreadsheet be distributed to third parties without the express permission of BERR.
- 40** The information in the applicant spreadsheet is derived from the Financial Appendices to the GBI application, and therefore there is no issue of confidentiality. Case officers are advised to share the applicant spreadsheet with the applicant, so that they can endorse the figures used, and understand the basis for the productivity targets contained in the offer letter.

## Annex H: Evaluating alternative project locations

- 1 When an applicant bases their GBI application on the existence of an alternative project location the credibility of the alternative location should be tested by monetising the costs and benefits associated with siting the project at each location. The value of the different locations should be appraised in the context of the company's overall strategy and the full costs and risks of each location should be considered, not just particular elements, such as comparative wage rates.
- 2 Specifically, case officers should seek to answer the following questions:
  - a) is the company's overall strategy based on a distribution of capacity over main markets of which the UK is one?
  - b) is there evidence that the company has seriously assessed the costs and risks of alternative project locations?
  - c) how would relocation to an alternative site affect distribution, marketing costs and the ability to win contracts?
  - d) how do labour costs compare, taking account of relative productivity, employer social security contributions and hiring and firing costs?
  - e) what would be the costs to a company of closing a facility in a deprived area and relocating elsewhere?
  - f) are any claims about foreign assistance credible and/or documented?

# Annex I: Seasonal jobs, homeworking and teleworking

## Seasonal jobs

- 1 Seasonal jobs may be included in offers and cost per job calculations (calculated as full-time equivalents) provided that: there is a contract of employment; the jobs are integral to the project; are specified in the company's application and the offer letter; and last for a minimum of four weeks per annum. Seasonal jobs should be subject to a "conditions" period of identical length to permanent full-time employment resulting from the project. Where the number of seasonal workers varies each year, the smallest number created in the relevant years should be adopted.

## Homeworking and teleworking

- 2 Developments in employment policy have created full time job opportunities in the form of homeworking/teleworking.

## Homeworking

- 3 There are two sorts of homeworking:
  - individuals, generally highly skilled in administrative, professional and technical occupations who are contracted to do work in their homes, and
  - pieceworkers who are generally self-employed individuals whose remuneration is linked to output levels. They are normally engaged in low paid, low technology and mostly manual occupations which are taken from the factory floor.

## Teleworking

- 4 Teleworking is a flexible way of working which covers a wide range of work activities, all of which entail working remotely from an employer, or from a traditional place of work, for a significant proportion of work time. It may be either a full-time or part-time basis. The work often involves electronic processing of information (via a computer), and always involves using telecommunications (telephone, fax, modem and (possibly) a video conference link) to keep the remote employer and employee in contact with each other. This form of teleworking is also known as homeworking.
- 5 To be eligible for assistance, homeworking or teleworking jobs must fulfil the following criteria:
  - a permanent full time contract of employment with the applicant, relating directly to the project;
  - clear evidence that the appointment is an integral part of the project and that the job will be required for the life of the project;
  - in the case of part-time homeworking or teleworking there must be a permanent contract of employment with the applicant, relating directly to the project of at least 15 hours a week. Two such contracts will count as the equivalent of one full time job.
- 6 Applicants will need to demonstrate that homeworking or teleworking employees are permanently domiciled in Assisted Area. Where based at the office or in a satellite office, this will need, as usual, to be in an Assisted Area.

- 7 Homeworkers or teleworkers who move outside of an Assisted Area will automatically disqualify the applicant from any further assistance for those jobs. Where this should happen to any significant extent, monitoring officers will also need to consider the normal guidelines on clawback.
- 8 It may be acceptable that homeworking or teleworking employees could be domiciled in another Assisted Area, but this will need to be decided on a case by case basis with particular concern for the feasibility of monitoring.
- 9 An additional clause to the offer letter should be added to enable adequate monitoring of homeworking or teleworking.

## Annex J: Economic appraisal

### Overview

- 1 This Annex sets out a common approach to the economic appraisal of applications for GBI. The procedures for assessing whether a project meets the efficiency criterion need to be related to the likely level of assistance.
- 2 The rationale for the Economic Appraisal is that assistance should not only benefit the company in receipt of aid and the region in which it is based, but also not be detrimental to the UK economy as a whole.
- 3 The methodology used in the appraisal reflects Treasury guidance set out in the "Green Book" (Appraisal and Evaluation in Central Government, Treasury Guidance). The particular form of the test, with its emphasis on the efficiency of resource use, reflects a belief that, in the long term, the main influences on growth of real national income and employment arise on the supply side of the economy (through competitive and innovative processes) rather than on the extent to which governments stimulate aggregate demand.
- 4 Treasury guidance also emphasises the dangers of subsidies to individual companies driving other, unsubsidised, companies out of business (or at least restricting their growth) directly through "unfair" competition, and indirectly through higher taxes, interest rates and wages as a consequence of the extra government expenditure (so-called "crowding-out"). The view is therefore taken that projects should only be supported where they use resources at least as efficiently as the activities which they may crowd-out.
- 5 The combination of direct benefits and wider economic effects examined in the economic appraisal will reflect the value which society places on the output of a project, the efficiency with which a project uses resources (bearing in mind the opportunity costs of those resources) and the extent to which the UK economy benefits as a result.
- 6 The depth of the economic appraisal should be proportional to the amount of grant:
  - **Cases for grants of less than £250,000**  
Where a grant is likely to be less than £250,000, cases should be assessed on a qualitative basis only unless there are sufficient doubts to warrant using the procedure for larger cases set out below.
  - **Cases for grants above £250,000 and below £2 million**  
Where the amount of grant requested is more than £250,000 but less than £2 million, a Commercial Efficiency Test (CET) should be carried out to ensure that the project provides a net direct benefit. In order to pass the CET the net present value (NPV) of the difference in cashflows between the with- and without-project scenarios must be positive.  
  
Sometimes a project will fail the CET because of particularly high start-up costs, or a long-run efficiency disadvantage caused by operating in an Assisted Area. If the case officer believes that the project may justify state support despite failing the CET the project may be referred to BERR economists who will carry out a Full Economic Appraisal (FEA) that will assess the regional and national costs and benefits of the project.



- **Cases for grants over £2 million**

Where the proposed amount of GBI support is greater than £2 million BERR will undertake a Full Economic Appraisal of wider costs and benefits of the project. These costs and benefits do not accrue to the company, but affect the efficiency and competitiveness of other UK competitors, suppliers and customers. A project will satisfy the FEA if the sum of direct and wider effects indicates that the project will be of net benefit to the national income. A positive net direct effect on national income (a CET pass) is neither necessary nor sufficient to satisfy the FEA.

### **Commercial efficiency test (CET)**

- 7 The CET uses the discounted cash-flow (DCF) of a project. The test estimates the effect of the project on national income by comparing a "with project" scenario with the most likely alternative course of action for the company (the "without project" scenario). The test should normally be carried out by an accountant.
- 8 The underlying data for the CET should be drawn from the financial projections provided by the applicant. Additional data may be required to estimate the DCF of the "without project" scenario, though it should normally be possible for the company to derive projections for this scenario from its management information system.
- 9 The "without project" DCF should be deducted from the "with project" DCF. Projections should normally extend over at least 10 years, though it will sometimes be necessary to extrapolate the data provided by the firm to cover this period. If the financial forecasts include an allowance for general inflation this should also be removed to ensure that the project is assessed on a constant price basis. For long term projects financial projections should cover the entire anticipated project lifetime.
- 10 Cash-flows should measure the value of all the outputs from the project less the costs of all the inputs. Trading profit is the key output of the project, but there are others. For example, all project investment (fixed and working capital) is treated as a cost irrespective of how it is financed. Therefore outputs should also include the payment of interest on debt used to finance the investment project and the depreciation on the capital assets. This ensures that project costs are not double-counted, and that neither the mode of financing the project, nor the method of accounting for depreciation, will affect the efficiency of a project. Where depreciation or interest are included in the project costs, they should be added back to the profit stream.
- 11 Working capital movements must be assessed carefully. In particular, the cause of a material fall in working capital should be investigated to ensure that the reduction is caused by improvements in business process efficiency.
- 12 The effects of transfer payments within the economy should be removed from projections. Specifically, costs and benefits should be gross of tax and state aid, as these payments simply represent a redistribution of national income and not a measure of project efficiency. For the same reason redundancy payments should not be included in the CET.
- 13 In order to reflect opportunity costs properly, capital expenditure (both fixed and working capital) should be deducted at the time at which it is incurred. In cases where the life of an asset is longer than the life of the project, an allowance should be made for the residual value of the asset, and this should be added to the cash-flow for the project for the final appraisal year. This ensures that an allowance is made for the disposal value of project assets.

### **Discounting**

- 14** The net project cash-flow should be discounted in order to express the future value of the project in terms of present values. The sum of the discounted net cash-flow for a project is a measure of direct benefit known as the Net Present Value (NPV). Discounting takes account of the (national income) opportunity costs of devoting resources to a project.
- 15** Discounting reduces the present value of future costs and benefits. Therefore, projects which bring benefits early on will have a higher NPV than those in which the benefits take longer to emerge.
- 16** A standard discount rate of 10% discount rate should be used when appraising. This rate reflects a typical commercial cost of capital. A standard discount rate is used because using a higher rate<sup>11</sup> can distort the time profile of the project cash-flows. In particular using an inappropriately high discount rate will cause short term costs to be over-estimated, and long term benefits to be underestimated. A profitable low risk project can appear to be NPV negative if the discount rate is too high.
- 17** A project will pass the CET if its direct contribution to national income is positive, i.e. the project is NPV positive using the standard discount rate. The CET should ensure that projects with inherently poor rates of return do not receive state support. Conversely, if a project is assessed to have an exceptionally high NPV, the additionality of the application should be re-examined carefully.

### **Dealing with uncertainty in the CET**

- 18** After the NPV of a project has been calculated the principal threats to the project's success should be identified and studied. There are three ways that this can be done: sensitivity analysis, scenario analysis and Monte Carlo simulation. The amount of analysis devoted to checking the robustness of the DCF should be proportional to the size of the project and the amount of risk borne by the public purse.

### **Sensitivity analysis**

- 19** The simplest way of testing the robustness of the CET evaluation is by sensitivity analysis. In this type of analysis the variables that may impact the success of a project are considered in turn, and the project NPV is recalculated using very optimistic and very pessimistic levels of these variables. This establishes a range of possible outputs that allows the case-officer to examine how much the key variables would need to change in order to make the project NPV negative. A project is described as "sensitive to" the variable if the range of possible NPVs for the project is wide, especially on the pessimistic side.
- 20** At a minimum sensitivity analysis should consider the impact on a project variation in: turnover, costs and appraisal period:

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<sup>11</sup> Firms often mitigate against risk by using a high discount rate or by requiring a project to generate a high internal rate of return (IRR).

- **Turnover**

Turnover should be decreased until the NPV of the project is zero. By changing turnover levels while holding costs constant the effect of a pure price change is investigated (it is assumed that demand for the project output is constant despite the decrease in price). A decrease in price may occur where:

- a) the strength of competition has been underestimated. The incumbent may decide to fight the entrant for market share by lowering prices. The entrant will have to respond by reducing its price to achieve its predicted sales level;
- b) buyers have market power. For example, in the car industry, large car manufacturers will have a high degree of monopoly power and may be able to negotiate a price for a given level of parts;
- c) transfer price policy was overestimated. A branch plant may overestimate the price at which they expect the company to purchase their product, through overestimating the value of the good to the company.

- **Costs**

Either direct and/or indirect costs can be varied. A change in direct costs (i.e. variable costs) can be caused by either changing wage rates for direct employees or costs of inputs. For example, a company may underestimate the wage rates that they will have to pay employees or the cost of raw material may increase or decrease depending on world and local market conditions. Indirect costs relate to the fixed (sunk) costs of production, for example, managers' salaries. Small changes in production levels will not directly affect these costs. Direct costs are likely to be more volatile than indirect costs.

- **Appraisal period**

Some projects are sensitive to the appraisal period, and may fail the CET if it is conducted over less than 10 years. In such cases it is worth altering the appraisal period to test this sensitivity.

### **Scenario analysis**

- 21 Sensitivity analysis of the kind described above is easy, but it is not always helpful. Variables do not usually change one at a time. If costs are higher than expected, it is likely that prices will also be higher. And if prices are higher it is likely that sales volumes will be lower. If the DCF model does not allow for any dependencies between different variables, then it is likely to incorrectly predict the potential costs and benefits of an investment project. The most straightforward method for dealing with the dependency problem is to examine the effect on the DCF model of alternative plausible combinations of variables. In other words, estimate the NPV of a project under a number of different scenarios and compare these estimates with the base case.
- 22 For example, changing output volumes affect both the turnover level and the direct costs in a proportional fashion, assuming constant returns to scale. If a firm does not achieve its target level of sales then it may respond by reducing output, for example, by reducing the number of hours worked. Hence, turnover figures and direct costs should be changed by the same proportion until the NPV of the project is zero. Decreasing volumes could arise for a number of reasons such as over-optimistic sales forecasts by the applicant, a decline in demand for that product due to a change in consumer tastes or competition from new or existing products.

### **Monte-Carlo simulation**

- 23** In a sensitivity analysis the project variables are changed one at a time; with a scenario analysis a limited number of combinations of variables are examined. Normally these two types of analysis will provide enough insight into the financial mechanics of an investment project that the case officer will be able to make an assessment as to likelihood of the project being successful and the risk to the public purse. However, these techniques are of limited use when appraising complex projects with a number of interdependent variables. In these cases it is appropriate to use a Monte-Carlo simulation to cope with the complexity of the financial model.
- 24** For a Monte-Carlo simulation a complete model of the project must be constructed and the probability distribution of each of the determinants of the cash-flow specified. The amount of correlation between determinants must also be specified. A computer model should then be used to select random (correlated) values for each of these determinants and calculate net cash-flow for the project. After the model has repeated this process a few thousand times it will yield the probability distribution of the expected cash flow for the project.
- 25** Monte-Carlo simulation can be a useful tool, and the discipline of building a financial model can lead to a deeper understanding of the project. However, Monte-Carlo simulation is a non-trivial task and it should only be used for appraising large and complex projects where sensitivity or scenario analysis does not provide sufficient information about potential cost and benefits.

### **Options analysis**

- 26** All DCF forecasts are based on assumptions about future investment and operating strategy. Inevitably companies will face decisions about pricing, production, expansion and abandonment, but assumptions about these decisions are often buried in the financial model. A financial model may implicitly identify a future strategy for an investment project, but this is unlikely to be the optimal real-world strategy because in practice companies constantly modify their operations. If cash-flows are better than anticipated, the project may be expanded; if they are worse, it may be reduced in scale or abandoned altogether.
- 27** Options to modify investment projects are known as real options. The valuation of real options is beyond the scope of these Guidelines, and it is not necessary to value the options associated with an investment project for the purposes of appraising a GBI application. However, case officers should be aware that unlike in most financial contexts options associated with risky (high-variance) assets are more valuable than options on safe assets. Companies value options (though often not explicitly) when deciding whether to invest in a project, and case officers should consider whether the presence of options in the business plan of the applicant company should influence the level of state support.
- 28** There are four main categories of real options:
- **The option to make a follow on investment**  
Companies often cite “strategic” value when taking on NPV-negative projects. A close look at the project’s payoffs often reveals an option to make a follow on investment that may generate cash flows in addition to those of the initial investment project;

- **The option to wait (and learn) before investing**

This is equivalent to owning a call option<sup>12</sup> on the investment project. The call is exercised when the company commits to the project. It is sometimes better for a company to defer a NPV-positive project than to make the investment immediately. Deferral is most attractive (and the value of the option to defer most valuable) when uncertainty about the project is large, and immediate project cash-flows (which are lost or postponed by waiting) are small;

- **The option to abandon**

The option to abandon a project provides a partial insurance against project failure. This is a put option<sup>13</sup>; the put's exercise price is the value of the project's assets if sold or shifted to a more valuable use; and

- **The option to vary a company's output or its production method**

Companies often build flexibility into their production facilities so that they can use the cheapest raw materials or produce the most valuable set of outputs. In this case they effectively acquire the option to exchange one asset for another.

- 29 Good managers take account of real options when they value a project. One convenient way to summarize real options and their impact on cash-flow is to create a decision tree that sets out what could happen to a project and the main counteractions that the company would take. The NPV of each branch of the decision tree then provides a guide as to which action the company should take at each decision point.
- 30 Decision trees can help to identify the possible impact of real options on project cash-flows. However, the real options encountered in practice are often complex. Each real option introduces its own issues and trade-offs to a project and this can make valuing them difficult.

### **Full Economic Appraisal (FEA)**

- 31 A full economic appraisal (FEA) estimates the value of wider national effects of an investment project. A FEA must be carried out by BERR economists for all cases where the amount of grant is greater than £2m. A FEA is not required for cases where the grant sought is less than £2m as these cases are required only to pass the CET. However, where the CET test is failed, but the case officer believes that there is value in providing state support for the project a FEA should be undertaken.
- 32 The FEA quantifies wider effects that are directly related to the provision of state support. Costs and benefits that are independent of this support and would be defrayed or accrued in a business as usual scenario are not included in the FEA.
- 33 Although the information needed to place precise monetary values on wider costs and benefits of a project will not always be available, it is normally possible to estimate their approximate size (for example, in terms of the number of people affected) and associated uncertainty.
- 34 As a rule of thumb the case for providing state support for an investment project will be stronger if the wider benefits (net of costs) are additional to the direct income effects of the project measured by the DCF test.

12 A call option gives its owner the right to make an investment (such as buying stock) at a specified exercise price on or before a specified date.

13 A put option is the right to sell something (typically a number of shares in a company) at a specified exercise price on (or before) a specified date.

- 35 The FEA is closely related to the market assessment described in Section 5.4. Economists should work closely with market analysts when carrying out a FEA.

### **Externalities**

- 36 The crucial distinguishing feature of all wider benefits, is that they relate to situations where a company undertakes an activity, (e.g. research and development, staff training or polluting a common resource) but does not capture for itself all of the economic benefits, or pay all economic costs, of that activity.
- 37 The wider costs and benefits that the FEA tries to measure are those parts of the business activity for which the company receives no payment or bears no cost, but which have an impact (positive or negative) on other companies or individuals. The presence of these externalities normally results in a sub-optimal investment level and provides a rationale for state assistance or regulation.
- 38 The reasons why a company may fail to receive full payment for the benefits arising from its activities are many. They can arise from the difficulty and costs of establishing property rights (particularly intellectual property rights) and from the need to price new products and processes attractively if they are to gain acceptance in a market uncertain of their true worth.
- 39 Similarly, environmental impacts such as pollution are externalities. A firm might keep down its own costs by not investing in water pollution controls, but in so doing it would raise the costs of those firms and individuals relying on using clean water. As a result the polluter has imposed an external cost on other users, or alternatively, a reduction in pollution confers an external benefit upon these other users.

### **Consumers of project outputs**

- 40 Where a project has an output which embodies a new technology with potential applications in a range of industries (e.g. microprocessors) that may enable new, better and/or cheaper goods and services to be produced, the FEA should examine:
- To what extent will sales of the end product be concentrated in a few user industries;
  - How important is the project output and its innovative element to the competitiveness of users;
  - To what extent are users' costs likely to be reduced by the project output;
  - To what extent does the project output afford users the opportunity of producing new or improved goods and services themselves;
  - To what extent will the project output give UK users access to cost-reducing or product-improving technology before their international competitors; and
  - What value (if any) will accrue to UK users as a result of such earlier access.

**National source of supply**

- 41** Where an investment project establishes a UK source of supply for a project output which was either previously not available in the UK or available only from foreign suppliers on disadvantageous terms, the FEA should examine:
- The structure of the world market for the end product in terms of number, locations and competitiveness of suppliers;
  - The benefits that UK users would enjoy from being geographically closer to their supplier;
  - The evidence that overseas suppliers are unreliable or slow in making the latest technology available to UK companies; and
  - Whether there are any obstacles to entering the proposed market and whether these obstacles are significant.

**Price competition**

- 42** Where an investment project has the potential to stimulate price competition by enabling the company to enter new or previously uncompetitive UK market the FEA should examine:
- Whether the company will be selling the project output into markets in which it was not previously present? If so, how significant will its presence in these new markets be?
  - What is the structure of the markets concerned? Are they competitive?
  - Is the entry of a new company likely to have a significant effect on the degree of competition? Will the new entrant stimulate economic efficiency and cause output prices to be reduced or cause the quality of the goods or services provided to be improved?

**Impact of project on suppliers of other goods and services**

- 43** Where an investment project has the potential to stimulate demand for goods or services provided by other UK companies, the FEA should examine:
- To what extent will demand for goods or services provided by UK companies increase as a result of the project;
  - Whether there are any economies of scale in the production of any of the components or equipment for which there will be increased demand i.e. will increased demand result in lower supply prices for some or all these components or equipment;
  - Whether the project outputs will be usable by wide or limited range of end users;
  - The company's procurement policies and in particular the amount of assistance (if any) that gives to its suppliers in terms of design and quality control;
  - Whether the project will stimulate the development of new and/or improved components or equipment by suppliers, and whether this equipment would have alternative uses.

**Sector competition**

- 44** Where an investment project makes use of a technological advance, the FEA should investigate whether the advance is likely to produce sustainable competitive advantage. In particular the FEA should examine:
- Whether the industry has a good record for quickly identifying and adopting new techniques or technologies;



- Whether there are other companies undertaking similar projects in the same product or technological area; and
- How easily will it be for the company to use patent or copyright laws to prevent competitors making use of the technological advance?

### ***Skills and training***

- 45** The FEA should examine what impact an investment project is likely to have on the skill level of company staff. In particular the FEA should consider:
- Whether labour and management will have to acquire new skills or know-how with potential applications outside the company as a result of the project;
  - Whether any of the skills or know-how likely to be acquired by labour or management in short supply and whether they could be used by other companies;
  - The rate of labour turnover in the occupations whose skills or know-how is enhanced. As the rate of turnover increases a greater part of the benefits of the training accrue to other employers;
  - Whether the project involves a significant amount of research and development, and the extent to which the benefits of this research and development will be captured by other UK companies;
  - Whether new general management techniques will be introduced by the project (for example, just-in-time delivery), and the extent to which other UK companies will benefit from the introduction of these management techniques;

### ***Environmental improvements***

- 46** The FEA should estimate the wider environmental cost and benefits of an investment project. The FEA should highlight:
- Whether the project will have any direct positive or negative impacts upon the environment. For example will the project reduce the level of chemical emissions discharged into the atmosphere;
  - Whether contaminated or waste land be reclaimed; and
  - Whether the public will benefit from the provision of facilities such as public access roads, which would otherwise not be available?

### ***Employment and balance of payments***

- 47** Effects on aggregate employment and the balance of payments do not constitute wider benefits and should not be taken into account in the FEA.

### ***Scale of impact***

- 48** The measurement of any wider costs and benefits will rarely be simple and in many cases it will be impossible to monetise these impacts with any precision. However, it should normally be possible to estimate a range of costs and benefits at the company level, and then extend these to other companies and society. For example the impact of the introduction of a generally applicable new stock management technique which cuts costs by between 5% - 10% will have a far greater impact on the wider economy than the introduction of a process specific component by a company, even if this component has the potential to cut the company's operating costs by more than 10%.



- 49 In reality the introduction of genuinely innovative technology or management techniques will be rare and the majority of projects will only involve iterative product development. Furthermore, the FEA should reflect the fact that the introduction of genuinely innovative technology is unlikely to be dependent on the provision of state aid. However, the provision of state aid can accelerate the adoption of innovative technology and the FEA should attempt to estimate the benefits to society of this acceleration.

### ***Displacement***

- 50 Displacement is the degree to which an increase in an activity promoted by government policy is offset by reductions in the activity elsewhere. Notwithstanding the fact that one of the policy objectives underpinning the GBI scheme is the displacement of economic activity into the Assisted Areas and into the SME sector the FEA should estimate the amount displacement caused by a project, by looking at, for example, the number of competitors and supply linkages.
- 51 In some instances the 'without project' scenario involves the closure of a UK plant, thus the 'with project' scenario is safeguarding jobs (though perhaps only a proportion of existing jobs). In such instances, at a national level it is assumed that the lost jobs will be displaced and taken up elsewhere in the economy, but at a local level, if the number of job losses is relatively large, the impact on the local labour market in terms of its ability to adjust does need consideration.

## Annex K: Information sources

### Private sector databases

- 1 Coverage can include address, product, financial and credit information on registered and unregistered companies, sole traders and directors in the UK and overseas and also market surveys for the UK and overseas. Information cannot be guaranteed to be accurate or up to date.

### Insolvency Service

- 2 The Insolvency Service will undertake checks to ascertain whether or not an individual has been subject to a bankruptcy order since 1973; has been involved in the management of a company that has failed i.e. gone into liquidation, receivership or administration since 1986; has been prosecuted (or proceedings contemplated); has been disqualified as acting as a director. Checks can only be made in respect of individuals or companies domiciled in England or Wales (not Scotland). If a positive match arises the Insolvency Service will provide:
  - in the case of a bankruptcy, full name, address (private or business at the date of order), occupation and if applicable the date of annulment or suspension of discharge. The date of discharge, if obtained, will not be given (most bankrupts are automatically discharged after 3 years);
  - in the case of a company failure, the name of the company.
- 3 In respect of any person who has been involved in the management of a failed company, the Insolvency Service will also state the nature of any return made on their conduct under The Company Directors Disqualification Act 1986. If this is classed as "Fitted" it indicates that there are no adverse matters relating to their conduct in the affairs of the company. However, if their conduct is described as "Unfitted" it indicates that the conduct is such as to make him or her unfit to be concerned in the management of a company.
- 4 If a candidate is positively identified as a bankrupt and/or director of a failed company, the Insolvency Service will, upon further application, check whether or not criminal proceedings have been initiated against the bankrupt/director in the course of, and in relation to, the insolvency. The institution of proceedings does not necessarily mean that the individual was found guilty and convicted.
- 5 Case officers need to send the individual's name, age, current and any known previous addresses to:

Insolvency Service,  
General Services Team - Audit Section,  
Ladywood House,  
45-56 Stephenson Street,  
Birmingham.  
B2 4UZ

Fax: 0121 698 4406

## **Companies House**

- 6** Companies House keeps records of disqualified directors as notified by courts in England, Wales and Scotland. However, case officers should note the following:
- a) the accuracy of the Disqualified Directors Register depends totally on the courts providing the Registrar with Notice of Disqualifications on the statutory forms;
  - b) it takes several weeks for information to reach Companies House from the courts, so a person may have been disqualified but not appear on the Register;
  - c) disqualifications last up to 15 years and are no longer recorded when the disqualification elapses;
  - d) not all offences under the Companies Acts result in disqualification;
  - e) a person may be disqualified in respect of certain activities or companies but not in respect of others. Grant of leave to act in relation to a Disqualification Order is at the courts discretion.

Website address: [www.companieshouse.gov.uk](http://www.companieshouse.gov.uk)

Phone number: 0870 3333636

- 7** It is noted that there may be a hard charge for some of the above services.

## **Receivers**

- 8** Where an applicant has a number of directors who are former directors of a company which went into receivership, case officers should ascertain from the receiver confirmation that:
- the directors are in no way to be criticised or blamed for the winding up of the company;
  - the directors have not, for example, had an Order made against them prohibiting them from being directors or managers of another company;
  - the original company has no right to claim against any of the directors; and
  - no assets from the original company or “know how” save such as may have been properly purchased in the course of the liquidation, are to be used for the project.

## Annex L: Skills test

### Determining the skill level of jobs associated with project

- 1 The jobs created and/or safeguarded by an investment project should be matched to skill levels using the standard occupational classification (SOC). The SOC is an index of occupations, similar to the SIC code for industry. It is possible to look up an occupation to a four-digit level and then match it against a skill level. The SOC is available on the web at:  
  
<http://www.ons.gov.uk/about-statistics/classifications/current/SOC2000/index.html>
- 2 The two relevant documents are SOC2000 Volume 1 and SOC2000 Volume 2. The second volume is the one with the 4 digit coding index.
- 3 From the job descriptions provided by the company in the application form, the case officer will have to look up the occupation in the SOC index. The qualifications provided by the company will usually be a good guide.

### Example 1 - Parceller

- 4 The case officer has to look up 'parceller.' The first step is to find the 4 digit code from SOC2000 Volume 2. There are two columns of SOC codes for each job type the first column is the 1990 SOC code and the second is the 2000 SOC code. For 'parceller' the appropriate SOC code is 9134.

600	3311	Paratrooper
862	<b>9134</b>	<b>Parceller</b>
821	8121	Parchmentiser

- 5 The SOC categorises skills at the 2 digit level. The 2 code associated with a particular job is the first two digits of the 4 digit code. For parceller this is 91 or 'Elementary trades, plant and storage related occupations.' This is then matched to a skill level using Table 1 in SOC2000 Volume 1 (reproduced at the end of this Annex). This table categorises 'parceller' as skill level 1 employment.

Level 1	<b>91</b>	<b>Elementary trades, plant and storage related occupations</b>
862	92	Elementary administration and service

**Example 2 - Steward**

- 6 It is not always straightforward to determine exactly which 4 digit code to use, and in these circumstances the case officer will have to make a value judgement.

190	4114	Steward, shop
441	<b>9149</b>	<b>Steward, shore</b>
621	9224	Steward, wine
621	9224	Steward (catering)
387	3442	Steward (horse racing)
630	<b>6214</b>	<b>Steward (airlines)</b>
621	9224	Steward (canteen)
175	<b>1224</b>	<b>Steward (club)</b>

- 7 There are a large number of occupations listed under steward and the choice can affect the related skill level. From the list below a 'club steward' (1224) is classed at skill level 3, an 'airlines steward' (6214) is at skill level 2 and a 'shore steward' (9149) is at skill level 1.

Level 1	<b>91</b>	<b>Elementary trades, plant and storage related occupations</b>
	92	Elementary administration and service

**Skills test threshold**

- 8 Case officers need to decide whether a case will pass the basic benchmark for the skills criterion. This is a straightforward test. If the majority of jobs are at skill level 2 and above then the project will pass the skills test threshold. If not it will fail.
- 9 When assessing projects case officers should weight jobs in line with skill level to determine the weighted average skill level for the project as a whole. The weighted average of the skill level may be helpful when assessing what level of support would represent value for money:
- each FTE job at skill level 4 or above is given a weighting of 4
  - each job at skill level 3 is given a of weighting 3
  - each job at skill level 2 is given a of weighting 2
  - each job at skill level 1 is given a of weighting 1
- 10 The weighted average is then determined by dividing the total weighted skill level of the project by the total number of FTE jobs.

**Example 3**

- 11** An investment project creates and/or safeguards 60 skill level 4 jobs, 245 skill level 3 jobs, 164 skill level 2 jobs and 40 skill level 1 jobs. The weighted average skill level (WASL) for the project is:

$$\text{WASL} = \frac{(60 \times 4) + (245 \times 3) + (164 \times 2) + (40 \times 1)}{60 + 245 + 164 + 40}$$

$$= \frac{1343}{509} = 2.63$$

- 12** The weighted average skill level for this project is 2.6.

**Skill levels and the sub-major group structure of SOC2000**

- 13** Table C reproduces the data from the summary table on page 6 of SOC2000 Volume 1.

Skill Level		Sub-major groups of SOC2000
Level 4	11	Corporate managers
	21	Science and technology professionals
	22	Health professionals
	23	Teaching and research professionals
	24	Business and public service professionals
Level 3	12	Managers and proprietors in agriculture and services
	31	Science and technology associate professionals
	32	Health and social welfare associate professionals
	33	Protective service occupations
	34	Culture, media and sports occupations
	35	Business and public service associate professionals
	51	Skilled agricultural trades
	52	Skilled metal and electrical trades
	53	Skilled construction and building trades
	54	Textiles, printing and other skilled trades
Level 2	41	Administrative occupations
	42	Secretarial and related occupations
	61	Caring personal service occupations
	62	Leisure and other personal service occupations

	71	Sales occupations
	72	Customer service occupations
	81	Process, plant and machine operatives
	82	Transport and mobile machine drivers and operatives
Level 1	91	Elementary trades, plant and storage related occupations
	92	Elementary administration and service occupations

## Annex M: Cumulation

- 1** The following forms of assistance should be included in the gross grant equivalent calculation in addition to GBI investment aid, where it is provided in respect of the same project:
  - a) rent free periods on publicly owned facilities. If the value of the annual rental is not known, an estimate should be made. The value of the rental may be discounted;
  - b) loans from any public body at below commercial rates;
  - c) local authority assistance, such as capital grants and loans at below commercial rates; loan guarantees which lower the cost of capital of the applicant company and rent free periods;
  - d) assistance provided towards training that involves different identifiable eligible costs. The use of supplemental training aid for projects in Tier 1 and Tier 2 is covered in Annex E;
  - e) lottery funding (very exceptionally where a project does not involve commercial competition, it may not be necessary to cumulate).
- 2** Where project expenditure includes the costs of special equipment funded or part funded by the Ministry of Defence, the GBI aid ceiling for the project must be reduced by an amount equal to the subsidy provided by the MOD.
- 3** Department for Work and Pensions employment measures and Learning and Skills Council training assistance which is based on national schemes directly aimed at benefiting individuals and are therefore not project related should not be cumulated.

### Loans and Guarantees

- 4** The Commission is concerned only with the subsidy value of a loan or guarantee. For a loan this is the difference between the actual interest rate and the current discount rate. If the loan is repaid in one instalment, the gross grant equivalent is the discounted value of the subsidy. If the loan is repaid in several instalments allowance must be made for the fact that the balance of the loan is reducing and the subsidy for each year is therefore only calculated on the level of the loan outstanding.
- 5** The value of a guarantee is the difference in the commercial interest rate that the recipient company is charged on a loan compared with the commercial interest rate that would have been incurred if the loan had not been guaranteed.



## Annex N: Dealing with companies in financial difficulties

- 1 This Annex sets out the procedures when dealing with companies in financial difficulties. It provides guidance and sets out the legal process with respect to:
  - Practical implications for GBI claims
  - Fraudulent or wrongful trading
  - Fraudulent applications
  - Insolvency
  - Liquidation and dissolutions
  - Receivership, administration and voluntary arrangements
  - Recovery and write-off
- 2 GBI procedures require an appraisal of the merits of individual projects. Examination of the initial case and its viability, and the continuing scrutiny involved in monitoring, inevitably means that the operating departments possess information which does, or could be held to, provide a knowledge of the company's affairs. The operating department is therefore vulnerable in its dealings with companies in financial difficulties. As a general rule, operating departments should not provide assistance to a company which is in a situation where it cannot pay its debts as they fall due. Therefore, for reasons of law as well as best practice, case officers must establish as far as possible that the company is or remains capable of carrying out the project, both before any assistance is given and as part of project monitoring.

### Practical implications for GBI

- 3 A first requirement in responding to a company's request for financial assistance when it is in jeopardy, or where the situation arises in the course of assistance being paid, is to protect the operating department's position.
- 4 The company should immediately be informed that:
  - a) the operating department will consider the request for assistance or for grant payment urgently; but
  - b) the company cannot assume that assistance will be provided;
  - c) the directors cannot take the approach to the operating department into account in considering their own position under the Companies or Insolvency Acts;
  - d) decisions on the running of the company are for the directors of the company to make; and
  - e) the operating department in no way takes upon itself any responsibility for the company continuing to trade.
- 5 This notification should be confirmed in writing to a director of the company. The same line should be taken in response to any queries from the banks or other creditors about the operating department's attitude. The points should also be made as appropriate where a request for deferment of repayment is received. Where, exceptionally, assistance is provided to a Receiver, there should be no implications since all who assist the Receiver do so in full knowledge of the status of the business.

- 6 Continued trading by a company losing money is likely to lead to creditors suffering greater losses. Consequently, even though the operating department has taken steps to avoid any implications for itself, there is still an obligation to deal with the approach as expeditiously as practicable. However, it is important, not to mislead the company on how long a decision might take. Where a negative decision is possible without detailed appraisal, this should be indicated to the company as soon as possible.

### **Appraisal**

- 7 GBI should only be made available to projects which are considered to be viable. Provided the provisions in paragraphs 4 and 6 of this Annex are met, the refusal of assistance to a project which is not viable, or acceptance of the possibility of the provision of assistance at a later date to enable viable elements of the business to be acquired from a Receiver and continued under new ownership as set out in Section 8.6 will not create further implications for the operating department.
- 8 All applications which might be considered operating aid for companies in difficulties in England must be handled by BERR.

### **Monitoring**

- 9 Grant instalments should only be made if the monitoring officer is satisfied that the company can pay its debts as they fall due. When it is not clear from routine monitoring information whether or not this requirement can be met, further information must be sought from the company in order to avoid the risk of fraudulent or wrongful trading and to avoid wasting public funds should the company go into liquidation after the grant has been paid.

### **Fraudulent or wrongful trading**

*This background is based on Chapter 16, section 2 of the BERR Finance Handbook, but is also intended as a guide for Scottish Executive and National Assembly for Wales.*

- 10 When dealing with companies in financial difficulties, it is important that case officers are aware of the risks to their operating departments through fraudulent or wrongful trading. An explanation of what this means is given below.

### **Fraudulent trading**

- 11 Under section 993 of the Companies Act 2006 it is an offence for anyone to carry on any business of a company with the intention of defrauding the creditors of the company or the creditors of anyone else; or for any fraudulent purpose; or to be knowingly party to the carrying on of business in either of these ways.
- 12 In addition, in the course of winding up a company, a Liquidator may, under section 213 of the Insolvency Act 1986, apply to the civil court for a declaration that anyone who was involved in a fraudulent carrying on of a business is liable to contribute to the company's assets, if it appears that fraudulent trading has occurred.

### ***Wrongful trading***

- 13** When a company goes into liquidation, a Liquidator is appointed to try and ensure that all the company's creditors are correctly paid. To meet the company's debts, the Liquidator needs to assess all the company's assets, and may look also at the assets of the directors and any "shadow directors" of the company. The risk of involvement in wrongful trading arises when a company goes into liquidation and officials act in a manner that causes the Liquidator to regard them as "shadow directors."
- 14** A "shadow director" is defined in section 251 of the Insolvency Act 1986 as a "person in accordance with whose directions or instructions the directors of the company are accustomed to act..." The identification of a shadow director will depend on the facts of any particular case, and officials should avoid acting in a way that suggests they or the Department could be shadow directors.
- 15** If it appears to the Liquidator that, at some time before the winding up began, a director or shadow director knew or ought to have known that there was no reasonable prospect the company would avoid going into liquidation, the Liquidator may make an application to the civil court for a declaration that the director or shadow director be liable to contribute to the company's assets.
- 16** Before making such a decision, the court will consider, under section 214 of the Insolvency Act 1986, whether the director or shadow director took every step possible to minimise the loss to the creditors (assuming he or she knew there was no reasonable prospect that the company would avoid going into liquidation).
- 17** The operating department should not be drawn into substantial involvement in the decision-making processes of a company during a time when it is in financial difficulties. If the decisions made by the company in that period are taken as a result of discussions with the operating department, or by the directors subject to the operating department's approval (whether in a detailed day to day basis or within a framework of strategic approval), the operating department runs a considerable risk of being held to have become a shadow director of the company during the period of financial difficulty, and of therefore being liable to make a contribution to the company's assets. The risk will be much greater where the operating department has exercised this type of control before the financial difficulties became apparent.

### **Fraudulent applications**

- 18** This section explains the procedures when fraudulent applications are made and the responsibilities of appraisal officers when it happens. It is important that appraisal officers know what the procedures are. Fraud occurs where there has been some false pretence or deception on the part of the accused which has produced a definite practical result which need not be prejudicial to the victim. Fraud includes the falsification of documents and the true certification of facts known to be wrong.
- 19** The fact that information is incorrect does not mean it is fraudulent. For example, it could be a genuine mistake or a misinterpretation of information. Any suspected irregularity should be treated cautiously and sensitively by operating department officials.
- 20** Information should be sought for regarding the financial history of the

company. For example, the local Official Receiver may have information concerning liquidations, the Insolvency Service may have pursued civil disqualification proceedings against one of the directors, Companies House can provide copies of filed accounts and there is a register of bankrupts held by the Insolvency Service in Birmingham. If a company is based abroad, similar sources of information held in that jurisdiction may be available. For Scottish cases, section S of the SOFM and section 37 of Government Accounting provide some further guidance related to fraud and staff should also consult the Scottish Executive's Fraud Response Plan on the Scottish Executive intranet.

- 21 If a case officer suspects that an application contains false information or supporting documentation does not appear authentic, further detail and clarification should be sought, but allegations should not be made. It is not uncommon for the applicant to withdraw in these circumstances if the information is not verifiable.
- 22 If operating departments have doubts during the vetting or monitoring of a project, they should seek to clarify the issues with all those involved (i.e. not only the applicant). For example, unannounced visits to premises and research on the background of the applicant are two good ways to raise further awareness of the project. If suspicions are confirmed legal and management advice should be sought before any allegations are made.
- 23 If evidence gathered by the operating department suggests that a criminal offence has been committed, then the matter should be referred quickly (and following internal procedures) for possible legal action.
- 24 Only copies of documents related to a GBI case should be distributed. The original documents should be kept safe by the GBI unit of the operating department.
- 25 Officers must not under any circumstances give an assurance to an applicant that criminal proceedings will not follow. If case officers have sufficient information to show that a criminal offence has been committed (and the applicant is unhappy at the delay in processing the application or thinks he has been found out), then case officers should only say that the papers have been referred to the operating department's legal team for further consideration.

### ***Common offences which give rise to prosecutions in grant fraud cases***

- 26 While Case Officers are not expected to know the detailed provisions of the Theft Act ("TA") 1968 or any other Act, they should be aware of the most common offences under this Act which give rise to prosecutions in grant fraud cases. These are as follows:
  - section 1 TA 1968: theft (i.e. stealing property)
  - section 15 TA 1968: obtaining property (e.g. money) by deception
  - section 15A TA 1968: obtaining a money transfer by deception (i.e. by CHAPS or BACS)
  - section 17(1)(a) and (b) TA 1968: false accounting: (a) falsifying a document made or required for an accounting purpose; (b) producing or making use of a misleading, false or deceptive document which is made or required for an accounting purpose

### ***Making a witness statement***

- 27** Case officers who have been involved in the grant application process may be called upon to make a witness statement. When this occurs, it is important that:
- the statement accurately reflects the case officer's recollection of the events in question;
  - the case officer does not rely on the assistance of others if the case officer does not know all of the facts. Case officers may be called as witnesses to give evidence and be cross examined on the accuracy of their statement's contents;
  - case officers may receive help from a legal investigator or Police officer in putting the statement together in a concise form. However, the case officers must be comfortable that the wording of the statement accurately reflects what happened.
- 28** It is important that the case lawyer or prosecution counsel are made aware of any events that may have a bearing on the case that occur after the referral of the case papers.

### ***Commencement of criminal proceedings in England and Wales***

- 29** It is important that case officers are familiar with the legal process; which prosecution material documents may be disclosed and how they are expected to conduct themselves in court.

### ***The legal process***

- 30** If a case officer is a witness, they may receive correspondence from the Law Clerk informing them of the progress of the case or requesting dates of availability for attendance at a trial.
- 31** The case lawyer (or an appointed agent) will appear at the magistrates' court. Some cases are dealt with entirely in the magistrates' court. However, others, because they are very serious or because the defendant chooses so, are dealt with at the crown court. If the case is transferred or "committed" to the crown court, the case lawyer will brief Counsel (a barrister) or a solicitor advocate. In most cases involving grant fraud, it is likely that the case will be heard in the crown court.
- 32** If the defendant pleads guilty to the charges (listed on a "summons" in the magistrates' court or an "indictment" in the crown court), it is unnecessary for the witnesses to attend court and the defendant can be sentenced by the Magistrates or the Judge. If not, the case will be adjourned to a fixed trial date and directions will be given as to the conduct of the case (e.g. service of additional evidence, schedules of transactions etc.) at a plea and directions hearing or a pre-trial review. Depending on the number of witnesses, the trial could last from a couple of days to many weeks. Most last a couple of weeks. Each witness may only be required for an hour or two.

### ***Disclosure of prosecution material***

- 33** Prosecutors have a duty to disclose to defendants material, i.e. such as file notes, other forms, company papers etc. which may help their case. Under the Criminal Procedure and Investigations Act 1996 this is a two stage disclosure process:
- Primary disclosure of all material which might undermine the prosecution's case against the defendant; and

- Secondary disclosure which only applies once the defendant has served a statement of his defence. It is only compulsory to serve such a statement in cases being tried in the Crown Court. If he does so, then any material which might reasonably be expected to assist the accused's defence should be disclosed.

### **Conduct in court**

- 34** Case officers may be required to give evidence as a witness in court. If this happens case officers should answer the questions put to them by counsel in a fact based and concise manner. Case officers should not make speeches or present arguments.
- 35** Case officers are allowed to read their witness statements outside court to refresh their memory. If a case officer is asked a question which requires research, then the case officers should say so. The case officer should not under any circumstances guess at an answer or be evasive.
- 36** As a witness case officers cannot take sides. If a case officer has to admit something that they believe is harmful to the prosecution case, they should do so if this is a fair representation of the facts. Case officers should draw conclusions only if asked to do so. If asked to provide a "yes" or "no" answer to question, the case officer must consider whether this is appropriate. If the case officer believes that a "yes" or "no" answer would be inappropriate it is important to say so. The case officer may explain to the judge why this is the case. In these circumstances the judge is likely to allow the case officer to answer the question in his or her own words.
- 37** It is vital that case officers are well prepared. Case officers should arrive at the court early carrying any necessary documentation. Case officers should be prepared for a long wait as the start of a trial can be delayed by legal argument.

## **Liquidations and dissolutions**

### **Insolvency**

- 38** The Insolvency Service (IS) can undertake checks to ascertain whether or not an individual has been subject to a bankruptcy order since 1973; has been involved in the management of a company that has failed, i.e. gone into liquidation, receivership or administration since 1986; has been prosecuted (or proceedings contemplated); has been disqualified as acting as a director. Checks can only be made in respect of individuals or companies domiciled in England or Wales (not Scotland). If a positive match arises, case officers will be provided with:
- in the case of a bankruptcy, full name, address (private or business at the date of order), occupation and if applicable the date of annulment or suspension of discharge. The date of discharge, if obtained, will not be given (most bankrupts are automatically discharged after 3 years); or
  - in the event of a company failure, the name of the company.
- 39** There are three types of liquidation: winding up, voluntary liquidation and compulsory liquidation. Each process and the relevant procedures are described below.
- 40** Winding up ("liquidation") is the first stage in a process by which the existence of a company is terminated. Some companies are dissolved, however, without insolvency proceedings. The Insolvency Act 1986 provides that a company may be wound up compulsorily by the court or voluntarily by the members (shareholders) or creditors.

- 41** Voluntary liquidation follows a resolution by the company members that it should be wound up. In a members' voluntary liquidation, the Board must first make a statutory declaration that the company is solvent. The Members appoint the Liquidator. If there is no such declaration, or the company is found not to be solvent, it is a creditors' voluntary liquidation, where the creditors have primary power to appoint the Liquidator.
- 42** Compulsory winding-up most commonly follows a petition to the Court from a creditor on the basis that the company is unable to pay its debts. For example, the company is indebted to the creditor for a sum exceeding £750 which it has failed to pay (or otherwise made arrangements to the reasonable satisfaction of the creditor) within 3 weeks of being duly served with a written demand in the prescribed form. There are, however, wide powers for interested parties to petition the court on a number of other possible grounds. Unless the court orders otherwise, the Official Receiver, by virtue of his office, becomes Liquidator on the making of a winding up order. An insolvency practitioner may subsequently be appointed as Liquidator in place of the Official Receiver by the creditors or contributories, the court or the Secretary of State.

### ***Powers and duties of the Liquidator***

- 43** In a winding up, the management of a company's affairs is taken out of its directors' hands and placed in those of a Liquidator. The Liquidator has to establish the liabilities of the company and realise the assets to satisfy those liabilities in due order of priority and as fully as possible. Any balance of funds remaining after the expenses of the liquidation and liabilities have been met is distributed among the members according to their rights or to the persons entitled to it.
- 44** The company is subsequently dissolved, usually three months after the Liquidator notifies the Registrar that the liquidation is completed.

### ***Meetings of creditors***

- 45** Meetings of creditors are convened in accordance with the Insolvency Act and the Insolvency Rules 1986. In a compulsory liquidation, the Official Receiver must decide whether to summon first meetings of creditors for the purpose of appointing a Liquidator other than the Official Receiver. Generally, resolutions may be passed at first meetings of creditors in both creditors voluntary and compulsory liquidation in order to, for example, establish a liquidation committee or specify the terms on which the Liquidator is remunerated.
- 46** The Liquidator has a statutory duty in certain circumstances to summon periodic meetings of creditors at which, for example, he is required to report on the conduct of the liquidation. Where the Department is an unsecured creditor, it may be appropriate to attend the creditors' meeting and to vote

### ***Liquidation Committee***

- 47** The Liquidator is required to report regularly to the liquidation committee, which is a committee of the creditors, and certain of his powers can be exercised only with the sanction of the court or the liquidation committee. In those liquidations where the Official Receiver is Liquidator, or where a liquidation committee is not established, the functions of the liquidation committee are exercised by the Secretary of State, the Scottish Ministers or the National Assembly for Wales. It is preferable that the operating department should neither seek, nor accept, nomination to the liquidation committee unless there is some special reason for doing so.



***Dissolved companies***

- 48** Under section 652 of the Companies Act 1985 (or sections 1000, 1001 and 1002 of the Companies Act 2006 when they come into force), the Registrar of Companies may strike a company name off the register and dissolve it if he believes that the company is no longer trading. If no response is received from two letters issued to the company's registered office enquiring if it is still in business, a notice is published in the London Gazette stating the intent to strike off the company in 3 months. If cause has not been shown to the contrary, the company is subsequently dissolved by notice in the London Gazette. If an objection is received, the Registrar may delay strike off. Assets held by a company are passed, in most cases, to the Crown.
- 49** A company which is being dissolved is rarely likely to have significant assets. If the company has been dissolved, a GBI offer letter would no longer have effect and there would be no company assets. There will therefore normally be no point in pursuing such cases unless there are wider interests, most particularly the possibility of fraud. The cost involved in restoring the company to the register, which requires court action, is unlikely to be justified.

**Receivership, administration and voluntary arrangements*****Receivership***

- 50** A Receiver, including an administrative Receiver, is appointed for the purpose of realising sufficient funds or assets of a company in order to meet the claims of the secured creditor or creditors who appointed him. Once the debt is fully discharged the Receiver ceases to act.
- 51** Some types of creditors, for instance banks providing loans, will require security in the form of a charge on company assets. The terms are set out in the document creating the charge. If there is a fixed charge (i.e. secured against identified assets), the Receiver's role will be to realise the value of those particular items sufficient to pay the creditor.
- 52** If the creditor has a floating charge over all, or substantially all of the company's assets, he may be entitled to appoint a Receiver and manager, who is called an administrative Receiver. He usually acts as agent to a company.
- 53** The Receiver's powers are set out in the charge document and, for an administrative Receiver, in Schedule 1 to the Insolvency Act 1986. They usually include:
- a) power to take possession of all the property charged;
  - b) for an administrative Receiver, power to carry on, or to concur in the carrying on of, the business of the company;
  - c) power to sell, or concur in the selling of, all the property charged; and
  - d) to make any arrangements or compromise which the Receiver considers expedient in the interest of the debenture holder.
- 54** The priority of debts in administrative receivership is:
- a) debts due to fixed charge holder creditors;
  - b) preferential debts (for example, certain sums owed to the Inland Revenue and Customs and Excise, Social Security contributions, contributions due to occupational pension schemes, employees remuneration);
  - c) debts due to the floating charge holder.



- 55** Subject to the terms of the charge document under which the Receiver is appointed, it is the sole responsibility of the Receiver to decide what action to take once he is appointed. An administrative Receiver usually makes an initial visit to the company to assess the situation: the broad decision is taken as to whether to carry on the business of the company or to close it down and realise the assets. Subject to the availability of funds to pay wages and to acquire essential trading stocks, his initial decision is usually to complete contracts and continue the business for a limited period while he makes a fuller assessment of the possibilities. This leads to one or more of the following courses of action:
- a) continued trading in order to achieve an orderly rundown of stocks or to complete some partly executed orders;
  - b) continued trading to allow time for the negotiation of an arrangement of the kind described below;
  - c) continued trading on a longer term basis. This may be justified if the Receiver sees prospects of the company being restored to a profitable basis; and
  - d) arranging a sale of the assets, including goodwill, with or without all or some of the liabilities.
- 56** The secured creditor who appoints the Receiver may replace him if he so wishes. An administrative Receiver can only be removed by the court.

### ***Unsecured creditors***

- 57** Operating departments are normally unsecured creditors. The administrative Receiver has no obligation to meet the amounts outstanding to unsecured creditors incurred before his appointment. Operating departments need to petition for the winding up of the company if their claims are not met. However, this process should not be initiated as part of a GBI claim. An administrative Receiver can himself petition the court for a compulsory liquidation.
- 58** The only obligation the administrative Receiver has to unsecured creditors is informational:
- a) Every company letter, invoice or order for goods must state that the company is in receivership.
  - b) The administrative Receiver must tell all creditors within 28 days that he has been appointed. He must also advertise his appointment in the Gazette and in the news- paper which he considers most appropriate for ensuring that it comes to the notice of creditors.
  - c) The administrative Receiver is required within 3 months of his appointment to prepare a report covering: the events leading to his appointment; his disposal of assets of the company and the extent to which he is carrying on the business of the company, as appropriate, and any proposals for these; the amounts payable to the debenture holders who appointed him and to preferential creditors; and the amount likely to be available for the payment of other creditors.
  - d) The report should have attached to it a copy of the summary of the statement of affairs produced by officers, or previous officers of the company showing assets, debts liabilities and various other information. However, the report need not include any information likely to seriously prejudice the carrying out of the administrative Receiver's functions.

- e) The administrative Receiver is required to send the report to the Registrar of companies, to any trustees for secured creditors and to all secured creditors. If a Liquidator is appointed, the administrative Receiver must also send a copy to the Liquidator. If the administrative Receiver is able to send the report to the Liquidator within 3 months of his appointment as administrative Receiver, then he does not have to send the report to unsecured creditors or communicate it to them in any way. However, if the report is not sent to the Liquidator within the 3 month period, then the Receiver must:
- either send a copy of the report to all unsecured creditors; or publish a notice in the newspaper in which his appointment was advertised stating that the report is available on request; and
  - present a copy of the report to a meeting of the unsecured creditors, unless the court otherwise directs. If that meeting appoints a creditors' committee, the administrative Receiver can be required to meet them and provide them with such information as they may reasonably require.

**59** The Insolvency Act 1986 introduced a procedure whereby a company that is, or is likely to become, unable to pay its debts may obtain a moratorium on actions for repayment of debts by creditors while, under a court administration order, a qualified insolvency practitioner (the administrator) formulates a plan for dealing with the company. In effect the order normally needs to be agreed by all the secured creditors who are entitled to appoint an administrative Receiver.

**60** It must be agreed by any creditor who had actually appointed an administrative Receiver. An administrator has three months in which to prepare proposals and to put them to a meeting of the company's creditors. The aim is normally likely to be the survival of the company. If the creditors' meeting agrees a proposal, the administrator is required to manage the business accordingly. If the meeting doesn't agree to the proposals the administration order may be discharged by the court. The moratorium on creditor action also prevents the company being wound up or an administrative Receiver being appointed. The administrator must apply to the court for the Administration Order to be discharged or varied if the purpose for which it was made has been achieved, is incapable of achievement or if he is required to do so by a duly convened meeting of the company creditors.

### ***Voluntary arrangements***

**61** Under the Insolvency Act 1986, a CVA is an arrangement between a company (which could be proposed by its directors, an administrator or Liquidator) and its creditors. The CVA's purpose is to give the company a breathing space by delaying and/or reducing debt payments to creditors so that it can continue. Meetings of the company's creditors and of the company's members (shareholders) are summoned. Providing that a 75% majority of the creditors' meeting and a simple majority of the members meeting approve the proposed arrangement, a CVA is binding on all creditors who had notice of the meeting and were entitled to vote.

### ***Recovery and write-off procedures***

**62** Receivership, Administration and Voluntary Arrangements might all result in the survival of a company and its project. If it becomes clear that a project will not survive, procedures for recovery and write-off, including in liquidation cases, will need to be followed.

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