



# **JESSICA**

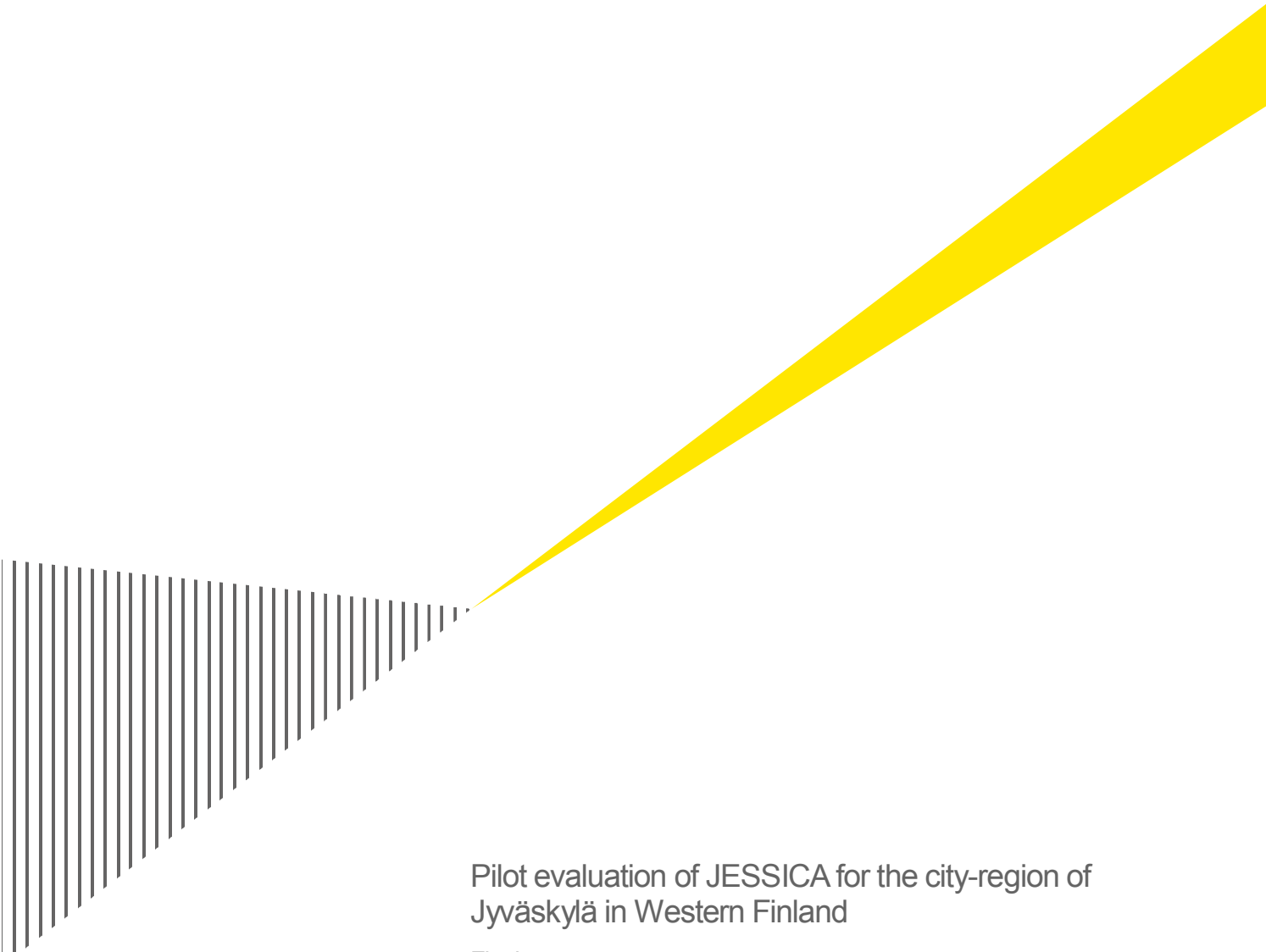
***JOINT EUROPEAN SUPPORT FOR  
SUSTAINABLE INVESTMENT IN CITY AREAS***

***JESSICA in Western Finland***

**EVALUATION STUDY**

**December 2009**

This document has been produced with the financial assistance of the European Union. The views expressed herein can in no way be taken to reflect the official opinion of the European Union.



Pilot evaluation of JESSICA for the city-region of  
Jyväskylä in Western Finland

Final report

9 December 2009

Ernst & Young Oy

**JESSICA Task Force  
European Investment Bank  
100, Bvd. Konrad Adenauer  
L-2950 Luxembourg  
Luxembourg**

23 November 2009

Dear Sirs

In accordance with instructions from the JESSICA Task Force at the European Investment Bank, we have completed our study into the feasibility of implementing the Joint European Support for Sustainable Investment in City Areas (JESSICA) in the city-region of Jyväskylä within the context of the ERDF Operational Program for Western Finland.

Our report to you is based on our examination of data and information received from a range of organizations including the Finnish Ministry of Employment and the Economy, the city of Jyväskylä, the Regional Council of Central Finland, the Employment and Economic Development Centre of Central Finland, the European Investment Bank, and the case study organisations. We have not sought to verify the accuracy of this data or information.

This report contains information in summary form and is therefore intended for general guidance only. It is not intended to be a substitute for detailed research or the exercise of professional judgment. Furthermore, our report may not have considered issues relevant to any third parties. Neither Ernst & Young Oy nor any other member of the global Ernst & Young organization can accept any responsibility for loss occasioned to any organization or person acting or refraining from action as a result of any material in this publication.

Our work was completed by 20 October, 2009. This report does not take account of any events or circumstances occurring after the completion date. Any forward looking estimates and statements are subject to change based on market events and decisions and actions taken by different parties.

Helsinki, 23 November 2009

Ernst & Young Oy

Tuija Korpelainen  
Partner

Mette Vilos  
Partner

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© 2009 Ernst & Young Oy, Elielinaukio 5 B, FI-00100 Helsinki, Finland  
Telephone +358 207 280 190, fax +358 207 280 199  
Business ID 2204039-6, domicile Helsinki  
[www.ey.com/fi](http://www.ey.com/fi)

# Abbreviations and Terminology

| <b>Abbreviation / Term</b>       | <b>Name / Description</b>  |
|----------------------------------|--|
| EIB                              | European Investment Bank   |
| ERDF                             | European Regional Development Fund   |
| ESF                              | European Social Fund   |
| EU                               | European Union   |
| Financial Engineering Instrument | In the context of Structural Funds and JESSICA, “Financial Engineering Instrument” refers to new ways of deploying capital from Structural Funds as investments into development funds as an alternative to traditional grants                             |
| JESSICA                          | Joint European Support for Sustainable Investment in City Areas  |
| MEE                              | Ministry of Employment and the Economy in Finland  |
| N+2 challenge                    | The challenge arising from the stipulation in the Structural Funds regulation that funds have to be spent by a Member State within two years of the particular year for which they were allocated, or otherwise they have to be returned to the Commission |
| Member State                     | Member States that are part of the European Union.   |
| PPP                              | Public-private partnership   |
| Structural Funds                 | Contain funds from the EU set up to target specific areas. The ERDF is the Structural Fund that will be used for part of the JESSICA program.  |
| The Commission                   | The European Commission (formally the Commission of the European Communities)  |
| UDF                              | Urban Development Fund   |
| WFOP                             | ERDF Operational Program for Western Finland (or Western Finland Operational Program)  |

## 1 Executive summary

JESSICA is a new initiative enabling EU member states to deploy a share of their grants from EU's Structural Funds as repayable investments into projects for sustainable urban development. The return on investment may then be used for other regeneration and development projects, providing a revolving fund. This report is an assessment of the feasibility of implementing JESSICA in the context of the Western Finland Operating Program (WFOP) for Structural Funds deployment. The assessment is based on a pilot evaluation study in the city region of Jyväskylä.

We found that in the city region of Jyväskylä there is a need for new forms of financing for urban development, and there are several development projects which could potentially benefit from JESSICA funding. Most of these projects are aimed at developing new business facilities that are needed to support the creation of new enterprises and jobs in the city region. New employment opportunities are urgently needed to replace those that are being lost in the ongoing structural change in the Finnish economy. All of the projects are estimated to contribute to the creation of new sustainable employment opportunities in Jyväskylä. In this way, these projects would contribute to the achieving of the employment objectives of the WFOP. Supporting these projects with a JESSICA instrument using Structural Fund resources from the WFOP could thus be justified.

However, the possible grant allocations from EU Structural Funds for a JESSICA Urban Development Fund (UDF) in Jyväskylä are substantially smaller than needed in order to obtain an efficient fund structure. While the size of the projects ranges from some EUR 10 to 50 million each, the total Structural Fund allocations and public match funding available for urban development in Jyväskylä is some EUR 2-6 million. Additional public funding on a city, regional, province or state level is unlikely. Additional private funding into an UDF is possible but not evident according to interviews made in the study. The situation is similar in other cities in Western Finland, such as Vaasa and Tampere.

It would be beneficial for the city-region as well as for the WFOP as a whole if new forms of funding could be mobilized to accelerate the development of premises and other types of infrastructure in the city-region to support the creation of new businesses. However, the structural funds available for JESSICA appear to be too small to achieve a fund of sufficient size to have any real impact on the development in Jyväskylä. Based on this study we are therefore not in a position to recommend an implementation of the JESSICA instrument in Jyväskylä in the current Structural Funds program period. For similar reasons, we are also unable to recommend an implementation of JESSICA in the other city-regions in Western Finland.

Some further assessment could be made of the possibility of utilizing JESSICA within the Eastern Finland Operational Program, which has a larger amount of funds to allocate than the WFOP. We also recommend exploring whether JESSICA could be utilized in the next Structural Funds program period. We further recommend looking into other possibilities to realize urban development through various forms of public-private partnership.

## 2 Introduction

### 2.1 Background

#### 2.1.1 JESSICA

The Joint European Support for Sustainable Investment in City Areas (JESSICA) is an initiative developed by the European Commission and the European Investment Bank (EIB), in collaboration with the Council of Europe Development Bank (CEB).

Under this initiative, Member States are given the opportunity to use grants from the European Regional Development Fund (ERDF) through new financial engineering mechanisms in order to support projects forming part of integrated plans for sustainable urban development. According to ERDF Regulation 1080/2006, §8, which includes the scope of JESSICA, “sustainable urban development” should promote activities such as:

- ▶ Strengthening economic growth
- ▶ Rehabilitation of the physical environment
- ▶ Brownfield redevelopment
- ▶ Preservation and development of natural and cultural heritage
- ▶ Promotion of entrepreneurship, local employment and community development
- ▶ Provision of services to the population taking account of changing demographic structures

Investments in urban development projects are made through Urban Development Funds (UDF), which are capitalized with EU Structural Fund grants and additional public or private match funding. The UDF's invest in projects by providing loans, equity or guarantees. Additional private or public capital can be sought on project level but is not counted as match funding to the UDF. The UDF investments need to be recoverable, so that the funds can be reinvested into other projects, thus creating a lasting legacy of investment.

JESSICA is not a new source of funding, but a new way of using existing Structural Fund grant allocations to support urban development. The key potential benefits for Member States that are sought by implementing JESSICA are:

- ▶ Sustainability by retaining and recycling funds after the end of the operational program
- ▶ Greater accountability and stronger incentives towards better performance by converting grants to repayable investments

- ▶ Achieving a lower return requirement than with private capital alone, thus enabling investment in locations that would otherwise fail
- ▶ Leverage effect of using grants to attract and combine with private capital
- ▶ Ability to immediately draw down Structural Funds allocated for the whole program period, and thus accelerate activities while also helping to deal with the challenge that the funds allocated for a particular year have to be spent within two years of the allocation year (the so called “N+2” challenge)
- ▶ Ability to unlock structural funds that could otherwise not be utilized
- ▶ New sources of expertise and know-how from private actors through public-private partnerships (PPPs)
- ▶ Development and modernization of financial markets by utilizing EU Structural Funds grants in a new and innovative way

The JESSICA operating framework was provided in the EU Structural Funds legislative package for the period 2007 to 2013 and a number of studies have since been undertaken by the EIB and Member States. Further information about the JESSICA instrument can be found on the web pages of the European Commission<sup>1</sup> and the EIB<sup>2</sup>.

The EIB, in partnership with the Ministry of Employment and the Economy in Finland, has requested Ernst & Young Oy to assess the initial feasibility of implementing JESSICA in Western Finland, based on a pilot evaluation study in the city-region of Jyväskylä. This report is the result of this study.

## 2.1.2 Project eligibility criteria

At a European level, there are six key criteria that an investment must meet in order to be financed with ERDF funds through the JESSICA instrument:

- ▶ Expenditure must be incurred and recorded in a Statement of Expenditure by the end of 2015
- ▶ The project must be part of an integrated plan for sustainable urban development
- ▶ The project must have sufficient eligible component expenditure and also take into account any national eligibility criteria
- ▶ The project must be capable of providing a return so that the capital invested can be repaid to the UDF

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<sup>1</sup> [http://ec.europa.eu/regional\\_policy/funds/2007/jjj/jessica\\_en.htm](http://ec.europa.eu/regional_policy/funds/2007/jjj/jessica_en.htm)

<sup>2</sup> [http://www.eib.org/products/technical\\_assistance/jessica/index.htm](http://www.eib.org/products/technical_assistance/jessica/index.htm)



- ▶ The necessary documentation must be in place
- ▶ Public match funding must be provided

### 2.1.3 EU Structural Funds for urban development in Jyväskylä

In Finland, EU grants are delivered from the following EU Structural Funds:

- ▶ The European Regional Development Fund (ERDF)
- ▶ The European Social Fund (ESF)

The planned allocation of these funds is detailed in Operational Programs. Jyväskylä is included in:

- ▶ The ERDF Western Finland Operational Program (WFOP)
- ▶ The national ESF Operational Program for mainland Finland

ERDF support within WFOP is around EUR 159 million for the period 2007-2013 and the total public match funding is EUR 239 million. This means that EU's share of the total public funding for regional development is 40% and by consequence in a potential JESSICA scheme as well. The support for urban development within the city-region of Jyväskylä will mainly fall within the WFOP priority axis 3, "*Improvement of the accessibility of regions and of the operating environment*". The ERDF funding for priority axis 3 in Western Finland is EUR 27 million.

Within the ESF Operational Program for mainland Finland EUR 78 million is reserved for Western Finland. ESF funding may be used as additional funding according to JESSICA regulations. However, the ESF Operational Program for mainland Finland does currently not allow for this type of additional funding.

## 2.2 Scope

### 2.2.1 Objective

The objective of this study is to answer the two following questions:

1. Could JESSICA be successfully used to unlock/facilitate the implementation of regeneration and development schemes in the city-region of Jyväskylä?
2. How might JESSICA be best deployed in the city-region?

## 2.2.2 Limitations to our scope

Due to the limited time and resources available for this study, the following limitations are set:

- ▶ We have only identified and assessed projects in the city-region of Jyväskylä.
- ▶ The purpose of this study is not to assess the appropriateness of the current policy concerning regional and urban development in Finland, as manifested in the operational programs, only to examine whether JESSICA could be of benefit as an instrument to support the attainment of current policy objectives.
- ▶ We have not been in a position to verify the accuracy of information presented to us about the case study projects, including any estimates of project schedules, costs, revenues and other results such as employment effects.

## 2.3 Approach

Our approach to this study is to answer the two questions of the objective as follows:

The answer to the first question of the objective is presented in chapter 3. In chapter 3.1 we assess the interest in and benefits of JESSICA in Jyväskylä. This is done by assessing the interest in receiving funding in accordance to JESSICA, by analyzing potentially eligible projects and by comparing the existing funding mechanisms with the potential benefits brought by JESSICA.

In chapter 3.2, we assess whether JESSICA will be beneficial to the province of Western Finland. Here we examine how JESSICA can support the WFOP and identify complementary ESF actions.

In chapter 3.3, we examine the availability of Structural Funds and public and private match funding for a potential JESSICA fund in the city-region of Jyväskylä.

In chapters 3.4 and 3.5 we assess the feasibility of implementing JESSICA in Jyväskylä from a legal and administrative point of view.

Chapter 3.6 summarizes the benefits and drawbacks with JESSICA in the context of Jyväskylä and WFOP.

The conclusions of this study are presented in chapter 4. The main conclusion of this study is that an implementation of JESSICA in Jyväskylä or other parts of Western Finland does not appear feasible in the current program period, for reasons summarized in that chapter. However, this does not rule out the possibility of implementing JESSICA in the next program period, or even in the current period in other parts of the country, if sufficient ERDF funds can be

allocated in those settings. With these possibilities in mind, we outline the main aspects of the answer to the second question in Appendix 2, including key participants and their roles in a JESSICA implementation, project selection criteria, structure and legal forms of an UDF, and legal challenges to consider.

We have utilized the following sources for the study:

- ▶ Interviews and workshops with key people from the Ministry of Employment and the Economy, EIB, the city of Jyväskylä, Jykes Kiinteistöt, Regional Council of Central Finland and the Employment and Economic Development Centre
- ▶ Material available from potentially eligible projects, such as business plans, project plans, feasibility studies, financing plans, capital investments appraisals and interviews
- ▶ Urban development plans for the Jyväskylä region
- ▶ The program documents of the Western Finland Operating Program and the ESF Operational Program for mainland Finland
- ▶ Interviews with potential investors including real estate investment companies, real estate investment funds, and private and public pension insurance companies
- ▶ Legal experts in Ernst & Young Oy
- ▶ JESSICA regulation (EU Regulation 1083/2006, 1080/2006, 1081/2006 and 1828/2006)

## 3 The case for JESSICA

### 3.1 Benefits of JESSICA in the city-region of Jyväskylä

Driven by globalization and further accelerated by the ongoing recession, major structural changes are taking place in the Finnish economy. Many enterprises and jobs in traditional manufacturing sectors are disappearing. The Jyväskylä area has, for example, recently been affected by the closure of Nokia's unit in the city and significant redundancies at Metso. The future of the Kangas paper mill is also uncertain. New jobs are needed to replace the lost ones. It is commonly perceived that these to a great extent will have to come from new businesses in various new service industries.

Several factors are needed to support the creation of new service businesses: innovations, new business concepts, entrepreneurs, networks and skilled employees, among others. In addition to these, there is also a need for new types of facilities to optimally support new forms of service businesses. Urban regeneration is the key for creating and developing these new types of facilities. The execution of this regeneration is dependent on urban development companies.

#### 3.1.1 Urban development in Jyväskylä

Jyväskylä is the largest city in the region of Central Finland. The rural municipality of Jyväskylä was merged with the city of Jyväskylä in the beginning of 2009 to become the city-region of Jyväskylä. Together with its neighboring municipalities, the city-region of Jyväskylä owns a real estate development company named Jykes Kiinteistöt. Most important among the private real estate development companies in the city-region are Sponda and Technopolis.

Jykes Kiinteistöt has previous experience in establishing, managing and utilizing real estate funds. In 2005 Jykes Kiinteistöt started a pilot fund meant for private investors. Based on the experience from the pilot fund, a second larger fund was then established for institutional investors. A third fund was planned, but is now on hold. Due to the current economic recession the interest from real estate investors has declined.

As Jykes Kiinteistöt has experience in managing real estate funds they have expressed their interest to manage a potential JESSICA Urban Development Fund. There are also other real estate development companies that could possibly fulfill the same role.

Smaller cities in Finland such as Jyväskylä find it more difficult to attract private real estate developers than the Helsinki metropolitan area. In order to ensure an appropriate mix of different types of facilities in the region's urban development, the role of an active urban development company such as Jykes Kiinteistöt is important. Otherwise, real estate development often tends to focus only on housing developments. The development of Vitapolis (see

Appendix 1), for example, is likely to have resulted in residential properties had not Jykes Kiinteistöt been involved.

Financing of real estate development projects is needed in the early development stages. Real estate investors are generally interested in investing in existing real estate or real estate under construction, not in the actual development of the projects.

At present, projects at Jykes Kiinteistöt are self-financed during the planning stage while the construction phase is generally fully financed through loans, with municipality guarantors, from the public sector owned Municipality Finance as well as from commercial banks. Due to competition regulation, municipality guarantees may not be available in the future. And even if municipality guarantees would be available, the size of the potentially eligible projects may be too big for the municipality guarantee due to the weakened economy of the municipalities in Finland.

During the identification and planning stages Jykes Kiinteistöt usually finances the development directly with its own cash resources. The costs in this stage generally arise from the following:

- ▶ Acquiring the land needed
- ▶ Land planning and development, in cooperation with the city of Jyväskylä
- ▶ Architectural planning
- ▶ Technical construction planning

Before the construction phase can begin, over 70% to 80% of the real estate space need signed leases. Jykes Kiinteistöt's expected yield of the developed projects is currently between 8.5% and 9%.

The construction itself is financed through loans. The creditor of the loans is chosen through a competitive tendering process. The city of Jyväskylä and other municipalities, if applicable, are acting as guarantors. Projects are often financed with loans from Municipality Finance (Kuntarahoitus Oy). Municipality Finance is owned by the municipalities in Finland and has therefore received an AAA credit rating which allows cheap refinancing to municipalities.

When the property has reached a normal level (~95%) of the space being rented, Jykes Kiinteistöt aims to divest the property. This is done by selling all the stocks of the housing corporation (which also owns the land) usually to an institutional investor such as a pension fund. The return on investment for most projects is estimated at around 10%. At this stage the property is already fully developed and the real estate investor is not affected by the risks of development.

There are currently several projects in Jyväskylä that are in an early development phase. In the next chapter we identify the projects that are potentially eligible for a JESSICA funding.

### 3.1.2 Urban development projects suitable for JESSICA in Jyväskylä

One of the main eligibility criteria for JESSICA financing is that the project to be financed is part of an integrated plan for sustainable urban development. In Jyväskylä, integrated plans for sustainable urban development exist in the form of land use plans. These are made by Jyväskylä's City Planning Office. The land use plans lay out the development in the urban areas. They are integrated with other development plans and strive towards an environmentally sustainable development.

In discussions with the Council of Central Finland, the City of Jyväskylä, and Jykes Kiinteistöt we found that there were several projects that potentially could be suitable for JESSICA funding. In planning these projects a land use plan has to be approved by the city of Jyväskylä. All of the following projects either have an approved land use plan or are in the process of developing such a plan. In other words, all projects are part of an integrated plan for sustainable urban development.

Seven potential projects have been identified in this study. Together, these projects support the creation of more than 1,000 new sustainable jobs, ranging from tens to hundreds of employment opportunities per project. The total amount of needed investments before the end of 2015 amount to over EUR 140 million. The majority of the projects identified below are business parks concentrated on specific fields such as logistics or green technologies. The projects are briefly summarized in Table 1 below. More information about the projects is included in Appendix 1.

**Table 1** Potentially eligible JESSICA projects in the city-area of Jyväskylä

| Name and description  | Budget and financing 2009 - 2015   | New jobs by 2015 | Land use plan status (urban development plan)  |
|---|--|------------------|--|
| <b>Vitapolis</b> – a center for well-being services and serviced housing especially for senior citizens.                    | EUR 30 million. The development is financed by Jykes Kiinteistöt, the hospital district of Central Finland and the municipality of Muurame through loans with municipal guarantee. | 200              | Land use planning draft is ready and includes 47,500 m <sup>2</sup> for service premises and 40,500 m <sup>2</sup> for housing |
| <b>Voimala</b> – extension to the Kivääritehdas business park.  | EUR 21 million for the first building. Planning has been financed from Jykes Kiinteistöt's treasury and the construction will be financed through loans with municipal guarantee.  | 450-500          | Land use planning is currently being drafted for 5 buildings of around 11,500 m <sup>2</sup> each.                             |
| <b>Eteläportti</b> – expansion of Moventas' wind mill turbine factory.  | EUR 30 million. Planning has been financed from Jykes Kiinteistöt's treasury and the construction will be financed through loans with municipal guarantee.                         | 200              | Land use planning is currently being drafted for 2-3 buildings of around 16,000 m <sup>2</sup> each.                           |
| <b>Innoroad park</b> – international business park for road traffic and vehicle companies.                                  | EUR 30-40 million. Planning has been financed from Jykes Kiinteistöt's treasury and the construction will be financed through loans with municipal guarantee.                      | 100              | Land use planning is currently being drafted for a 50 hectare area.  |
| <b>Aviapark</b> – a business park for aviation and logistics companies.   | EUR 20 million. Planning has been financed from Jykes Kiinteistöt's treasury and the construction will be financed by through loans with municipal guarantee.                      | 100              | Land use plan draft is ready for 7,000 m <sup>2</sup> .  |
| <b>Event squares</b> at Lutakko harbor for trade fairs, public events and exhibitions.                                      | EUR 8.8 million. Financed from the city of Jyväskylä's budget. Project seeks EUR 1.4 million from the local TE-center.   | 20-50            | Land use plan draft is ready for three squares of 5,700, 13,000 and 3,700 m <sup>2</sup> .                                     |
| <b>Korkeakoskenlahti</b> – a business competence center developed by Technopolis together with the University of Jyväskylä. | Budget is still open. Technopolis is currently planning to finance the construction independently but is waiting to sign renting pre-agreements for most of the space.             | Not estimated    | Land use plan of 40,000 m <sup>2</sup> has been approved.  |

### 3.1.3 Benefits of JESSICA to urban development in Jyväskylä

Based on our understanding of the current state of urban development in Jyväskylä, it seems that a potential JESSICA implementation could help in unlocking private investments for the identified projects at an earlier stage and to a greater extent. Many of the projects presented in the previous chapter are in the planning phase where the risk is still high. It has been challenging to attract financing in this phase. There is a limit to how much funding risk Jykes Kiinteistöt can carry on its own. Therefore, external financing would be highly beneficial. Without external financing, the projects will proceed much slower and the possibility to develop several projects concurrently is limited.

Jykes Kiinteistöt considers JESSICA as an opportunity to attract more private investors to Jyväskylä. A JESSICA Urban Development Fund would receive EU ERDF grants that need not to be repaid as well as public match funding from the government. According to Jykes Kiinteistöt, a potential fund consisting of an initial investment including a portion of non-repayable money would act as an incentive for private investors. The risk for the other UDF investors is smaller since the ERDF grants invested in the fund can be used as a buffer in the fund.

## 3.2 Benefits of JESSICA for the Western Finland Operating Program

### 3.2.1 JESSICA's role in reaching the goals of the WFOP

A potential JESSICA fund in Jyväskylä would be capitalized with ERDF funds from the Western Finland Operating Program (WFOP). To be justifiable, an implementation of JESSICA in Jyväskylä would therefore have to fit with the priorities of the WFOP and contribute to the achievement of the objectives of the program.

Based on our understanding of the WFOP gained in discussions with the Council of Central Finland, it seems that the program is proceeding well in terms of identifying projects to support, and committing funds. There is currently no concern that the program would be unable to meet some of the "N+2" challenges and thus have to return funds to the Commission. While there is much talk about the 2015 timeframe challenges in other regions of Finland, this has not been an issue for Western Finland.

However, due to the economic downturn, it has become increasingly difficult to meet the main objectives of the program in terms of new employment opportunities and new enterprises. More than 8,000 new employment opportunities and some 2,000 new enterprises are still needed in Western Finland for the program to reach its goals. As Central Finland represents roughly a third of Western Finland in terms of program resources and expected results, this means that some 3,000 new employment opportunities need to be created in Central Finland. A major share of these would have to come from Jyväskylä.

Thus, all initiatives that contribute to generating employment opportunities and enterprises are in principle welcomed by the WFOP authorities.

There are two types of investments within the scope of JESSICA that can be said to contribute to the creation of enterprises and jobs, and thus support the achievement of the WFOP objectives:

- ▶ Creation of business facilities for new types of service businesses (and conversion of existing industrial facilities into such facilities) to support the structural change in the economy and the development of new service businesses.
- ▶ Investments that increase the attractiveness of the city area, thus helping to attract population to the city to achieve a thriving area and supply the human resources which are needed to drive the development of new business.

All identified projects represent either of the two types, and the projects are estimated to directly support the creation of more than 1000 sustainable employment opportunities in total. In this sense, the identified projects can be said to support the WFOP.

However, due to the regional policy defined on both EU and national levels, the type of investments that JESSICA directly represents are of rather low



priority in the WFOP. For one thing, there is more emphasis on supporting rural areas and less emphasis on supporting the relatively prosperous city areas. This is for example demonstrated in the national public business financing where Jyväskylä has been defined as a “white zone” in which the development of business premises should not be supported with public funds. Moreover, the Commission has advised the program authorities in Western Finland to reduce the financing of infrastructure projects with Structural Funds. Consequently, projects representing “urban development” have a rather low priority in the WFOP.

The Council of Central Finland has also expressed concerns with regard to the leverage effect, of using grants to attract and combine with private capital, and the size of the investments from a potential UDF. The investments, and by consequence the UDF, should be large enough to concentrate on a few key investments. A too scattered investment scheme would not be beneficial to the projects, neither to the WFOP. If an investment is too small the leverage effect will be lost.

### **3.2.2 Complementary ESF actions in a JESSICA scheme**

Based on discussions with the Ministry of Employment and the Economy, it seems that the national ESF Operational Program for mainland Finland has had some challenges in finding sufficient eligible activities to finance to get the yearly allocated amounts utilized within the required 2-year time frame. A potential additional benefit with JESSICA therefore arises if JESSICA could bring such projects forward that would include complementary activities, which could be financed with ESF resources.

ESF grants can be given to training for new types of employment. This fits well with some of the potential projects identified for a JESSICA funding. For example, Vitapolis will need well-being service personnel and Aviapark airplane service personnel.

The Employment and Economic Development Centre (TE-keskus) of Central Finland is the local authority in charge of allocating ESF grants. According to them, all grants have been allocated for 2009, but for 2010 the budget is EUR 10 million in Central Finland. The application process is done yearly. Projects apply for funding directly from the Employment and Economic Development Centre which approves the grants.

Complementary actions financed by ESF resources are not directly dependent on whether the projects receive funding from a JESSICA UDF or not. If the projects move forward, they may apply for ESF grants.

### 3.3 Availability of funding for JESSICA

#### 3.3.1 Structural Funds and other public funding

The Commission, the Ministry of Economy and the Employment, as well as the program authorities of the WFOP are all positive to the idea of deploying structural funds through financial engineering instruments, i.e. allocating the structural funds as repayable investments through revolving funds as an alternative to giving them away as one-time grants.

However, according to the Council of Central Finland, the WFOP could allocate at most EUR 2-3 million to a JESSICA fund in Jyväskylä, including both ERDF and national match funding.

According to the regional councils in Vaasa and Tampere, potential allocations in these cities are even smaller. As in Jyväskylä, potential JESSICA funding would most likely fall within the WFOP's third priority axis. The third priority axis does not include any allocations in Vaasa and Tampere for the kind of urban development that JESSICA would support. There is the fourth priority axis in the WFOP, which is focused on development of major urban areas, applicable only to Vaasa and Tampere. However, this priority axis' total ERDF budget is under EUR 7 million and it is not directly meant for the kind of projects that a JESSICA UDF would invest in. Major changes in allocations are only possible via amendments to the WFOP. Operational Programs are not easily amended and the process can be long because the Commission needs to approve all amendments.

The Commission has recently brought forward a new option to use ESF funds as a complement to ERDF funds in a JESSICA implementation. This option has not been evaluated in previous JESSICA feasibility studies in other countries. In Finland ESF additional funding to ERDF projects is currently not allowed in the national ESF Operational Program. However, discussions with the Commission are presently being held on the question whether ESF funds could be allocated to a JESSICA fund. The current estimate is that some EUR 10 million of ESF funds could potentially be allocated to financial engineering instruments in Western Finland, at most. This would correspond to a share of EUR 3 million for Central Finland.

The city of Jyväskylä has decided that they cannot contribute any funds to a potential JESSICA fund. The reason for this is that the city already has a significant amount of property on its balance sheet and that it wants to reduce, not increase, its property investments. Jyväskylä could also consider participating in a JESSICA fund with land lot properties. However, the proportion of the land lot value is usually only a few percent of the whole project's investments.

To our understanding, EIB will not make any equity contributions to JESSICA funds. They will potentially lend against existing guarantees. EIB funding is thus an option but an implementation of JESSICA will not bring in any new EIB funds that would not otherwise also be possible to obtain.

With the investment need in the projects amounting to several tens of millions, a JESSICA fund with some EUR 2-6 million in structural fund contribution appears too small to be feasible.

To create a larger fund spanning a wider set of regions is not really realistic due to the way the structural funds programs are organized. The administration of ERDF funds for Finland has been divided into four operational programs (Western Finland, Northern Finland, Eastern Finland, Southern Finland), which are strictly separate, and a pooling of funds between the programs is not allowed. Also within one operational program, e.g. the WFOP, there is unlikely to be a political will to pool the funds among regions, unless each region gets back (at least) its own share from the pool.

### 3.3.2 Private funding

To assess the interest among private investors to participate with capital in a potential JESSICA UDF, a number of institutional investors active in the real estate market were interviewed.

Institutional investors and real estate investment companies do invest in real estate projects in Jyväskylä, and could potentially increase their investments. For example, one pension insurance company interviewed showed a preliminary interest in participating in a JESSICA UDF with a 25% share, if the fund would be of the size of EUR 10-20 million. In that case this company would expect to get influence over the fund's management.

Large real estate investors seem to prefer to concentrate their direct investments. Another pension institution interviewed expressed that they would rather invest directly into fewer projects but with larger amounts. A small UDF which invests in several projects is therefore less interesting than the possibility to invest directly into one of the projects.

In the Finnish real estate market, funds do not invest in other real estate funds because the market is relatively small and the double management fees would lower the profits.

Most investors focus mainly on investing in properties that are already constructed and leased to around 95%, or in properties which are at least developed to a stage with signed lease contracts for 80% of the rentable area. The risk of the initial development is left to urban developers, primarily public ones such as Jykes Kiinteistöt. Private urban developers currently often find smaller cities in Finland too risky for new projects.

Yield requirements are higher in 2009 than in recent years because of the lack of available financing. This affects the risk of real estate development even further.

It seems that private funding to a UDF is possible but not evident. Institutional investors are mostly interested in investing in real estate that has already been developed. The risk of investing in urban development in Jyväskylä is currently deemed too high.

### 3.3.3 Debt financing

In addition to the examination of possible equity contributions to a JESSICA fund, it can also be considered whether the implementation of a JESSICA scheme could help in mobilizing private or public loan financing for urban development.

Loan financing is an essential instrument for financing urban development projects. Loans from various financial institutions is currently the main form of external financing that Jykes Real Estates is utilizing to fund its projects, in addition to its own cash resources.

Loan financing from commercial banks, as well as from public financial institutions such as the EIB, generally requires collateral, which can be provided in the form of assets or in the form of guarantees from an entity with sufficient standing. Guarantees from Municipality Financing are commonly used for development projects in Jyväskylä and other municipalities.

The amount of available collateral currently limits the amount of loan financing that can be obtained for the identified projects in Jyväskylä. To obtain additional loan financing in the context of a JESSICA scheme, new sources of collateral would have to be obtained.

The JESSICA scheme as such does not bring any new assets or institutional guarantees that could be utilized as collateral. The UDF could use its funds to issue guarantees to projects, but to be considered a credible guarantor for loans of the size that are required, the UDF would need significantly larger funds than the EUR 2-6 million, which now appear to be available. Any guarantees issued by the UDF would also correspondingly limit the fund's ability to make other forms of investments.

Thus it does not seem like an implementation of JESSICA could help mobilize any loan financing in addition to what is already available today.

### 3.4 Feasibility from a legal point of view

When assessing the feasibility from a legal point of implementing JESSICA in Finland, consideration needs to be given to the legal form of UDF as well as the legal rules relating to the granting of the support itself, such as the Acts on Structural Funds, State Aid and Public Procurement (or Contracts).

Based on our understanding of JESSICA it appears that these acts do not contain any rules that would prohibit an implementation of JESSICA in Finland. However, these acts do contain some limitations as regards the type of projects that may be supported by JESSICA as well some procedural provisions to be abided to cope with the restrictions on state aid. The relevant legal aspects of a potential JESSICA implementation are covered further in Appendix 2, under "Legal challenges in a JESSICA implementation in Finland".

### 3.5 Feasibility from an administrative point of view

The administrative work that a potential Urban Development Fund would require depends on the size of the fund, the number of projects the UDF invests in and the reporting requirements from the UDF's investors.

The management fee percentage of real estate funds is inversely proportional to the size of the fund. Jykes Kiinteistöt have estimated that for a EUR 100 million fund the annual management fees may be around 1% to 2% of the total fund capital, whereas for a EUR 10 million fund the fees may be as high as 5%. According to the EU Structural Funds implementation regulation (1828/2006, §43) the UDF management costs may not exceed 3%. If the size of a UDF in Jyväskylä is only around EUR 2-3 million it is likely that the management fees will exceed the maximum fee allowed under JESSICA regulations.

The more projects that the UDF invests in, the more administrative work is required. A potential UDF in Jyväskylä would probably have to invest in several projects for the reason that the project selection should be objective and equal for all projects. The investors of an UDF set the reporting requirements. Possible private UDF investors include institutional investors and listed companies. These usually require extensive reporting. Additionally the reporting to the Managing Authority needs to comply with JESSICA regulations. This implies e.g. double accounting if the project has any non-eligible expenses.

It seems that the costs for an UDF in Jyväskylä are likely to exceed the regulated maximum limit and that the administrative work is demanding due to the number of investment objects and the requirements of UDF investors. These three issues suggest that it would not be feasible to implement JESSICA in Jyväskylä from an administrative point of view.

### 3.6 Main benefits and drawbacks of JESSICA

In chapter 2.1 we listed the key potential benefits of JESSICA. Based on our findings, a number of those benefits seem to be applicable in the context of Jyväskylä and the Western Finland Operating Program. However, the limited ERDF capital available and the small size of the potential UDF imply that these benefits could only be delivered to a limited extent. These benefits are:

- ▶ Sustainability by retaining and recycling funds after the end of the operational program
- ▶ Greater accountability and stronger incentives towards better performance by converting grants to repayable investments
- ▶ Achieving a lower return requirement than with private capital alone, thus enabling investment in locations that would otherwise fail
- ▶ Leverage effect of using grants to attract and combine with private capital
- ▶ New sources of expertise and know-how from private actors through public-private partnerships (PPPs)
- ▶ Development and modernization of financial markets by utilizing EU Structural Funds grants in a new and innovative way

The following potential benefits are not relevant in the context of the Western Finland Operational Program as the program has not had any challenges to allocate its funds:

- ▶ Ability to immediately draw down Structural Funds allocated for the whole program period, and thus accelerate activities while also helping to deal with the challenge that the funds allocated for a particular year have to be spent within two years of the allocation year (the so called “N+2” challenge)
- ▶ Ability to unlock structural funds that could otherwise not be utilized

The main drawbacks of a potential JESSICA implementation in Jyväskylä stem from the limited amount of ERDF resources available:

- ▶ The UDF would probably be too small to have any significant impact on the identified projects
- ▶ The administrative overhead and costs of running a JESSICA UDF would be high in relation to the limited benefits that could be gained from the small share of ERDF capital in the fund

## 4 Conclusions

It would be beneficial for the city-region as well as for the WFOP as a whole if new forms of funding could be mobilized to accelerate the development of premises and other types of infrastructure in the city-region to support the creation of new businesses. However, the structural funds available for JESSICA appear to be too small to achieve a fund of sufficient size to have any real impact on the development in Jyväskylä. We are therefore not in a position to recommend an implementation of the JESSICA instrument in Jyväskylä in the current Structural Funds program period.

For similar reasons, we are also unable to recommend an implementation of JESSICA in the other city-regions in Western Finland. The amounts of structural funds that could potentially be allocated to JESSICA in these regions are even smaller than those available in Jyväskylä.

However, it could still be explored whether JESSICA could be utilized within the Eastern Finland Operational Program. This program has a larger amount of ERDF funds allocated to it than the Western Finland Operational Program. The type of projects that JESSICA could fund also seems to fit somewhat better in the Eastern Finland Operational Program than in the Western Finland program. Direct infrastructure investments are, for example, possible in the Eastern Finland program. Both priority axes 2 and 3 in the Eastern Finland Operational Program contain development objectives that represent the type of development that JESSICA could support.

We also recommend that the Ministry of Employment and the Economy consider whether JESSICA could be utilized in the next program period. In the next program period, the structural fund allocation to Finland will most likely be smaller than in the current period. Then it will be even more crucial to utilize the funds as effectively as possible, and the use of new instruments to increase the effect and sustainability of the funds will be even more topical. Whether JESSICA will be appropriate to implement in the next program period will depend on a number of factors, most notably the development priorities and the importance of “sustainable urban development” in relation to other development needs. That is beyond the scope of this study to assess.

If the JESSICA instrument is to be utilized in the next program period, then it needs to be considered how UDFs of sufficient size and with a sufficient portion of ERDF capital can be achieved. The mechanisms for allocating the structural funds among the regions in Finland will probably need to be somewhat different than in the current program period. Some new mechanism is probably necessary to enable a pooling of funds among regions and the creation of UDFs on a “NUTS II region level”<sup>3</sup>, or even on a country level. With such a mechanism, it would be easier than currently to achieve sufficient ERDF funds for a JESSICA fund.

Even if the JESSICA initiative may not be possible to implement in Finland, the question still remains to be resolved how the development of business

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<sup>3</sup> “NUTS II” is an EU standard for defining regions; the NUTS II regions in Finland are Western Finland, Northern Finland, Eastern Finland and Southern Finland

premises and other required facilities should be financed in the future, particularly in cities outside the Helsinki Metropolitan Area. We recommend looking into the various possibilities to form public-private partnerships to optimally combine resources and align incentives around developments that the public and private sectors have a joint interest to advance.



## Appendix 1: Potentially eligible projects

### Vitapolis

Vitapolis is a former hospital area which will be transformed into a center for well-being services and serviced housing especially for senior citizens. The site was bought in 2008 by a real estate company owned by Jykes Kiinteistöt (40%), the hospital district of Central Finland (40%) and the municipality of Muurame (20%).

The project includes renovation of the existing buildings and construction of new buildings. At present the draft of the land use planning is being amended. The planned building rights are 47,500 m<sup>2</sup> for service premises and 40,500 m<sup>2</sup> for housing. The land use plan will be approved in 2010 after which the municipal engineering work will begin. The first new building at the site is currently being planned and the planning for the new Vitapolis center has started as well.

Investments by 2015 are likely to amount to around EUR 30 million. This will include the renovation of the existing main building, the construction of the Vitapolis center building and the municipal engineering costs for the area. The estimated rent and yield requirements for these phases are around 8.5% to 9%. It is estimated that Vitapolis will create 200 new jobs by 2015.

The Vitapolis project include residential buildings as well. Housing is one area which is not supported by EU funding in Finland. This means that the share of ERDF and public match funding in the UDF would have to be excluded from the funding of the housing buildings.

### Voimala

Voimala is the expansion project of an existing business park at a former rifle factory. This extension will provide 30,000 m<sup>2</sup> gross floor area of new office and business premises for growing and developing business service companies.

The plan is to realize the project in five phases, of which the first covers the construction of a building of around 11,500 m<sup>2</sup> gross floor area. This phase will be completed before 2012 and cost around EUR 21 million. The land lot has been acquired by Jykes Kiinteistöt and the architectural planning for the buildings will be ready during the autumn of 2009. At present the land use planning and site zoning are under work. The building rights are likely to be approved by 2010.

The project has so far been financed from Jykes Kiinteistöt's own cash resources. The construction may start when 70% to 80% of the premises have signed leases. The constructions will be financed through loans with municipality guarantees.

The rent revenue per square meter is estimated at EUR 18-20. Jykes Kiinteistöt's yield requirement is around 8.5% to 9%. A divestment is planned when the available space has reached a normal level of vacancy (~5%). It is expected that one Voimala building will provide premises for 450-500 new jobs.

### **Eteläportti**

Eteläportti is a business park for the green technology industry. At present the wind mill turbine manufacturer Moventas has a plant of 16,000 m<sup>2</sup> at the site. The land lot has building rights for two to three additional constructions of comparable size. In the long term an expansion of an additional 100,000 m<sup>2</sup> in Muurame is possible.

The land use planning for the next phase is currently under work. This includes a second plant for Moventas and a supportive logistic center. The total investments for these buildings are estimated at EUR 30 million.

The construction is likely to be financed by Municipality Finance with the city of Jyväskylä acting as guarantor. Jykes Kiinteistöt is developing the project and estimates a yield of 8.5% to 9%. When finished, this second phase is estimated to provide 200 new jobs.

Due to the current economic recession Moventas is waiting for the demand of their products to pick up before starting the construction of the second plant.

### **Innoroad Park**

Innoroad Park is an international business park for companies specialized in road traffic and vehicle industries. The whole project is estimated to cost around EUR 200 million and to be ready by 2025.

By 2015 the area should extend by around 50 hectares with buildings of 20,000 m<sup>2</sup> gross floor area. This translates to investments of roughly EUR 30-40 million. The land planning use of the area is currently under work. Jykes is financing the development with its own cash resources. Jykes Kiinteistöt's yield requirement is around 8.5% to 9%.

It is estimated that Innoroad Park will employ 100 more people by 2015.

### **Aviapark**

Aviapark is a business park for aviation and logistics companies next to the Jyväskylä airport. At present Lidl has a large logistic center in the area and the Finnish Air Force has around 7,000 m<sup>2</sup> of office and airplane overhaul space.

The land lot is owned by Jykes Kiinteistöt, the city of Jyväskylä and a private land owner.

There are currently plans to build an airplane overhaul hall for Patria Aviation. The investments needed are estimated at EUR 20 million. At present Jykes Kiinteistöt is financing the development with its own cash resources. The master land use plan for the area is ready and amendments are being done to the town land use plan.

Jykes Kiinteistöt is developing the project and estimates a yield of 8.5% to 9%. Aviapark will be expected to provide 100 new jobs by 2015.

### **Event squares at Lutakko harbor**

The city of Jyväskylä has been developing the Lutakko harbor area during several years. In connection to this area three larger event squares are planned. The development is estimated to be ready by 2012.

The main event square is the harbor square which will be 5,700 m<sup>2</sup> and include the needed infrastructure for organizing large events, exhibitions, and markets. Next to the harbor square comes the 13,000 m<sup>2</sup> Lutakko square which can be used for large public events as well. The third square is the 3,700 m<sup>2</sup> bridge square where restaurants and cafeterias are planned.

It is anticipated that the event squares will create around 20-50 new jobs in restaurant, tourism and maintenance related fields.

The total investments for the development of the harbor area are estimated at EUR 8.8 million. In 2009 the investments will be around EUR 4 million and in 2010 they are estimated at EUR 2 million. The city of Jyväskylä is presently negotiating with the Employment and Economic Development Centre (TE-keskus) in order to receive EUR 1.4 million financing for 2010-2011. The remainder is financed directly from the city's budget.

### **Korkeakoskenlahti**

A plan for a Business Competence Center has been developed by Technopolis in cooperation with the University of Jyväskylä and the city of Jyväskylä. The land use plan for the area has been approved and includes building rights for 40,000 m<sup>2</sup> gross floor area. The architectural planning for the buildings is ready and the tendering process for the construction has begun.

The first phase of the project is one building of 14,500 m<sup>2</sup> gross floor area. Technopolis has pre-agreements with the University of Jyväskylä and with YTHS, the Finnish student health service. However, Technopolis needs more leaseholders before the constructions can start. In the current economic situation Technopolis requires well over 70% to 80% of the available space to

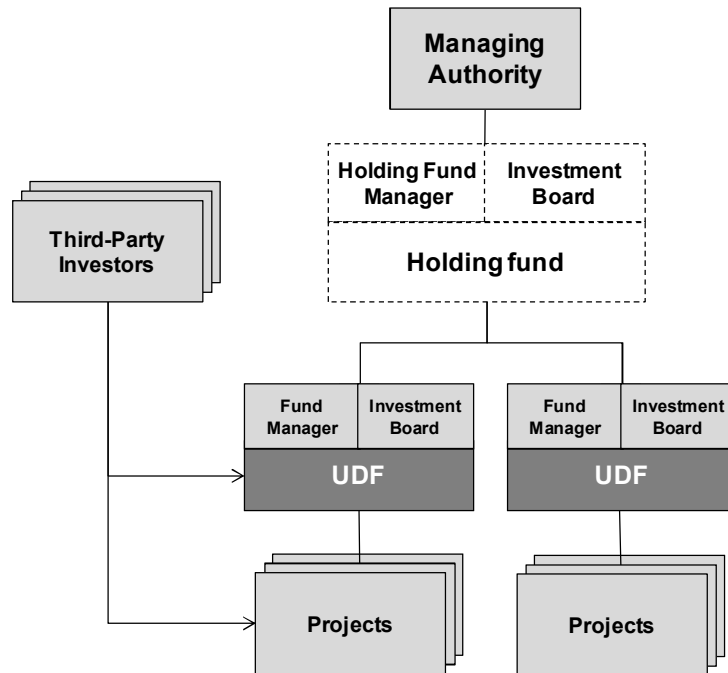
be rented before construction. The yield requirements are between 6% and 9%. Recently yield requirements have been closer to 9%.

After the construction phase has begun, it is expected to go on for 13-18 months. Technopolis is planning to finance the construction without external financing. However, due to current challenges Technopolis is also open for other possibilities.

## Appendix 2: Aspects of a JESSICA implementation in Finland

### Participants and structure

The key participants in a JESSICA implementation include the Managing Authority, a potential Holding Fund, one or several Urban Development Funds (UDF) and potential third-party investors. The structure of the JESSICA implementation is illustrated in Figure 1. The role of each party is briefly presented in the following sections.



**Figure 1** Participants and structure of a JESSICA implementation

### Managing Authority

The role of the Managing Authority is defined by the structural fund regulations, which require it to be responsible for managing and implementing the Operational Program in accordance with the principle of sound financial management. This is consistent with the responsibilities required for all Structural Fund activity.

### Holding Fund

A Holding Fund is an optional step within a JESSICA structure. A Holding Fund acts as an intermediary, managing the investment portfolio on behalf of the Managing Authority and appraising which Urban Development Funds (UDFs), and therefore which projects, are eligible for financing, based on the pre-approved criteria. The regulations state that the Holding Fund must be structured within a financial institution. On inception, the Holding Fund will

enter into a Funding Agreement with the Managing Authority and launch a call to potential UDFs who will prepare business plans for the Holding Fund Manager to evaluate.

The creation of a Holding Fund provides some potential benefits including the ability to draw down the ERDF contribution immediately as match funding is provided with the interest earned on this money used for project development or fund management fees. The addition of a dedicated Holding Fund Manager provides the Holding Fund with expert resource and the ability to strategically manage investment at a portfolio level. The structural funds regulations allow for the appointment of the EIB as Holding Fund Manager on a not-for-profit basis without a public procurement process.

Whether or not a Holding Fund would be beneficial to implement depends to a great extent on the scope of the JESSICA implementation and the way that ERDF funds are allocated. If the JESSICA implementation involves a pooling of ERDF funds between regions, then the Holding Fund would play an important role in coordinating the allocation of the common ERDF funds to the individual local UDFs. However, the current operational programs do not allow for such pooling to take place, which means that each UDF could only receive ERDF funds that have already been allocated to the region that the UDF represents. Thus there would be no need for a Holding Fund to coordinate the allocation of ERDF funds. However, the situation could be different in the next program period if the next operational programs are structured differently.

If a Holding Fund is established, it is recommended that an Investment Board is set up to approve or reject the recommendations of the Fund Manager relating to investment matters. The setup of the Investment Board for the Holding Fund is likely to be appointed by the Ministry of Employment and the Economy and should comprise experts in regeneration, economic development, finance, banking and policy. Its role will be similar to that of a credit committee in a commercial bank.

## **Urban Development Funds**

An Urban Development Fund (UDF) is an entity that invests in eligible projects within an integrated plan for sustainable urban development by means of equity, loans or guarantees. UDFs may also support urban projects receiving grant assistance from an operational program but are not able to re-finance acquisitions or participate in completed projects. UDFs can be national, regional or urban funds, tailored to specific sectors or to specific projects. They may act as financing institutions providing simply funding or, at the same time act as development companies.

In Jyväskylä, Jykes Kiinteistöt provides an existing delivery vehicle that could act as an UDF. There are also other real estate investors which could possibly fulfill the same role.

In order to ensure that the UDFs will use the resources from the structural funds in line with the urban policy objectives of the Managing Authority, the

Managing Authority can set requirements within the Funding Agreement signed with the Holding Fund and will also enter into a separate Funding Agreement with the UDF.

In a similar manner as with the potential Holding Fund, each UDF should also have an Investment Board to ensure that all the relevant stakeholders have appropriate influence over the investment decisions taken by the fund. This would include representatives of the operational program that contributes ERDF funds to the UDF as well as third-party investors, who most likely also want to have an influence over the investments undertaken by the fund.

### **Third-party investors**

A key objective with JESSICA is to facilitate a combination of public and private resources in urban development. The aim is thus to get third-party investors to participate in the investments undertaken by the JESSICA funds.

Potential third-party investors include

- ▶ Real estate investment companies
- ▶ Real estate investment funds
- ▶ Private and public pension insurance companies
- ▶ Various financial institutions

Third party investors can participate either on UDF level or on project level. Due to the strict and specific investment criteria of institutional investors, it is most likely to get third-party investors to participate with funding on project level, which allows them to thoroughly appraise the risk and return prospect of the project to be invested in before committing funds.

Moreover, if the investor is already diversified, then there is no added value of the UDF, only an additional layer of management costs.

### **Project selection criteria**

The eligibility criteria at a European level were listed in chapter 2.1.2. On a national level, more specific criteria should be defined to support the selection of projects to be funded.

Since JESSICA is a means of allocating ERDF funds, the criteria should reflect the objectives of the ERDF operational program. The projects to be funded should thus be ones that contribute to the achievement of the objectives of the operational program. In the Western Finland Operational Program, the key objectives are expressed in terms of new employment opportunities generated and new enterprises created.

The project selection criteria should also reflect the particular development needs and objectives of the city area(s) covered by the UDF. In the case of Jyväskylä, the key priorities related to real estate development are:

- ▶ To create business facilities for new types of service businesses to support the generation of new employment opportunities to replace the jobs being lost in traditional industries
- ▶ To increase the attractiveness of the city area, thus helping to attract population to the city to achieve a thriving area and supply the human resources that are needed to drive the development of new businesses

The above priorities apply to the current WFOP and in Jyväskylä. The actual criteria to be applied in a JESSICA implementation would have to be derived in a corresponding manner from the particular operational program(s) and city area(s) that the implementation would cover.

## Possible legal forms of an UDF

To be able to act as intended it is advisable to structure the UDF as a legal entity. The available legal forms are a limited company, a limited partnership and a partnership. The limited partnership appears to be the most advantageous legal form of the UDF. The limited partnership brings some tax advantages and it also provides convenient methods to allocate risks and profits differently to each partner. In Finland the limited partnership has been the most common form used for real estate funds comparable to JESSICA.

The general partner of the limited partnership would be a limited company, which in turn would be owned by the parties setting up the fund, either one or several municipalities or another actor such as a private real estate fund. The purpose of the limited company is to shield the owners from the unlimited risk that the general partner of the limited partnership carries. Third-party investors would participate in the limited partnership as limited partners, which do not carry any risk in excess of the capital that they have supplied into the partnership.

The limited partnership is not a taxpayer in itself. The income of the partnership is only taxed in the taxation of the partners. This provides an advantage for tax-exempt investors such as pension funds, which can earn tax-free returns on their investments in the fund if it is set up as a limited partnership.

One of the benefits sought with JESSICA is to enable investments into projects that do not fully meet the return requirements of private investors. This is to be achieved by combining private capital with structural funds and other forms of public capital that has lower return requirements than the private capital. The private investors would be given preference to the returns of the fund up to a level that corresponds to their return requirement. The structural funds capital would provide a buffer against the risk that the overall return of the fund is lower than the return provided to the private investors. This model can be



achieved with the limited partnership, which allows for profits to be distributed differently to different partners. The distribution of profits and risks among the partners can be flexibly defined in a partnership agreement.

## Legal challenges in a JESSICA implementation in Finland

If JESSICA were to be implemented in Finland, some consideration would have to be given to the stipulations of legal rules in the Act on Structural Funds, the Act on State Aid and the Act on Public Procurement (or Contracts). These acts contain some limitations as regards the type of projects that may be supported by JESSICA as well some procedural provisions to be abided.

### State Aid and Structural Funds

According to the Vademecum on Community law on State Aid (European Commission Directorate-General for Competition, 30 September 2008) the operational programs under the structural funds for 2007-2013 contain a standard form clause providing that *"any public support under this program must comply with the procedural and material State Aid rules applicable at the point of time when the public support is granted"*. It is the responsibility of the managing authorities to ensure that this condition is fulfilled. Therefore the Finnish rules on state aid must be taken into consideration when evaluating the appropriateness of JESSICA.

The main Finnish act governing state aid is the Act on Discretionary Government Transfers (688/2001). The Act stipulates, inter alia, the general conditions for granting discretionary government transfers. The respective provisions stipulate that that discretionary government transfers may be granted from a budgetary or extra-budgetary state fund, if granting a transfer is judged to cause only minor distortion to competition and the market in a state belonging to the European Economic Area (Chapter 2, Section 7). The Finnish practice on the state aid issues follows the general European principles.

For example, the main principles relating to the notification are:

- ▶ De minimis rule; where the maximum amount of the aid is less than EUR 200,000 during the present and two following years, no notification must be made to the Commission;
- ▶ Block exemption and certain SGEI services; within 20 days from the execution of the plan, the outlines of the plan must be submitted to the Commission;
- ▶ Pre-notification to the Commission is necessary if any of the above mentioned rule cannot be applied

It should also be noted that the Act on Structural Funds (1401/2006) stipulates that the Finnish authorities shall draft the national scheme in cooperation with

the European Commission. This national scheme serves as a guideline for action plans that are designed for different purposes. The Finnish authorities that have prepared action plans are obligated to submit the action plans for approval by the Commission.

The aid is generally permitted without further analysis when it is provided to activities that are undisputedly outside the interests of the private parties, whereas in the cases when aid is considered for activities close to the interests of private parties, the relevant matters relating to state aid are duly scrutinized. The projects identified in this study in chapter 3.1.2 all involve potential interest of private parties.

### **Public procurement**

The rules of the Act on Public Contracts (348/2007) i.e. public procurement must be applied for example when a purchaser has received more than half of the value of the contract in aid for the award of the contract from a public authority. Therefore the obligation to comply with the rules of the Act on Public Contracts could often be triggered in cases, where an UDF is involved in financing a project.

It is important to note that e.g. the Ministry of Employment and the Economy has taken the view that as a main rule, there is no gratuitous benefit, and therefore there is no state aid when the procurement is carried out in accordance with the rules of the Act on Public Contracts.