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Subject: State Aid N 421/2006 – Portugal – Zona Franca da Madeira

Dear Sir,

1. PROCEDURE

- (1) By electronic notification dated 28 June 2006, registered at the Commission on the same day with the reference A/34659, the Portuguese authorities notified, pursuant to Article 88(3) EC, the above mentioned measure “*Zona Franca da Madeira*”.
- (2) By letter of 29 August 2006, in accordance with point 106 of the Guidelines on national regional aid for 2007-2013¹ (hereinafter “RAG”), the Commission signalled to the Portuguese authorities that since they must be coherent with the regional aid map, notifications of regional aid schemes or ad hoc aid to be granted after 31 December 2006, cannot normally be considered complete until the regional aid map has been adopted for the Member State concerned.

¹ OJ C 54, 4.3.2006, p. 13.

Sua Excelência
Luís Filipe MARQUES AMADO
Ministro dos Negócios Estrangeiros
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- (3) The Commission by letter of 16 November 2006 requested additional information on the above mentioned measure. The Portuguese authorities submitted additional information on 19 December 2006.
- (4) A meeting between representatives of the Portuguese authorities and the Commission was held on 10 January 2007, where the former presented additional information for the evaluation of the measure.
- (5) The Portuguese regional aid map 2007-2013 was adopted on 7 February 2007.²
- (6) The Commission by letter of 30 January 2007 requested additional information to which the Portuguese authorities replied on 13 February 2007.
- (7) A second meeting with the Portuguese authorities took place on 9 March 2007.
- (8) The Commission requested additional information by letter 28 March 2007 to which the Portuguese authorities replied by letter of 11 May 2007.

2. DESCRIPTION OF THE MEASURE

2.1. Objective

- (9) The measure aims to promote regional development and the diversification of the economic structure of Madeira, thereby enabling the companies established in an area qualified as an outermost region to overcome their natural structural handicaps.

2.2. Legal basis

- (10) The measure seeks to renew the application of the “*Zona Franca da Madeira*”³ (hereafter “ZFM”) which expired on 31 December 2006. The ZFM was established before the accession of Portugal to the European Union. The Commission has three times authorised the extension of the aid scheme on the ZFM by three, six and four years respectively (State aid E 13/91, E 19/94 and N 222/A/2002 and N 222/B/2002).^{4, 5}
- (11) The legal basis of the scheme is the “*Projecto de Decreto-Lei*” that modifies the “*Decreto Lei nº 163/2003, de 24 de Julho – Alteracao do artigo 34 do statuto dos Benefícios Fiscais*”, “*Decreto Lei nº 215/1989, de 1 de Julho- Estatuto dos*

² Commission Decision of 7 February 2007 on State aid N 727/2006 – Portugal – Regional aid map 2007-2013.

³ State aid nº N 222/A/2002 – *Regimen d’aides de la Zona franche de Madère pour la période 2003-2006*”.

⁴ The measure was suspended by the Portuguese authorities in 2001 and 2002.

⁵ In the last approval of the ZFM, the part concerning the shipping register was covered by a separate Commission decision of 4 February 2003 on State aid N 222/B/2002 – Portugal– *Regime de auxílios da Zona Franca da Madeira para o período 2003-2006*. However, this decision covers the conditions for the granting of aid to the international shipping register.

Benefícios Fiscais” and “Decreto Lei nº 500/80 de 20 de Outubro –Criação na Região autónoma da Madeira de uma zona franca”.

2.3. Administration of the scheme/Authority granting the aid

- (12) The authority granting the aid is the “*Ministério das Finanças e da Administração Pública*”. The scheme will be administered by the “*Sociedade de Desenvolvimento da Madeira, S.A.*” (hereinafter “SDM”).

2.4. The measure

- (13) The ZFM concerns a preferential tax regime which comprises an industrial free zone, an international services centre and an international shipping register (MAR).

2.5. Form and amount of aid

- (14) The measure under scrutiny concerns fiscal incentives in the form of a reduced corporate taxation applicable to companies licensed under the ZFM. It allows aid beneficiaries to apply a reduced rate of taxation to the profits resulting from activities effectively and materially performed in Madeira up to a ceiling placed upon their annual taxable base.
- (15) In comparison with the previous existing schemes State aid N 222/A/2002 and N 222/B/2002 which expired at 31.12.2006, the measure covered by this decision foresees an increase in the applicable tax rates. The changes are summarised in Table I.

Table I: Tax rates applicable to beneficiaries of the scheme⁶

Years	Previous existing schemes N 222/A/2002 N 222/B/2002	Years	New scheme N 421/2006
2003-2004	1%	2007-2009	3%
2005-2006	2%	2010-2012	4%
2007-2011	3%	2013-2020	5%

- (16) In addition, companies that carry out industrial activities can benefit from a further 50% tax cut as long as they fulfil at least two of the following conditions⁷:
- (a) modernisation of the regional economic fabric through technological innovations relating to products, manufacturing or business methods,

⁶ For comparison purposes, the nominal rate of corporate taxation in Madeira is 22.5%.

⁷ The further 50% tax cut is provided to registered companies having started their activities and only for those exercises in which the fulfilment of the mentioned conditions is verified.

- (b) diversification of the regional economy, particularly through the introduction of new activities with a high added value,
 - (c) employment of highly qualified human resources,
 - (d) improvement of environmental conditions,
 - (e) creation of at least 15 new jobs with a minimum maintenance period of five years.
- (17) Moreover, as in the previous Commission decisions on State aid N 222/A/2002 and N 222/B/2002, the companies authorised to operate in the ZFM will also enjoy exemption from municipal and local taxes, as well as exemption from transfer tax payable on immovable property for the setting up of a business in the ZFM.⁸
- (18) The tax benefits for which such companies will be eligible, however, will be limited by a corresponding maximum taxable amount. The ceiling placed upon the annual taxable base subject to the reduced tax rate depends on the number of jobs created by the beneficiary according to the following scale: EUR 2 million for 1 to 2 jobs, EUR 2.6 million for 3 to 5 jobs, EUR 16 million for 6 to 30 jobs, EUR 26 million 31 to 50 jobs, EUR 40 million 51 to 100 jobs and EUR 150 million more than 100 jobs. The ceiling applicable is assigned on the basis of the number of jobs the beneficiary holds each fiscal year.
- (19) In comparison to the previous existing schemes State aid N 222/A/2002 and N 222/B/2002, the current proposal of the Portuguese authorities foresees an increase of 25% in the applicable taxable base ceilings subject to reduced taxation. The method of adjustment takes into account two factors, the rate of inflation experienced since the previous existing schemes were authorised and the increase in the level of taxation per company. The changes are summarised in Table II.

Table II: Applicable tax base ceilings (Thousand EUR)

Number of jobs	Previous existing schemes	New scheme
	N 222/A/2002 N 222/B/2002	N 421/2006
1 to 2 jobs	1,500	2,000
3 to 5 jobs	2,000	2,600
6 to 30 jobs	12,000	16,000
31 to 50 jobs	20,000	26,000
51 to 100 jobs	30,000	40,000
More than 100 jobs	125,000	150,000

⁸ The Portuguese authorities have confirmed that the Portuguese legislation levies the capital duty to the companies authorised to operate in the ZFM in case of contribution of capital consisting of immovable property.

- (20) The companies registered under the previous existing schemes State aid N 222/A/2002 and State aid N 222/B/2002 at 31 December 2006 will continue to pay the reduced taxes fixed in the referred schemes until 31 December 2011. From 1 January 2012, those companies will pay taxes according to the provisions laid down in the present decision.

2.6. Beneficiaries

- (21) The companies that intend to access to the above-mentioned benefits should comply with one of the following two specific eligibility conditions:
- (a) Creation of 1 to 5 jobs in their first six months of operation and carrying out an investment of at least 75,000 EUR in the acquisition of fixed assets, material or immaterial, in the first two years of operation.
 - (b) Creation of 6 or more jobs in their first six months of operation.
- (22) Apart from this, the companies concerned must always start their operation within a given period of time from the moment of registration (six months in the case of international services, one year where industrial or shipping activities are concerned), or the new licences granted in the ZFM will lapse. The Portuguese authorities commit to issue the licenses in a transparent fashion and on the basis of objective criteria.⁹

2.7. Duration of the scheme

- (23) The period of application of the proposed scheme is from 1 January 2007 to 31 December 2013. The companies registered and authorised under the scheme before 31 December 2013 can continue benefiting from the fiscal advantage until 31 December 2020.¹⁰

2.8. Budget

- (24) The indicative budget of the measure for the period 2007-2020 is estimated at EUR 300 million (approximately EUR 22.5 million per year).¹¹ The annual breakdown of foregone revenue implied by the measure is provided in Table III.

Table III: Budget breakdown (EUR)

⁹ The scheme applies without distinction to companies' resident and non resident in Portugal.

¹⁰ In order to perceive the aid, the conditions applicable after 2013 to the companies registered before 31 December 2013 are the same as the conditions applicable in the present decision for the period 2007-2013.

¹¹ The estimated budget has been calculated using the effective average rate of taxation in Madeira for the fiscal year 2004 which amounts to 16.45% and on a stable rate of registration of 78 companies per year over the period 2007-2013.

Year	Total Fiscal expenditure
2007	1,288,743.29
2008	5,154,973.16
2009	10,309,946.32
2010	14,315,111.34
2011	19,086,815.12
2012	23,858,518.91
2013	26,330,606.41
2014	28,524,823.61
2015	28,524,823.61
2016	28,524,823.61
2017	28,524,823.61
2018	28,524,823.61
2019	28,524,823.61
2020	28,524,823.61
Total	300,018,479.80

2.9. Scope of the scheme

- (25) The access to the ZFM is restricted to the activities in the list drawn up for this purpose by the Portuguese authorities, which is based on the statistical nomenclature of economic activities in the European Community (the General Industrial Classification of Economic Activities within the European Communities - NACE Rev. 1.1).¹² This list includes services relating to:
- agriculture and animal production (Section A, codes 01.4 and 02.02),
 - fisheries, aquaculture and related services (Section B, code 05),
 - manufacturing industry (Section D),
 - production and distribution of electricity, gas and water (section E, code 40),
 - wholesale trade (Section G, codes 50 and 51),
 - transport and communication (Section I, codes 60 - 64),
 - activities relating to immovable property, leasing and services to companies (Section K, codes 70 - 74),
 - higher education and/or adult education (Section M, codes 80.3 and 80.4),
 - other collective services activities (Section O, codes 90, 92 and 93.01).
- (26) All activities involving financial intermediation, insurance and auxiliary financial and insurance-related activities (Section J, NACE codes 65 – 67), as well as all intra-group service activities (coordination, treasury and distribution centres) which could be carried out under Section K, code 74 (services provided mainly to companies) are excluded from the application of the scheme.

¹² OJ L 6, 10.1.2002.

- (27) In addition, the measure excludes the provision of operating aid intended to promote exports.
- (28) The application of the measure excludes companies in difficulties or firms in a restructuring process as defined in the Community Guidelines on State aid for rescuing and restructuring firms in difficulty.¹³
- (29) Should there be any changes to this list, given that classification systems of this type are liable to develop further, they will be duly notified to the Commission.
- (30) Moreover, according to the information provided to the Commission by the Portuguese authorities, the granting of the aid in question will comply with the regulations and guidelines under Community law covering certain types of activity in the fields of industry, agriculture and fisheries.

2.10. Cumulation

- (31) The aid to be granted under the scheme will be cumulable with aid from other sources or in different forms, under the condition that there is no overcompensation of the additional costs prescribed by the scheme.

2.11. Commitments

- (32) Concerning the application of the scheme, the Portuguese authorities committed to:
 - (a) Exclude enterprises in the financial sector and enterprises carrying out intra-group services from the application of the scheme.
 - (b) Submit annual reports on the scheme, which identifies the ten largest beneficiaries of operating aid, specifying the sector(s) of activity of the beneficiaries and the amount of aid received by each. (cf. point 83 of the RAG). In addition, provide to the Commission the names of the companies that have been refused for registration in the ZFM explaining the reasons for their refusal.
 - (c) Exclude from the application of the scheme projects for which eligible expenditure was incurred before the date of publication of the final scheme in the Internet (in compliance with point 108 of the RAG).
 - (d) Suspend payment of aid under the scheme to any undertaking that has not yet reimbursed or paid into a blocked account any illegal and incompatible aid plus interests it received under this aid scheme.
- (33) The scheme provides for respect of individual notification obligation foreseen in section 4.3. of the RAG – Aid for large investment projects.

¹³ OJ C 244, 1.10.2004, p.2.

3. ASSESSMENT OF THE MEASURE

3.1. Legality

- (34) By notifying the scheme, Portugal respected its obligations under Article 88(3) of the EC Treaty.

3.2. Existence of aid

- (35) The Commission considers that the measure constitutes State aid within the meaning of Article 87(1) of the EC Treaty. The involvement of State resources is demonstrated by the fact that the envisaged tax reductions constitute foregone revenue for the public budget. Moreover, given the scope of the sectoral and geographical application of the measure, the Commission considers that it is selective in that the measure targets specific enterprises active in Madeira. The measure potentially confers an advantage to the recipients by relieving them of charges they would normally have to bear, and might therefore threaten to distort competition. Moreover, to the extent that the activities carried out by these enterprises are open to international competition, they can affect trade among Member States.

3.3. Legal foundations of the measure

- (36) As the measure is aimed at regional development, the Commission assessed the compatibility of the measure on the basis of the RAG.
- (37) In accordance with point 17 of the RAG, the Commission takes note that, in recognition of the special handicaps which they face by reason of their remoteness and specific constraints in integrating into the internal market, regional aid for the outermost regions covered by Article 299(2) of the Treaty also falls within the scope of the derogation in Article 87(3)(a) of the EC Treaty. In this context and in accordance with the Portuguese regional aid map 2007-2013¹⁴, Madeira constitutes an outermost region fully eligible for regional aid under Article 87(3)(a) of the EC Treaty until 31 December 2013.
- (38) Consequently, the Commission has to assess whether the scheme meets the conditions of application of the exceptions of Article 87(3)(a) of the EC Treaty.

3.4. Compatibility of the aid measure

3.4.1. Qualification of the instruments

- (39) The Commission notes that the aid measure does not meet the conditions to qualify as investment aid. Fiscal aid can be considered aid to initial investment when these investments constitute its tax base. Additionally, all types of fiscal aid can enter into this category if its amount reaches a limit expressed in a percentage of the investment. In fact, the reductions on the taxes levied on the company's profits contribute to reduce the company current expenses it would normally have

¹⁴ See footnote 2.

to bear as part of its normal activities. Due to this reduction in the current expenses, the beneficiary would increase its profits and therefore the rate of return of its operations.

- (40) Therefore, the Commission establishes that the measure constitutes operating aid in the sense of the RAG.

3.4.2. Assessment of the measure

- (41) Insofar as the aid instrument in the measure constitutes operating aid, the Commission notes that, in accordance with point 80 of the RAG, in the outermost regions eligible for exemption under Article 87(3)(a) of the Treaty, this aid may be authorised in so far as it is intended to offset the additional costs arising in the pursuit of economic activity from the factors identified in Article 299(2) of the EC Treaty, the permanence and combination of which severely restrain the development of such regions (remoteness, insularity, small size, difficult topography and climate, and economic dependence on a few products).
- (42) On the proposed changes to introduce in the measure, the Commission considers that the increase in applicable tax rates applied per beneficiary is a positive factor since it diminishes the reduction from the standard rate of business tax in Madeira and thus the overall amount of aid.
- (43) Additionally, the Commission assesses positively the degressive nature of the measure since the aid amount perceived by potential beneficiaries diminishes over time.

3.4.2.1. Quantification of the additional costs

- (44) In order to justify that the measure is proportional to the handicaps it seeks to alleviate (cf. points 76 and 80 of the RAG), the Portuguese authorities have submitted the study “*Para uma Estratégia de Diversificação na Região Autónoma da Madeira*”¹⁵. The study prepared for the “*Governo da Região Autónoma da Madeira*” by the independent Dutch research institute, ECORYS-NEI (Netherlands Economic Institute) provides an estimation of the additional costs incurred by the private sector in the outermost region of Madeira.
- (45) The study is largely based on the results and the methodology applied in the study on the “*Costes de la ultraperiferia de la Economía Canaria*”¹⁶, used as supporting evidence to quantify the permanent handicaps faced by companies located in the Canary Islands of the two recently approved operating aid schemes in the Canary Islands for the period 2007-2013.¹⁷

¹⁵ Governo da Região Autónoma da Madeira, “*Para uma Estratégia de Diversificação na Região Autónoma da Madeira*”, 16 June 2003.

¹⁶ Consejería de Economía y Hacienda del Gobierno de Canarias, “*Los Costes de la Ultraperiferia de la Economía Canaria*”, 2001.

¹⁷ Comprising the two operating aid schemes for the Canary Islands, the “*Regimen Económico y Fiscal de Canarias*” (N 376/2006) and “*Zona especial Canaria*” (N 377/2006).

- (46) The study for Madeira has been customised to take into account of the specificities of the island by employing data extracted from the Regional Directorate for Statistics of Madeira and from the National Statistical Office of Portugal. Chapter 2 of the study identifies the different sources of costs faced by the companies located in Madeira and compares them to companies located in mainland Portugal. Table IV provides the breakdown of the additional costs per category in 1998.

Table IV: Breakdown of additional costs of the private sector in 1998

	% of GVA of private sector ¹	million EUR ²	% of GDP 1998 ³
Transport ⁴	7.9	121.6	5.1
Business trips	0.6	9.2	0.4
Stocks	4.0	61.6	2.6
Human resources	6.7	103.1	4.3
Instalations	0.4	6.2	0.3
Financing	4.0	61.6	2.6
Marketing	2.4	36.9	1.5
Total	26.0	400.1	16.7

1. The estimates of the additional cost apply the same percentages as the study of the Canary Islands.
2. Calculated on the basis of the GVA of private sector for 1998 of EUR 1,538.9 million
3. Computed on the basis of a GDP for 1998 of EUR 2,395.2 millions.
4. The distance between Lisbon and Funchal is approximately 530 nautical miles.

- (47) The repartition of the cost differentials with regard to the overall additional costs are the following: transport of goods (31% of total costs), business trips (2%), maintenance of stocks (15%), human resources (26%), marketing/advertising costs (9%), duplication of installations (2%) and financing (15%).
- (48) In view of the results of the mentioned study, the minimum additional cost deriving from the outermost character of Madeira amounts to 26% of the Gross Value Added (GVA) for the private sector or 16.7% of the regional Gross Domestic Product (i.e. EUR 400 million in 1998).
- (49) The Commission notes that the estimates of the additional costs drawn from the study remain rather conservative insofar as other studies carried out on behalf of the European Commission have identified that outermost regions face a wider set of additional costs.¹⁸ Moreover, the study used by the Portuguese authorities leaves unaccounted a series of additional costs which are extremely difficult to quantify. Examples of such costs are those deriving from the impediment to develop certain activities in Madeira or to account for the disappearance of certain companies that would have survived if it were not for the additional costs linked to the outermost character of the region. There are also non quantified costs connected to the excessive fragmentation of the market and to the particular

¹⁸ LL&A and Université Libre de Bruxelles, “*Etude sur l’identification et l’estimation des effets quantifiables des handicaps spécifiques propres aux régions ultrapériphériques ainsi que des mesures applicables pour réduire ces handicaps*”, January 2006.

constraints faced for experiencing economies of scale linked to the small size of the economy.

- (50) Contrary to the operating aid scheme on the “*Régimen Económico y Fiscal de Canarias* (State aid N 377/2006)” which is open to all companies, the scope of application of the proposed measure is limited to companies registered in the ZFM. In consequence, the Commission considers that to assess the proportionality of the measure and the potential overcompensation at the aggregated level it is required to confine the advantage of the measure to the additional costs faced by companies registered in the ZFM.
- (51) For this purpose, the identified additional costs are adjusted to the economic dimension of the ZFM. This dimension is approximated by the contribution of the ZFM to the regional economy of Madeira as provided in Table V.

Table V: Contribution of the ZFM to the regional economy of Madeira in 2004**Million EUR**

	R.A. Madeira	ZFM	ZFM / R.A. Madeira (%)
Turnover	14,375 ⁽¹⁾	4,486 ⁽²⁾	31.2 %
GVA	3,505 ⁽³⁾	712 ⁽²⁾	20.3 %
GVA/Turnover (%)	24.38%	15.87%	-

Source:

- (1) Turnover in 2004 for all companies – INE, to be published in the Statistical Yearbook of R.A. of Madeira 2005
- (2) Regional Government of Madeira
- (3) Provisional value National Statistical Institute

(52) According to the data provided by the Portuguese authorities, the ZFM represented 20.3% of the Gross Valued Added of Madeira in 2004 (approximately EUR 712 million).

3.4.2.2. Proportionality of the measure

Overcompensation at the aggregated level

(53) The assessment of the proportionality of the measure at the aggregate level requires comparing the foregone revenue implied by the measure with the additional costs attributed to the companies registered in the ZFM. Table VI provides an estimate of the proportionality of the aid for the period 2000-2004.

Table VI: Proportionality of aid**Million EUR**

	2000	2001	2002	2003	2004
Foregone fiscal revenue ZFM (*)	22.50	22.50	22.50	22.50	22.50
GDP Madeira	3,289.60	3,284.70	3,961.30	3,979.40	4,041.80
Additional Costs of Madeira (**)	549.36	548.54	661.54	664.56	674.98
Additional Costs of ZFM (***)	111.60	111.43	134.38	135.00	137.11
%Fiscal advantage/Additional cost of ZFM	20.16%	20.19%	16.74%	16.67%	16.41%

(*) Estimate of the average annual foregone revenue for the period 2007-2020 as provided by the Portuguese authorities in the notification.

(**) The additional cost incurred by companies located in Madeira due to the outermost character of the Islands in the ECORYS study is 16.7% of the GDP Madeira in 1998. The calculation of the additional cost for the remaining years rests on the assumption that the share of the additional costs over GDP has remained constant over the period analysed.

(***) The allocation of the additional costs of the ZFM is computed applying the estimated contribution of the ZFM to the regional GVA of Madeira which according to the Portuguese authorities represents 20.31% of the GVA of Madeira in 2004. The GVA of Madeira has been extracted from the Regio Database of EUROSTAT.

(54) The Commission observes that for the period 2000-2004, the fiscal advantages represent between 16.41% and 20.16% of the total additional costs of the ZFM.

- (55) The Commission notes that the measure allows to compensate the additional costs of companies located in the referred outermost region.
- (56) This measure constitutes the main operating aid scheme in Madeira. Since the advantage conferred by the scheme remains significantly below the additional costs faced by the ZFM, the Commission concludes that at the aggregated level the measure does not in principle incur in overcompensation and that the aid envisaged in the measure is proportional and targeted to the specific handicaps it is seeking to alleviate.

3.4.2.3. Overcompensation at the level of each beneficiary

- (57) The design of the measure where ceilings apply to the taxable base which is subject to reduced taxation ensures that the perceived amount of aid per company is limited.
- (58) The proportionality of the measure at the level of each beneficiary is estimated by comparing the additional costs faced per company to the fiscal advantage provided by the measure.
- (59) For the purpose of this decision, the additional costs at the individual level are approximated by assuming that the same percentage of additional costs identified at the macro level for the outermost region (16.7% of the regional GDP in 1998), also applies to the profit structure of the companies registered in the ZFM. Therefore, the additional cost faced per aid beneficiary would amount to 16.7% of its taxable base.
- (60) An approximation to the advantage provided by the measure results from calculating the difference between the effective tax rate applicable in Madeira (16.45%) and the reduced rate taxation applicable to companies licensed in the ZFM (3% for 2007-2009) multiplied by the taxable base ceiling. For the period 2007-2009, the advantage amounts to EUR 269,000 for companies creating 1 to 2 jobs, EUR 350,000 for companies creating 3 to 5 jobs, EUR 2.15 million for companies creating 6 to 30 jobs, EUR 3.5 million for companies creating 31 to 50 jobs, EUR 5.38 million for companies creating 51 to 100 jobs and EUR 20.17 million for companies creating more than 100 jobs. For the periods 2010-2012 and 2013-2020, the advantage per company diminishes since the applicable tax rates increase to 4% and 5% respectively.¹⁹
- (61) The Commission notes that the advantage provided by the measure diminishes with the number of jobs created by the beneficiary. Therefore, the design of the measure follows a principle of proportionality. Additionally, at the level of each beneficiary, the advantage provided by the measure is below the imputed additional costs.

¹⁹ Even under the worst case scenario of application of the conditions of points 16 and 17 of the present decision, the advantage provided by the measure is below the additional costs faced per aid beneficiary. It should be noted that in most of the cases the aid beneficiary will not reach the maximum taxable base ceiling allowed by the measure.

- (62) Consequently, the Commission considers that, in principle at the level of each beneficiary, the measure is proportional and does not lead to an overcompensation of the additional costs it is intended to offset.

3.4.2.4. Contribution to regional development

- (63) In view of the type of economic activities supported, the Commission notes that the scheme contributes to the regional development and the diversification of the economic structure of Madeira.
- (64) The Commission observes that the scheme supports the generation of employment since one of the conditions for the companies to benefit from the scheme is to create and maintain the employment created. Table VII shows the volume and evolution of employment in the ZFM.

Table VII: Employment in the ZFM

Sectors of activity	2002	2003		2004		2005	
	Number	Number	Annual variation	Number	Annual variation	Number	Annual variation
Total	2752	2888	5%	3141	9%	2843	-9%
Of which:							
International services	1,778	1,862	5%	2,038	9%	1,902	-7%
Industrial economic zone	488	604	24%	709	17%	763	8%
Financial services	486	422	-13%	394	-7%	178	-55%

Source: Annual report of the ZFM for 2005, completed by the SDM for 2005.

- (65) The Commission notes that the industrial economic zone is the sector in the ZFM that has experienced the largest increase in employment during the period 2002-2005. The Commission observes that it is companies in the industrial economic zone that have the largest potential to contribute to the regional development of the Island as these companies are more likely to develop closer links with the local economy.
- (66) In accordance with the data provided by the Portuguese authorities (see Table V above), the Commission notes the significant contribution of the ZFM to the regional economy which amounts to a GVA of EUR 712 million (20.3% of the GVA of Madeira).
- (67) In view of the above, and also on the basis of the principle underlying its previous decisions on State aid N 222/A/2002 and N 222/B/2002, the Commission concludes that the scheme contributes in a proportional way to the regional development of Madeira.

3.4.2.5. Aid to transport activities

- (68) The international shipping register (MAR) complies with the Community guidelines on State aid to maritime transport²⁰ which state that, *“in the context of regional aid schemes, the Commission will apply the general rules set out in its*

²⁰ OJ C 13, 17.1.2004, p.3.

communications on national regional aid or future amendments thereto” (Section 6).²¹

- (69) The quantification of the additional costs in the outermost region of Madeira also includes activities carried out in the transport sector. The costs identified in the study include in particular transport of goods, regulatory stocks, human resources, duplication of installations and business and correspond largely to the costs that the Commission has accepted as regards the aids in the transport sector.

3.4.2.6. Aid to fisheries, aquaculture and related services

- (70) The Portuguese authorities engage the aid awarded to the fisheries, aquaculture and related services covered by the notified scheme to comply with the conditions established in the Guidelines for the examination of State aid to fisheries and aquaculture.²²

3.4.2.7. Aid to agriculture activities

- (71) The Commission notes that the present scheme also covers the agriculture and forestry activities. The operating aid granted under this measure to the sectors of production, processing and marketing of Annex I products of the EC Treaty can be authorised on the basis of the Community Guidelines for State aid in the agriculture and forestry sector²³ and on the basis of the Council Regulation 247/2006 of 30 January 2006 laying down specific measures for agriculture in the outermost regions of the Union.²⁴

3.5. Conclusion

- (72) On the basis of the foregoing assessment, the Commission considers the notified measure “*Zona Franca da Madeira*” to be compatible with the common market pursuant to Article 87(3)(a) of the EC Treaty.

4. DECISION

- (73) The Commission has accordingly decided that the aid awarded under the “*Zona Franca da Madeira*”, fulfils the criteria to be considered compatible with the common market pursuant to Article 87(3)(a) of the EC Treaty.
- (74) The Commission reminds the Portuguese authorities about the necessity of respecting the rules on cumulation of aid, both in the case of aid awarded for different purposes and in the case of aid awarded for the same purpose under schemes approved by one single entity or by various entities (central, regional

²¹ Cf. previous Commission decision of 4 February 2003 concerning State aid N 222/B/2002.

²² OJ C 19, 20.1.2001, p.7

²³ OJ C 319, 27.12.2006, p.1.

²⁴ OJ L 42, 14.2.2006, p.1.

and/or local authorities). In the latter case, the cumulated intensity of the aid shall not exceed the largest maximum foreseen in the different aid schemes concerned.

- (75) The Commission also reminds the Portuguese authorities to submit an annual report on the application of the measure which allows the Commission to verify that all given conditions are being fulfilled, in particular the respect of the proportionality between the operating aids and the additional costs faced by the economic activity in the region. In addition, to provide the names of the companies refused for registration in the ZFM explaining the reason for their refusal.

In case this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt. If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site: http://ec.europa.eu/community_law/state_aids. Your request should be sent by registered letter or fax to:

European Commission
Directorate-General for Competition
State Aid Greffe
B-1049 Brussels
Fax No: +32 2 29 61242

Yours faithfully,
For the Commission

Neelie KROES
Member of the Commission