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Archwilydd Cyffredinol Cymru  
Auditor General for Wales

# European Union Structural Funds 2007-2013



WALES AUDIT OFFICE  
SWYDDFA ARCHWILIO CYMRU





I have prepared and published this report in accordance  
with the Government of Wales Act 2006.

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# Summary

- 1 This report examines the administration of the 2007-2013 European Union (EU) structural funding programmes in Wales (**Exhibit 1**). As the 'Managing Authority', these programmes are managed by the Welsh European Funding Office (WEFO), a division of the Welsh Government, and are overseen by a Programme Monitoring Committee<sup>1</sup>. Individual projects are overseen by a 'project sponsor' organisation but can involve several partner organisations.
- 2 WEFO's responsibilities include selecting projects and approving their business plans, paying grant and claiming reimbursement from the Commission, monitoring progress and evaluating impact. WEFO is also responsible for ensuring compliance with the regulations governing the deployment of EU funding, with potentially severe financial penalties for non-compliance.
- 3 Reflecting experience from the 2000-2006 programmes, the Welsh Government embarked on the 2007-2013 programmes with a desire to streamline programme structures, focus the programmes more closely on strategic priorities and manage performance more effectively through fewer but larger projects. The Welsh Government also wanted a stronger emphasis on collaboration between stakeholders and greater use of competitive procurement.

## Exhibit 1 – Wales and the European Union Structural Funds

Wales is eligible to receive around €2.22 billion from the 2007-2013 EU structural funding programmes, which aim to reduce social and economic disparities between the regions of the EU. Spending under these programmes will continue until the end of 2015. Wales received €2.14 billion under the 2000-2006 structural funding programmes and has been provisionally allocated around the same amount for the 2014-2020 programmes.

As at the end of 2013, the value of the EU funding under the 2007-2013 programmes is equivalent to around £1.9 billion. With other match funding from UK sources, the total value of the programmes over the whole of the programming period is around £3.2 billion.

Because the value of the structural funds programmes to Wales is set in euros at the outset of the programmes, fluctuating exchange rates are part of the challenge in meeting annual spending targets. If these targets are not met, the unspent balance is withdrawn by the EU and is not normally re-committed to the programmes.

The EU funding comes from two main sources:

- £1.11 billion from the European Regional Development Fund (ERDF) for business support, commercial innovation, economic infrastructure, renewable energy and regeneration; and
- £756 million from the European Social Fund (ESF) to support training and other initiatives to increase economic participation and raise the skills of the workforce.

Each of these funds is delivered through two programmes – Convergence and Regional Competitiveness and Employment (Competitiveness) – making four main programmes in total. The Convergence Programmes account for around 94 per cent of the available EU funding and are designed to improve the economy of 15 local authority areas in West Wales and the Valleys that have a gross domestic product (GDP) of less than 75 per cent of the EU average. The Competitiveness Programmes are available for the rest of Wales (known as East Wales).

Each of the four programmes is supported by an 'operational programme' document, a plan setting out how funds will be used to meet agreed objectives. The operational programmes were agreed with the European Commission during 2007. For the 2007-2013 programmes, the operational programmes are complemented by a series of strategic framework documents developed by the Welsh Government that provide additional guidance on priorities and project design.

<sup>1</sup> The Programme Monitoring Committee comprises representatives from various organisations. The European Commission has observer status, receives regular progress reports and undertakes its own audits to verify compliance with its regulations.

- 4 This report considers whether the 2007-2013 programmes have been administered effectively by WEFO and are on track to deliver their intended benefits, examining progress against targets for the allocation of funding, expenditure and key outputs. This report was prepared by staff of the Wales Audit Office on behalf of the Auditor General for Wales. **Appendix 1** sets out in full our audit methodology. We reviewed the overall administration of the programmes at a relatively high level, supplemented by some case studies and supported by a survey of project sponsors and WEFO project development officers (PDOs). More in-depth reviews, such as our recent consideration of WEFO's funding of projects sponsored by the All Wales Ethnic Minority Association (AWEMA), do indicate some weaknesses in administration at project level. We have also taken into account other evaluations and reviews, including Dr Grahame Guilford's March 2013 report on arrangements for the next programming round.
- 5 We have concluded that the programmes have generally progressed well, supported by improved management arrangements when compared to the previous programming round and despite certain difficulties in the early stages. It is too early to assess the overall impact of the programmes, which may not be fully evident for some time after the programmes have closed, but there are positive signs from ongoing evaluations.
- 6 The European Commission has recently reviewed its guidance on the methodology to be used by Audit Authorities (the bodies in each region that audit expenditure on its behalf) in selecting projects for audit. As a result, it is now normally requiring the use of statistical sampling approaches rather than the random non-statistical sampling approach hitherto used by the Audit Authority in Wales and some other regions across Europe. This has led to a temporary interruption of ERDF payments on technical grounds while error rates are recalculated. Indications are that error rates remain relatively low overall in Wales and the Welsh Government has taken action to ensure that the interruption has not affected payments to project sponsors. The Welsh Government is optimistic that the situation will be speedily resolved.
- 7 In drawing comparisons with the 2000-2006 programmes, we have taken into account the findings from reports by the National Audit Office Wales in 2002 and 2004. We referenced these findings in our December 2013 report on *Public Funding of Penmon Fish Farm*. Penmon Fish Farm received EU funding under the 2000-2006 programmes. We also reported on issues relating to 2000-2006 programme funding in the *Management of public funding of Cymad Cyf* (May 2010) and funding for the Cywain Centre in Bala (April 2014).
- The programmes have progressed relatively well overall despite certain difficulties, but it is too early to assess their overall impact**
- 8 **Overall, WEFO has made good progress in committing available funds to projects.** Although some project sponsors appear to have expected that the programmes would have got off to a faster start, WEFO has since achieved most of its annual commitment targets, which were more challenging than those set in the operational programmes. Despite the impact of falling exchange rates<sup>2</sup> and the withdrawal of funding for certain projects following changes in Welsh Government policy, by the end of 2012 most programme areas were fully committed.

<sup>2</sup> A sharp decline in the £/€ exchange rate after programme approval released a substantial amount of additional funding that needed to be committed to projects.



While progress was slow in some programme areas initially WEFO has responded appropriately to address shortfalls in commitment by working with the Welsh Government to stimulate project development and by re-allocating funding to other areas.

9 **The programmes have met EU spending targets, despite the rate of expenditure overall being slower than forecast by project sponsors.** WEFO has met all the annual spending targets set for each programme, usually by a comfortable margin. In 2010, the European Commission revised its targets for the programmes to take account of the adverse impact of the wider economic downturn on match funding. WEFO decided that it would still seek to meet the original, more demanding, annual targets and has mostly done so.

10 As at the end of 2013, WEFO had certified £2.17 billion of project expenditure as being eligible for reimbursement by the EU. Programme spending rates have been boosted by: an increase in the average intervention rate<sup>3</sup> permitted by the European Commission, which released an additional £187 million of EU funding by 31 December 2013; some retrospective funding of projects which were wholly or partially complete before they were approved by WEFO for EU funding; and the payment of £73 million of EU funding into investment funds that counted against the ERDF targets when the money was paid into the funds, not when it was paid out from the funds through investments.

11 Individual projects do not have formal spending targets, but each project sponsor agrees with WEFO a delivery profile which includes forecast spend. In general, the pattern of project expenditure is consistent with the previous programmes. As at December 2013, around one in three projects in progress were 20 per cent or more behind their expenditure profile. The overall shortfall between actual and forecast spending fell from 31 per cent in June 2010 to 19 per cent in December 2013, but much of that improvement is due to project sponsors updating their profiles rather than catching up with their original profiles. Project spending has been slower than forecast for a variety of reasons including general over-optimism, difficulties with procurement and staff recruitment and the impact of the economic downturn.

12 **The programmes are on track to meet, and in some cases far exceed, most of their key performance targets.** Taking the Convergence and Competitiveness Programmes together, WEFO expects to meet the targets it has set for its key 'dashboard indicators' ([Exhibit 2](#)). The ESF programmes, in particular the Competitiveness Programme, have performed strongly and are forecast to exceed all of their programme level targets, many by a substantial margin ([Appendix 4](#)). At the end of 2013, project sponsors' forecasts indicated that the ERDF Convergence Programme would meet six of its 11 programme level targets and the Competitiveness Programme would meet five of its eight targets ([Appendix 3](#))<sup>4</sup>.

<sup>3</sup> The intervention rate for an individual project reflects the proportion of a project's total cost that is met by EU funding rather than match funding.

<sup>4</sup> Overall, the six ERDF programme level indicators that would not be met relate to the five themes of: gross jobs created; investment induced; new or improved products, processes or services launched; waste reduced, re-used or recycled; and profit benefit. The profit benefit measure is intended to capture increases in profits arising from savings or productivity benefits achieved with EU funding support. WEFO has not prescribed any particular method for calculating profit benefit and beneficiaries are finding it difficult to attribute and calculate profits to specific services received from EU funded projects. Under-reporting is likely, although economic conditions are also a factor.



## Exhibit 2 – Key performance indicators for ERDF and ESF programmes<sup>1</sup>

	Target <sup>2</sup>	Forecast <sup>2</sup>	% of target forecast to be achieved	Achieved at 31 Dec 2013
Enterprises assisted (ERDF)	15,900	22,038	139%	12,703
Enterprises created (ERDF)	5,604	11,849	211%	7,574
Gross jobs created (ERDF)	38,540	43,052	112%	23,649
Participants (ESF)	294,100	629,227	214%	487,542
Participants entering employment (ESF)	31,000	88,354	285%	53,781
Participants gaining qualifications (ESF)	89,180	235,396	264%	160,847

### Notes:

<sup>1</sup> WEFO focuses on between eight and 14 key performance indicators to monitor the delivery of each of the operational programmes. WEFO focuses particular attention on the six indicators listed above that form the basis of its performance reporting as part of the Welsh Government's wider performance management arrangements. We have combined here the Convergence and Competitiveness programme targets for each Fund.

<sup>2</sup> Target and forecast refer to the end of the programmes. The programmes are expected to close at the end of 2015.

Source: WEFO

- 13 There are over a hundred monitoring indicators altogether across the four programmes and their respective priorities. There is mixed performance at a priority level, reflecting the particular impact on certain priority areas of changes in economic conditions, policy and the distribution of funding compared with initial assumptions. Based on project sponsors' forecasts at 31 December 2013, 72 of the 125 ERDF priority-level targets and 50 of the 62 of the ESF priority-level targets would be met by the end of the programmes.
- 14 The programmes are now considerably bigger in terms of total committed expenditure (12 per cent - 38 per cent at the end of 2013) than envisaged when the targets were set, and performance needs to be viewed in this context. For the ESF programmes, the economic downturn has created more demand for employment support and retraining services for the newly unemployed and increasingly for young people entering the labour market. However, it appears that the ESF programme targets were set too low initially. Delivery on most indicators was lagging behind project sponsors' profiled figures at the end of 2013, in part reflecting slippage against projects' spending profiles.

- 15 **The cross cutting themes of environmental sustainability and equal opportunities are better established than in the previous programmes, but the programmes are likely to fall short of most of the related targets.** For example, the proportion of participants from older age groups and those with a work-limiting illness or disability is likely to fall well below the levels expected. However, because the ESF programmes are likely to exceed their overall participation targets by substantial margins, the overall number of women and black minority ethnic (BME) participants is likely to be higher than originally expected, despite the overall proportion of participants from these groups falling short of the targets set. In January 2011, an evaluation commissioned by WEFO reported variable progress among sponsors in integrating the cross-cutting themes into delivery of their projects, and found that sponsors often lacked the knowledge and resources to provide specialist advice to beneficiaries.
- 16 **While it is too early to assess the overall impact of the programmes, there are some positive signs and ongoing evaluations will paint a clearer picture.** The evidence is most developed for the ESF programmes and findings emerging from the ESF Leavers' Survey and other evaluation work indicate a positive effect on participants, but with the programmes' impact on employment rates varying significantly by participants' gender, age, location, state of health and employment history.
- 17 The 2011 ERDF Business Survey results suggest that the ERDF programmes have created or safeguarded a significant number of jobs, but only a minority of respondents credit ERDF with tangible outcomes for their business. The survey findings indicated that the effect of safeguarding jobs was at least as significant as job creation. The survey was based on a relatively small sample of programme activity, but it is being undertaken again in 2014.
- 18 **Evidence for the 2000-2006 programmes suggests a positive impact on jobs and skills, but the prosperity gap between Wales and the EU average remains significant.** An analysis by WEFO in 2011 attributed to the previous programmes the creation of between 26,000 and 45,500 jobs and between 1,700 and 2,500 small and medium sized enterprises (SMEs), with between 48,700 and 89,300 people entering employment or further learning as a direct result of their participation in ESF programmes. It is difficult to assess the wider economic impact of the programmes as they are intended to lead to long-term improvements in economic capacity that are hard to link to specific interventions. In fact, the region's GDP position relative to UK and EU averages worsened between 2000 and 2010, partly because of the effect of commuting between the Valleys and East Wales. However, other indicators such as primary income, employment rates, economic activity rates and qualification levels had all improved to some extent in the period from 2001 to 2008 and with some closing of the gap with UK averages.

## Management arrangements are effective and have improved since the previous programming round, despite some disruption in the early stages of programme implementation

- 19 **There have been mixed views about the overall administration of the programmes, although stakeholders generally support the action that WEFO has taken to simplify programme structures and reduce the number of projects.** We found that project sponsors tended to view WEFO's management system as slow and bureaucratic, but felt that it was working better after a difficult start. There was broad support for WEFO's decision to simplify programme structures and to reduce the number of projects (which has fallen from 2,463 in the previous programmes to less than 300), although sponsors raised some practical concerns about collaboration and partnership working and the delivery record of larger projects.
- 20 **The programmes have been flexible enough to respond effectively to the economic downturn and to some significant changes in policy.** WEFO re allocated resources and changed certain eligibility criteria to respond to the economic downturn. In 2009, WEFO used the opportunity of a weaker pound (which had increased the sterling value of the EU funding) to negotiate an increase in grant rates with the European Commission, thus easing pressures on match funding.
- 21 WEFO also worked quickly and effectively with other parts of the Welsh Government to reflect policy changes arising from the launch of the Economic Renewal Programme in 2010. The smaller number of projects compared with the previous programmes, many of them sponsored by the Welsh Government, made this a much easier task than it would otherwise have been. In addition, WEFO has modified the ESF programmes to avoid duplicating the UK Government's 'Work Programme'.
- 22 **The greater use of procurement as a delivery model proved difficult to implement, but if well managed should have positive effects in the longer term.** WEFO expects that around a third of all programme expenditure will be spent through procurement by project sponsors. In practice, many projects operate mixed delivery models, with some services being procured and others delivered directly or via grant schemes.
- 23 Although generally seen as the right approach, the greater emphasis on competitive procurement has been difficult to implement. However, some of the early challenges have been overcome after WEFO reviewed its guidance on delivery models. WEFO has achieved a high level of compliance with procurement regulations<sup>5</sup>, but the extent to which the increased emphasis on competitive procurement has delivered better value for money and wider access to EU funding is less clear. At the end of 2013, project sponsors had awarded a total of 2,569 contracts worth £1.09 billion through procurement, mostly to the private sector (£644 million), with the voluntary sector securing contracts worth £178 million. There is no data available with which to compare these figures with the previous programming round.

<sup>5</sup> WEFO has achieved a very low rate of error attributable to procurement issues, in contrast to some other part of the EU where the Commission has levied large fines on managing authorities.

- 24 **WEFO has established a robust system to support project development and selection but sponsors can find the process challenging and time consuming.** WEFO has established effective mechanisms for ensuring that projects align with strategic objectives, as set out in the strategic framework documents, but there is scope to develop a more sophisticated approach for the next round of programmes.
- 25 WEFO adopted a new approach to prioritise, develop and select projects for the 2007-2013 programmes, including the introduction of an expression of interest stage to filter out unsuitable projects. Overall, this system is based on sound criteria and has improved the quality of project proposals, helped by the introduction by WEFO of 'project development officers' to provide a single and continuing point of contact for project sponsors. The selection criteria have also been identified as good practice by the European Commission. However, the length of the process and its administrative requirements have been a source of frustration for some project sponsors and opinions about the overall system of support and guidance for project sponsors do vary.
- 26 Changes in programme administration, with many project sponsors and WEFO staff unfamiliar with the new systems, made it particularly difficult to provide effective support during the early stages of the programmes. However, we found no clear consensus on improvements that could be made and, in our view, there is no need to fundamentally change the process for the next programming round, which should help to ensure a smooth transition. WEFO aims to focus the 2014-2020 programmes more clearly on areas of economic priority using a single framework document and to further streamline the project development process without reducing its scrutiny of project bids.
- 27 **Financial management is sound.** The development of a new IT system has made it much easier for WEFO to manage programme finances, as well as streamlining other aspects of programme administration. The system has come at a significant cost – a development cost of £18.1 million and annual running costs of £1.25 million – although it is cited by the European Commission as a benchmark for other managing authorities and WEFO is confident that it will be able to continue using the system for another eight years with little additional investment required.
- 28 WEFO pays grants on a timely basis after making appropriate checks and has recently strengthened controls over advance payments. WEFO is also in a good position to manage fluctuations in the exchange rate and other financial risks as the programmes draw to a close. WEFO is pursuing a policy of over-committing the EU funding allocation to reflect the pattern of under-spending by sponsors in the previous programming round. WEFO intends to identify projects where provision could be scaled back if required or rolled forward through new projects in the next programming round.
- 29 WEFO has generally effective financial management systems, including a series of 'management verifications', to ensure compliance and to detect errors before project expenditure is declared to the European Commission. Grant claims are scrutinised by WEFO's payments team and subject to independent external audit. WEFO's Project Inspection and Verification (PIV) team reviews sponsors' systems of financial control and inspects project expenditure. WEFO itself is subject to audit by the Audit Authority (the Welsh Government's European Funds Audit Team – EFAT) and the EU's own auditors. The irregularity rate in expenditure declared to the European Commission has been well below the

two per cent level that is the maximum accepted by the European Commission. However, as noted in **paragraph 6**, the Audit Authority is currently in the process of recalculating error rates to meet the European Commission's revised requirements, although the indications are that these remain low overall.

30 Compliance and audit requirements can impose a heavy administrative burden on project sponsors and there is a significant degree of overlap between audit functions. Whilst this situation is largely unavoidable because each function is required by EU regulations, there is some scope for WEFO to coordinate this work to reduce overlap.

31 **Performance is better managed than under the previous programmes but could be tighter in some respects.** WEFO monitors the progress of projects after approval through the quarterly grant claims and progress reports, which all projects are required to submit, and regular meetings with sponsors at which any problems or significant issues can be discussed. Our review of project files indicated that these review meetings were not always held regularly and the reasons for delays in project implementation were not always clear from the files. Nevertheless, performance management is tighter than under the previous programmes, and is facilitated by the smaller number of projects. WEFO has withdrawn funding from projects that have not performed as well as expected, a process that is easier than it was under the previous programmes because many projects are managed by the Welsh Government.

32 **WEFO has strengthened monitoring and evaluation arrangements and developed more robust approaches to measuring impacts, but data quality remains a concern.** WEFO's Research, Monitoring and Evaluation (RME) team collates and reports monitoring data, organises programme level evaluations and advises projects on evaluation. There is a set of coherent, well-defined monitoring indicators. The 'gross jobs created' indicator, however, does not fully capture all the employment effects because it excludes safeguarded jobs, temporary posts and project administration jobs. There has also been variable progress in measuring 'soft outcomes' to capture the impact of activities designed to develop personal attributes among those at risk of exclusion from the labour market.

33 WEFO has introduced controls and guidance to improve the often poor quality of data in the previous programming round. However, concerns remain about data quality at the participant level and double counting of outcomes between projects.

34 WEFO's evaluation plan builds on experience with the previous programmes. A series of interim thematic evaluations is nearing completion and, with interim project evaluations, will inform the design of the 2014-2020 programmes, although it is too early to assess the impact of most projects at this stage. WEFO has developed a more sophisticated approach to measuring net impact using the Labour Force Survey and the business datasets held by the Office of National Statistics to develop control groups with which the results of the programmes can be compared. This approach has worked quite well for the ESF programmes, but poor data quality and the limited scope of the business datasets has prevented the ERDF Business Survey from building reliable control groups.

# Recommendations

- R1 Some sponsors were unclear initially about the project selection process and expected a shorter process than WEFO believed was realistic. To help ensure that expectations are more closely aligned at the outset for future programming rounds, **we recommend that WEFO publishes guidance that explains the content, purpose and likely duration of each step of the process leading up to project approval, indicating the most common causes of uncertainty and delay and how such problems may be averted or mitigated. The guidance should set out the responsibilities of both the sponsor and of WEFO for ensuring that the process runs smoothly and with minimal delay.**
- R2 Uncertainty about permissible delivery models (for example, procurement versus direct delivery) caused disruption and delay to the progress of some applications. Some sponsors were unprepared for the switch to a procurement-led approach and lacked the expertise to run an effective procurement exercise. **We recommend that:**
- a **WEFO specifies its policy on delivery models (and procurement more specifically) at the outset of the next programming round, making any changes to the current policy in consultation with stakeholders while the operational programmes are being developed, and subject to any changes required by the Commission.**
  - b **WEFO reviews the capacity of project sponsors to run effective procurement exercises and builds capacity where appropriate. This may include the provision of procurement expertise to a wider range of sponsors using technical assistance (only voluntary bodies currently benefit), training and dissemination of good practice.**
- R3 The Welsh Government's strategic framework documents have helped WEFO to assess applications but they have been of more limited value for applicants and have not been used proactively to monitor progress or develop actions to fill gaps in service delivery. For the 2014-2020 programmes, WEFO's proposals for an alternative *Economic Prioritisation Framework* that is regularly updated will help address this issue. **We recommend that:**
- a **strategic guidance (in the form of the Economic Prioritisation Framework or otherwise) should be as specific as possible about types of activity, target beneficiaries and delivery approaches, including relative priorities, whilst recognising the constraint that specific projects cannot be guaranteed funding unless and until they have gone through the appraisal process and been approved; and**
  - b **the guidance is updated regularly, with an emphasis on identifying actions to exploit any new opportunities or to address problems or gaps in delivery.**
- R4 The scope for simplifying the process is limited by the need to maintain a process that meets EU requirements and ensures that proposed operations are supported by clear, robust and credible delivery plans. **We recommend that:**
- a **WEFO make no major changes to the current process, but consider opportunities to simplify or clarify certain aspects of the process as part of its work to develop the 2014-2020 programmes;**
  - b **publish guidance in good time for the launch of the next programming round so that applicants have access to comprehensive guidance from the outset; and**



- c **make guidance as specific as possible, to avoid complaints about ambivalent guidance and inconsistent application by PDOs.**

R5 The duration of the project development process was a major concern of project sponsors. We recognise that each project will be different and a standard timetable may not be appropriate. However, **we recommend that a clear understanding is agreed with project sponsors at the outset of project development so that each party knows what is required of them by when, and that the key milestones in project development are monitored by WEFO so that allegations of undue delays can be investigated.**

R6 There were some problems mobilising the programmes in 2008 and 2009. Timely mobilisation is necessary to ensure a smooth transition between programming periods and to help meet spending targets. We endorse WEFO's proposals, acting on the Guilford Review, to introduce a mobilisation phase for the 2014-2020 programmes that will require sponsors to set aside time to establish delivery mechanisms, for example to select contractors. **We recommend that:**

- a **work begins before the new programmes are launched on developing key 'strategic' projects, with the aim of approving them as soon as possible of the approval of the operational programmes; and**
- b **WEFO require the timetable for project delivery to include key milestones for the mobilisation and delivery phases, and uses this timetable to challenge and amend unrealistic timescales, which often underlie over-optimistic spending profiles.**

R7 WEFO has already strengthened the monitoring of outputs and results compared with the last programming round and has improved its approach to evaluating impact. To further strengthen these arrangements, **we recommend that:**

- a **Given the fact that most ESF programme targets have been exceeded by a wide margin, targets for the new programming round should be set at a challenging but realistic level based on current economic conditions and experience to date in the current programming round.**
- b **For the next round of ESF programmes, the definition of an unemployed participant should be aligned with that used by the Labour Force Survey. Currently the ESF programmes only count Jobseeker's Allowance claimants as unemployed, but this tends to over-state the extent to which the programmes are targeting the most disadvantaged, economically inactive population.**
- c **WEFO replaces the 'profit benefit' monitoring indicator with one that is more clearly defined and easier to measure, such as increase in turnover or cost reduction arising from EU funding.**
- d **WEFO should strengthen its focus on monitoring output targets to ensure that output targets, including the distribution of outputs between target groups and geographical areas where appropriate, are agreed and monitored by all project sponsors at regular intervals.**



- e **Programme monitoring reports should include full explanations of any significant variations from expected figures, including significant shortfalls in the proportion of participants from disadvantaged groups or other evidence of potential gaps in project delivery. The Committee should discuss progress against output and result targets for each programme at least annually and recommend any actions to address any shortfalls.**
- R8 A large proportion of programme funding is delivered through procured contracts, which have the potential to benefit companies based in Wales, especially small and medium-sized enterprises. WEFO does not collect information on the value of contracts awarded to SMEs and Welsh-based companies. Such information would be helpful in order to evaluate the impact of programme delivery on the Welsh economy. **We recommend that WEFO monitor the value of contracts awarded to Welsh-based companies and SMEs.**
- R9 Project sponsors are subject to a rigorous audit and inspection regime that has successfully kept error rates relatively low. However, the system can be burdensome for sponsors. **We recommend that, for the 2014-2020 programming rounds, WEFO review the scope of each element of the audit and inspection regime with a view to removing unnecessary duplication, coordinating work to develop a risk-based approach as far as practicable, and building on its existing preventive work.**
- R10 WEFO has found it problematic to obtain participant level data of acceptable quality from project sponsors on a timely basis, especially for ERDF projects, and this has hampered ERDF evaluation efforts. Procurement data is also incomplete. **We recommend that WEFO:**
- a **more rigorously enforce data quality standards so that sponsors provide timely, accurate and complete information on participants and businesses; and**
  - b **consider replacing the provision of participant data on spreadsheets with an interactive database whereby sponsors enter data directly in a prescribed format, thus improving the quality of data submitted, reducing the risk of duplicate outcomes and reducing administrative costs for WEFO.**
- R11 The 2011 ERDF Business Survey, which is being repeated in 2014 had relatively high refusal and non-recall rates (businesses that could not remember even receiving assistance). To improve data quality, **we recommend that WEFO undertake the ERDF Business Survey on an ongoing basis, perhaps at a specified interval after the completion of support for a particular business, with periodic reporting of results to provide evidence of impact.**

R12 Most project evaluations are commissioned independently by project sponsors, and there is limited collaboration between sponsors or links with other evaluations that might provide good evidence of emerging impacts. **We recommend that WEFO:**

- a **Enable project sponsors to use data relating to their projects from programme wide evaluations (especially the ERDF Business Survey and the ESF Leavers' Survey) for project evaluation wherever appropriate (ie, subject to relevance and to data protection and security requirements).**
- b **Encourage and assist sponsors of similar projects or activities to commission joint evaluations or to collaborate on methods and good practice where a single evaluation would not be appropriate. In particular, WEFO should seek a common approach to evaluating soft outcomes, employment effects and other key impact indicators for the main programme themes, and ensure that such information is collected on an ongoing basis to inform project and programme management.**

Part 1

# Wales and the European Union Structural Funds



1.1 EU Structural Funds help finance a range of measures to support job creation, competitiveness, economic growth, improved quality of life and sustainable development. Structural Funds form part of EU regional policy and support three main objectives: Convergence; Regional Competitiveness and Employment; and Territorial Cohesion (**Exhibit 3**). However, most of the Structural Funds budget for 2007-2013 is directed towards the Convergence objective of reducing economic disparities between EU regions.

1.2 This part of the report outlines the main features of EU Structural Funding for the 2007-2013 programming period (1 January 2007 to 31 December 2013) and how it applies to and works in Wales. The seven-year timeframe for Structural Funds programmes allows longer-term planning and budgeting than is commonly the case with domestic expenditure. Planning for 2007-2013 began around 18 months before the start of the period and expenditure will continue for up to two years after the end of the period, followed by a process of review and audit by the European Commission.

### Wales stands to benefit from around £1.9 billion of EU Structural Funding for the 2007-2013 period, mainly for West Wales and the Valleys

1.3 Structural Funding in Wales is distributed through two funds:

- a The *ERDF* accounts for 60 per cent of the available funding. The ERDF aims to correct imbalances between the economic prosperity of member states by:
  - Research, Development and Innovation (RD&I) – building business capacity to develop and take up improved and new products, processes and services;
  - funding infrastructure linked particularly to regeneration, telecommunications, environment, energy and transport; and
  - finance – repayable and non repayable grants to support jobs and growth.
- b The *ESF* accounts for 40 per cent of the funding. The ESF aims to promote employment in the EU by funding projects to:
  - help employers and employees adapt to changing economic demands through training schemes;
  - improve access to job opportunities, particularly for those, such as the long term unemployed, who are furthest from the labour market; and
  - encourage lifelong learning, innovation in the workplace and equal opportunities for all.

Exhibit 3 – EU regional policy objectives and the distribution of EU Structural Funds

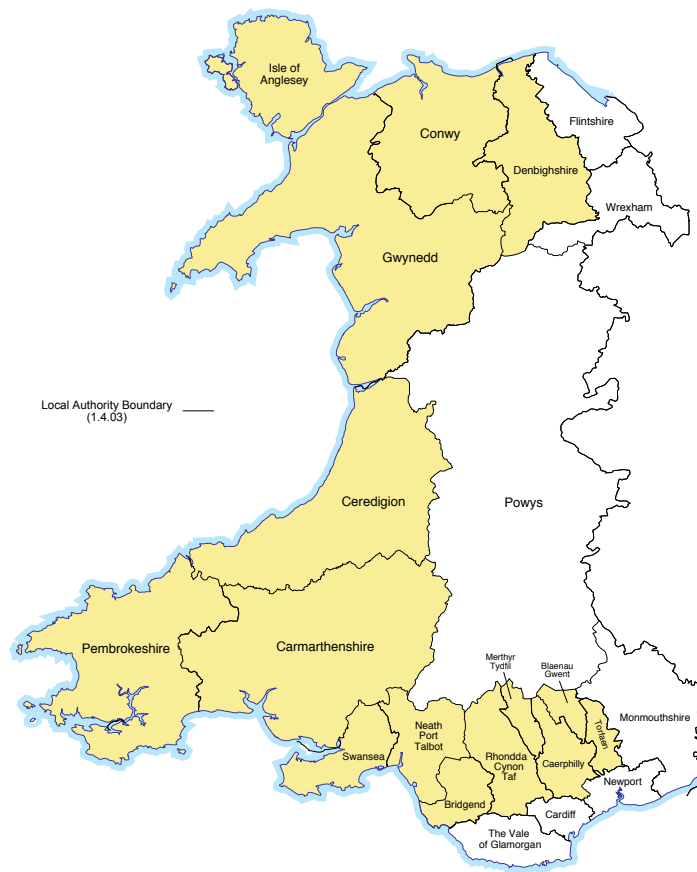
Policy objective	<ul style="list-style-type: none"> <li>• Regional coverage</li> <li>• Population coverage</li> <li>• Percentage of EU Structural Funds budget allocated to the objective</li> </ul>
<p><b>Convergence</b></p> <p>To reduce economic disparities between EU regions by enabling worse-off regions to catch up with better-off regions.</p> <p>Regions qualifying are those with a per capita GDP of less than 75 per cent of the EU average<sup>1</sup>.</p>	<ul style="list-style-type: none"> <li>• 99 regions</li> <li>• 170 million people</li> <li>• 81.5 per cent of budget</li> </ul>
<p><b>Regional Competitiveness and Employment</b></p> <p>To create jobs by promoting competitiveness and making the regions concerned attractive to businesses and investors.</p> <p>Applies to all regions not covered by Convergence. Intended to help better-off regions perform even better, create more balanced development, eliminate remaining pockets of poverty and to have a knock-on benefit on the rest of the EU.</p>	<ul style="list-style-type: none"> <li>• 170 regions</li> <li>• 330 million people</li> <li>• 16 per cent of budget.</li> </ul>
<p><b>Territorial Cohesion</b></p> <p>To encourage cooperation across borders – be it between countries or regions – that would not otherwise happen. Initiatives could include the shared management of natural resources, development of transport links and creating networks of universities and research institutes. These cross-border programmes potentially cover all regions.</p>	<ul style="list-style-type: none"> <li>• 269 regions</li> <li>• 500 million people</li> <li>• 1.5 per cent of budget</li> </ul>

Note:

<sup>1</sup> GDP – the value of goods and services produced – is measured in a way that adjusts for the effect of price differences between member states.

Source: EU website

## Exhibit 4 – The Convergence and Competitiveness areas for Structural Funding



1.4 Overall, Wales stands to benefit from some £1.87 billion of EU Structural Funding for the 2007-2013 programming period (as at 31 December 2013)<sup>6</sup>. There are two separate programmes (one for ERDF and one for ESF) for each of the following regions<sup>7</sup>:

a *West Wales and the Valleys* under the Convergence objective. The region covers 15 local authority areas, around 62 per cent of the land area of Wales and some 1.9 million people (Exhibit 4). The region will receive

around £1.76 billion of European funding for the 2007-2013 period – around 94 per cent of the total funding allocated to Wales.

b *East Wales* under the Regional Competitiveness and Employment objective. The region covers the better-off areas of Wales outside the Convergence region, with a population of just over one million, which will receive £115 million of European funding for the 2007-2013 period, around six per cent of the total available to Wales.

<sup>6</sup> The value of the programmes in sterling fluctuates depending on the £/€ exchange rate. The pound fell from €1.47 to €1.02 between the approval of the ERDF programmes in August 2007 and the end of 2008, increasing the potential value of the Structural Funds by around 44 per cent or £670 million. There followed a rise in the value of the pound to around €1.20 at the end of 2012, reversing just under half of the previous gains. Throughout this report, euro figures have been translated into sterling at a rate of 1.20, which WEFO used for planning and reporting purposes at 31 December 2013.

<sup>7</sup> Wales also takes part in, but is not the Managing Authority for, the Ireland-Wales cross-border programme, which encourages cooperation between the western areas of Wales and the south-eastern region of Ireland. The EU has allocated around £42 million to this programme for the 2007-2013 period, which is shared between the two countries. Wales may also bid for resources from the North-West Europe and Atlantic Coast programmes, which encourage transnational cooperation.

1.5 Each programme has a budget for EU funding alongside the required match funding from the public<sup>8</sup> and private sectors. Including this match funding, the 2007-2013 Structural Funds programme is worth around £3.20 billion to Wales. The ratio of EU funding to match funding varies by programme (Exhibit 5).

Exhibit 5 – Structural Funding allocations for Wales, 2007-2013, by Programme and Fund

	EU grant (£ million) <sup>1</sup>	Match funding (£ million)	Total funding (£ million)	Grant rate (per cent)
ERDF Convergence	1,053	786	1,839	57%
ESF Convergence	703	391	1,094	64%
<b>Convergence programmes</b>	<b>1,756</b>	<b>1,177</b>	<b>2,933</b>	<b>60%</b>
ERDF Competitiveness	62	75	137	45%
ESF Competitiveness	53	80	133	40%
<b>Competitiveness programmes</b>	<b>115</b>	<b>155</b>	<b>270</b>	<b>43%</b>
<b>Total for all programmes</b>	<b>1,871</b>	<b>1,332</b>	<b>3,203</b>	<b>58%</b>

Note:

<sup>1</sup> Financial allocations based on position at 31 December 2013 using an exchange rate of €1.20 to £1.

Source: WEFO

<sup>8</sup> Includes the voluntary sector.



**Structural Funds programmes are planned to help deliver EU-wide policies on jobs, growth and sustainable development**

- 1.6 Each programme is divided into priorities that relate to a particular social or economic objective, for example encouraging innovation or reducing economic inactivity. Each priority has its own budget (**Exhibit 6**), and priorities may be further divided into themes which have their own indicative (non-binding) financial allocations.
- 1.7 The European Commission agrees with the relevant authority in each member state operational programmes of work at the outset of the programming period<sup>9</sup>. In Wales, the relevant authority is the Welsh Government. Each operational programme:
  - a reviews the economic and social situation in, and the needs, strengths and weaknesses of, the programming area;
  - b proposes a strategy to address the area's needs in line with EU strategic guidelines and domestic (in this case Welsh Government) policy;
  - c sets out an integrated programme of activities to deliver the strategy, organised into priorities with specific budgets (see **Exhibit 6** for Wales), monitoring indicators and output targets;
  - d explains how the programme will promote the cross-cutting themes of environmental sustainability and equal opportunities; and
  - e describes the administrative arrangements that will apply for the duration of the programme.

<sup>9</sup> Approval of the operational programmes is the culmination of a process that takes around two years and includes the agreement by member states of the EU budget, publication of EU Structural Funds regulations, and European Commission acceptance of the UK Government's National Strategic Reference Framework, a document that sets out at a high level how allocated EU funds will be used and administered.

Exhibit 6 – Structural Funding allocations for Wales, 2007-2013, by Fund and priority

Priority name ( <i>number</i> )	Allocation (£ million) <sup>1</sup>		Examples of activities funded
	EU grant	Total	
<b>ERDF Programmes</b>			
Knowledge and innovation <i>Convergence Priority 1</i> <i>Competitiveness Priority 1</i>	291	531	Support for research and development with likely commercial benefits, ICT infrastructure and support for business innovation
Business growth and competitiveness <i>Convergence Priority 2</i> <i>Competitiveness Priority 2</i>	138	267	Support for entrepreneurship, business finance (including venture capital funds)
Strategic infrastructure <i>Convergence Priority 3</i>	327	588	Road and rail projects, community transport, sites and premises for business
Creating an attractive business environment <i>Convergence Priority 4</i> Tackling climate change <i>Competitiveness Priority 3</i>	204	350	Renewable energy, energy efficiency, flood defence, tourism initiatives based on local heritage and the natural environment
Sustainable communities <i>Convergence Priority 5</i> Regeneration for growth <i>Competitiveness Priority 4</i>	141	220	Physical regeneration, community economic development
<b>ESF Programmes</b>			
Supplying young people with skills for learning and future employment <i>Convergence Priority 1</i>	104	159	Initiatives to tackle under-achievement in schools and raise skills and aspirations, eg, through mentoring, volunteering, work experience, career guidance and awareness raising
Increasing employment and tackling economic inactivity <i>Convergence Priority 2</i> <i>Competitiveness Priority 1</i>	302	501	Personal job search support tailored to individual needs, work placements, incentives for employers to employ and retain jobless individuals
Improving skills levels and the adaptability of the workforce <i>Convergence Priority 3</i> <i>Competitiveness Priority 2</i>	308	494	Basic skills training, apprenticeships, training at all levels, initiatives to challenge gender segregation in the workforce
Modernising and improving the quality of our public services <i>Convergence Priority 4</i>	28	46	Encouragement of collaborative working between public bodies, projects to build capacity of public bodies to provide better quality public services

Exhibit 6 – Structural Funding allocations for Wales, 2007-2013, by Fund and priority (continued)

Priority name ( <i>number</i> )	Allocation (£ million) <sup>1</sup>		Examples of activities funded
	EU grant	Total	
<b>ERDF and ESF</b>			
Technical assistance ( <i>one Priority in each programme</i> )	28	47	Bespoke IT systems to manage EU funding, research and evaluation, training for project managers, expert advice, support for partnerships and networks
<b>Total</b>	<b>1,871</b>	<b>3,203</b>	

Note:

<sup>1</sup> Financial allocations based on position at 31 December 2013 using an exchange rate of €1.20 to £1. The Competitiveness programmes fund a more limited range of activity than Convergence.

Source: WEFO financial data and operational programmes

1.8 Once approved, operational programmes may be modified to reflect significant changes in policy or in the economic context, but only with the approval of the Programme Monitoring Committee and subsequently the European Commission. In the 2007-2013 funding round, the operational programmes are complemented by a series of strategic frameworks that provide additional guidance on priorities and project design. These frameworks are developed by the Welsh Government and do not require specific authorisation by the European Commission (Exhibit 7).

**Exhibit 7 – Strategic frameworks for the EU Structural Funds programmes in Wales**

There are 20 strategic frameworks that cover all areas of programme activity and apply to both the Convergence and Competitiveness programmes (Appendix 2). Each framework is linked to specific priorities and themes within the programmes. Fifteen are thematic frameworks, dealing with specific policy areas such as climate change or business finance. Five are spatial frameworks that cover regeneration activity in specific geographical areas (Swansea Bay, Pembrokeshire, South East Wales, Central Wales and North Wales) that reflect the areas delineated in the Wales Spatial Plan.

Each of the thematic frameworks also has a section dealing with the spatial context – the main challenges and opportunities facing each of the spatial framework areas and the locations and groups that should be targeted.

The frameworks have a common format and cover:

- an outline of the main strategies, policies and EU initiatives that are relevant to the framework;
- the types of activity that will be funded under the framework (known as fields of intervention), their purpose and expected approaches to delivery;
- monitoring indicators and financial allocations;
- key principles and regulations, with reference to relevant guidance; and
- framework evaluation and review, including evaluation questions to be used for project evaluation.

- 1.9 All programmes are expected to deliver against the 'Lisbon Agenda' for jobs and growth, agreed by all member states in 2000 and reinforced in 2005 by the EU Growth and Jobs Strategy. European Commission strategic guidelines for the Structural Funds outline how member states should contribute to the three main objectives of the strategy:
- a **Make Europe a more attractive place to invest and work** by investing in transport infrastructure, renewable energy and energy efficiency. To strengthen synergies between environmental protection and economic growth, the strategic guidelines urge member states to invest in environmental protection infrastructure, waste management and regeneration, and also to develop the economic benefits of natural and cultural assets.
  - b **Encourage knowledge and innovation for growth** by increasing and better targeting investment in research and development, facilitating innovation and promoting entrepreneurship, promoting the information society, and improving access to finance for small businesses.
  - c **Create more and better jobs** by attracting and retaining more people in the labour market, improving the adaptability of workers and enterprises, and increasing investment in human capital through better education and skills. The Structural Funds will also invest in the administrative capacity of public services.
- 1.10 The EU requires each Convergence operational programme to devote 67 per cent of funding to specified activities that contribute most to the Lisbon Agenda, rising to 75 per cent for Competitiveness programmes. This requirement limits the ability of member states to use Structural Funding to finance non-preferred activities, for example general business advice or inward investment incentives.
- 1.11 The EU 'Europe 2020' strategy re-stated the commitment to jobs and growth and introduced a stronger emphasis on sustainable development, economic recovery and fiscal consolidation. The Structural Funds are expected to contribute to the five key targets of the Europe 2020 strategy, which are that, by 2020:
- a 75 per cent of all 16-64 year olds will be in employment;
  - b the EU will invest three per cent of its GDP in research and innovation each year;
  - c to mitigate climate change, the EU will have cut greenhouse gas emissions by 20 per cent since 1990, increased energy efficiency by 20 per cent and will obtain 20 per cent of electricity from renewable sources;
  - d for education, school drop-out rates will be less than 10 per cent and 40 per cent of 30-34 year olds will have completed third level (higher) education; and
  - e the EU will have 20 million fewer people in or at risk of poverty and social exclusion.
- 1.12 Reflecting these EU objectives and targets, the Welsh Government led programmes for 2007-2013 focus more on innovation and infrastructure than was the case in the 2000-2006 programming round.

## The Structural Funds operate within a clearly defined framework of regulations and controls

- 1.13 The Structural Funds programmes are governed by EU regulations. These include specific regulations for each fund that determine eligible activities, expenditure, record-keeping and audit. General EU regulations on public procurement and state aid (government support for commercial enterprises) are also particularly important because projects funded by the programmes often involve the commissioning of services that have an international market or involve aid for particular enterprises. The programmes are subject to audit by several organisations including the European Court of Auditors, and irregularities may lead to the clawback of EU funding already paid to the member state.
- 1.14 The Structural Funds will only pay for activity that is genuinely 'additional' to that which would have been funded without EU support. The EU regulates additionality by agreeing with each member state a minimum level of domestic expenditure in the programming areas on the broad categories of expenditure (basic infrastructure, human resources and productive investment) that receive support from the Structural Funds. This level of expenditure must be maintained to demonstrate that the relevant authority has not used Structural Funds to replace public or equivalent structural expenditure.
- 1.15 The Structural Funds programmes are delivered through individual projects, of which there were 287 at 31 December 2013. Each project is led by one organisation, the 'project sponsor', which is accountable under contract (the Grant Offer Letter) to WEFO for managing and delivering the project in accordance with its business plan, relevant EU regulations, the Welsh National Eligibility Rules and the terms of the Grant Offer Letter. The project sponsor may be assisted by other 'joint sponsor' organisations. Most project sponsors are public sector organisations, often the Welsh Government itself. Ultimately the programmes' progress depends on the speed with which sponsors are able to plan and deliver their projects, but this in turn depends in large part on the support provided by WEFO.
- 1.16 The main bodies involved in the management of the Structural Funds for a particular region are:
- a The **European Commission** administers the Structural Funds for the EU and is responsible for:
    - allocating the overall Structural Funds budget between member states and programmes;
    - developing strategic guidelines for the use of the Funds;
    - approving operational programmes;
    - monitoring the progress of the programmes by reviewing annual reports and acting as observers at meetings of the Programme Monitoring Committee (see below);
    - authorising projects which exceed €50 million in EU grant; and
    - verifying compliance with regulations.
  - b The **Managing Authority** is accountable to the European Commission for delivering its programmes efficiently in accordance with the regulations governing the use of the Structural Funds. The Welsh Ministers act as the Managing Authority for the Welsh programmes, and responsibility is delegated to WEFO, a division of the Welsh Government. The Managing Authority is responsible for:

- selecting projects for funding in accordance with selection criteria and EU regulations;
  - ensuring that the programme as a whole makes good progress and is delivered in line with the operational programme;
  - paying EU grant to project sponsors based on claims for eligible expenditure and preparing requests for reimbursement from the European Commission;
  - undertaking verification checks on a sample basis to ensure that claims are valid and the underlying transactions are adequately documented;
  - monitoring and evaluating the programmes in line with an agreed plan;
  - communicating essential information to project sponsors and publicising the programmes more widely; and
  - preparing the annual implementation reports, annual control reports and the final reports required by the European Commission under EU regulations.
- c The **Certifying Authority** is responsible for checking claims for European funding from the Managing Authority, ensuring they are correctly stated and adequately supported, and submitting the claim to the European Commission. In Wales, WEFO acts as Certifying Authority, but the part of WEFO undertaking this task is functionally separate from the rest of the organisation to avoid a potential conflict of interest.
- d The **Audit Authority** is responsible for independently auditing the management and control systems for the Structural Funds, and auditing a sample of projects to ensure that expenditure claimed is correct and complies with the relevant regulations. The Audit Authority reports annually to the European Commission on the results of its work. It submits a closure declaration at the end of the programmes, assessing the validity of the Certifying Authority's application for the final payment to be released by the European Commission. The European Funds Audit Team is part of the Welsh Government's corporate governance team and acts as Audit Authority for the Welsh programmes.
- e The **Programme Monitoring Committee** is responsible for monitoring the effectiveness and quality of each programme. The Welsh Government has established a single committee to oversee all four of its programmes, comprising 14 representatives from the main stakeholder groups (including central government, local government and private business) and 10 appointed experts. The committee:
- agrees the strategic frameworks are fit for purpose as part of the criteria used to select operations;
  - examines and approves any proposals by the Managing Authority to amend the operational programmes which is then subject to the agreement of the European Commission ([paragraph 1.8](#));
  - monitors progress in delivering the programmes, in particular against the programmes' financial and output targets; and
  - considers and approves the annual and final reports required by the European Commission.



## Part 2

The programmes have progressed relatively well overall despite certain difficulties, but it is too early to fully assess their overall impact





- 2.1 This part of the report considers the overall progress of the programmes, with particular regard to:
- a the allocation of funds to projects, known as programme commitment;
  - b levels of spending once funds have been committed, both at a programme level against the European Commission's spending targets<sup>10</sup> and at a project level against project delivery profiles; and
  - c the performance of the programmes in delivering their intended outputs and outcomes.

## Overall, WEFO has made good progress in committing available funds to projects

WEFO has achieved most of the annual commitment targets it set itself, with most programme areas now fully committed

- 2.2 WEFO could not commit any of the funds due to Wales until the European Commission approved the operational programme for each of the Convergence and Competitiveness programmes. That approval is the culmination of a process that is largely outside WEFO control. However, to ensure a smooth transition from one programme to the next, it is important to gain momentum from the earliest stage in the new programming period.

- 2.3 WEFO agreed its ERDF operational programmes with the European Commission in August 2007, eight months after the start of the programming period but earlier than many other operational programmes across the EU. The ESF programmes were approved in October 2007, in line with many others. WEFO had already established a Programme Monitoring Committee in May 2007 and started developing project selection criteria and guidance for applicants from the first half of 2007. This meant that key requirements for project development were in place by December 2007, including: agreed project selection and prioritisation criteria; guidance for applicants; a monitoring and evaluation plan; and the supporting Welsh Government strategic framework documents.

- 2.4 By March 2008, WEFO had already received 160 expressions of interest from project sponsors, of which 50 had progressed for more detailed assessment. European Commission officials responsible for overseeing the Welsh programmes told us that they were content with the speed with which the programmes were launched. Our survey of project sponsors indicated that progress was much slower than many sponsors expected, but WEFO believes this may be associated with expectations about the standards expected of project proposals.

<sup>10</sup> The achievement of commitment and spending targets has been made more challenging by changes in the sterling/euro exchange rate that, overall, have increased the value of the programmes.

2.5 Targets set in the Operational Programmes assume a roughly equal commitment of EU funding in each year of the programmes. This commitment profile is an important early indicator of programme activity and is used to calculate the N+2 spending targets (paragraph 2.10), which the European Commission uses for control purposes. However, WEFO set its own commitment targets for each year between 2008 and 2012 (Exhibit 8). For 2009 onwards, these targets were more demanding than those set by the European Commission to help increase momentum and

minimise the risk of missing EU spending targets. In this regard, WEFO was learning the lesson from the 2000-2006 programmes, which experienced significant project slippage. Higher commitment targets were also part of a strategy to tackle the impact of the economic downturn, which included negotiating higher grant rates with the European Commission to make domestic match funding go further. In our view, this strategy – to bring forward commitment and maximise expenditure – was appropriate and helped WEFO exceed the formal European Commission targets.

Exhibit 8 – Cumulative commitment of EU funding compared with European Commission and WEFO targets, 2007-2013<sup>1</sup>

	2007	2008	2009	2010	2011	2012	2013
<b>Commitment targets<sup>2</sup></b>							
European Commission operational programme target	13%	27%	41%	55%	70%	85%	100%
WEFO internal target	n/a <sup>3</sup>	20%	50%	75%	80%	100%	100%
<b>Actual programme commitment</b>							
ERDF Convergence	0%	22%	42%	74%	79%	103%	101%
ERDF Competitiveness	0%	28%	53%	61%	70%	103%	111%
ESF Convergence	0%	35%	66%	86%	90%	94%	101%
ESF Competitiveness	0%	28%	62%	100%	97% <sup>4</sup>	101%	108%

Notes:

- 1 Figures are as at 31 December for each year and are based on the cumulative commitment over all previous years of the programming period, as a percentage of the total EU funding allocation at each year-end.
- 2 The European Commission and WEFO targets apply to each programme on an individual rather than aggregated basis.
- 3 WEFO did not set a target for 2007 because the operational programmes were not approved by the European Commission until August and October of that year and WEFO was not able to approve any projects until after programme approval.
- 4 A reduction in the proportion of programme funding that is committed can occur because funding is de-committed from projects.

Source: WEFO

2.6 WEFO was ahead of the Operational Programmes' profiles for programme commitment by the end of 2009 and has maintained this position since then. WEFO comfortably met its own ESF commitment targets for each year between 2008 and 2011 but fell short of its own more demanding ERDF targets<sup>11</sup>. The shortfall for the ERDF Competitiveness Programme in 2011 was due to the priority area with the highest budget, knowledge and innovation, having committed only 44 per cent of the £27.5 million funding available.

2.7 Overall, the increase in commitment between 2010 and 2011 was much smaller than in previous years. This was partly because many areas were fully or almost fully committed and because funding was de-committed (withdrawn) from some projects. Notably, the Welsh Government undertook a major review of its economic development policy in 2010 which resulted in some projects being removed or scaled back to better fit the requirements of the new policy. This resulted in the de commitment of around £50 million in 2010 from the ERDF Convergence Programme<sup>12</sup>. However, in March 2011, WEFO decided to close several areas of the ERDF programmes to new applications, primarily due to high levels of actual and potential commitment.

2.8 Commitment rates for the 2007-2013 programmes have exceeded those for the 2000-2006 programmes in all equivalent years of the programming period, especially in the third and fourth years<sup>13</sup>. At the end of 2013, commitment rates exceeded 100 per cent for all of the four programmes and nine of the 19 priorities had been fully committed. The priorities that were not fully committed accounted for only 2.8 per

cent of the total EU funding allocation for the ERDF programmes and 2.0 per cent for the ESF programmes. WEFO plans to over-commit the ERDF programmes by five per cent and the ESF programmes by 10 per cent to help ensure that the full amount of EU funding is drawn down even if projects under-spend or the pound weakens against the euro, releasing more EU funding at a late stage.

### Working with other Welsh Government departments, WEFO has responded appropriately to address shortfalls in commitment

2.9 WEFO has monitored the amounts committed to different policy areas and progress has been discussed regularly with Ministers responsible for the relevant Welsh Government departments. While progress had been slow in some areas initially, WEFO and other Welsh Government departments have taken appropriate action to stimulate project development or to re-allocate funding. For example:

- a *Modernising and improving the quality of public services*: At September 2010, only 25 per cent of the £27.5 million ESF Convergence Programme funding available for this purpose had been committed. WEFO officials told us that they expected early progress to be slow because this priority was innovative and the Welsh Government wanted to maximise strategic impact rather than there being a proliferation of small-scale, localised projects. WEFO attributed delays to the varying pace of the partners whose collaboration was needed to develop project proposals and the revision of the strategic framework to reflect evolving Welsh

<sup>11</sup> WEFO would have met all of its own ERDF commitment targets between 2008 and 2010 had the exchange rate remained at the 1.48 euros to the pound level as at August 2007 (when the operational programmes were approved by the European Commission).

<sup>12</sup> There have been other, more modest, de-commitments from projects to reflect under-performance, efficiency savings, ineligible expenditure and, in some cases, a shortage of match funding. WEFO has since recycled the released money into other projects but there was a temporary impact on commitment levels.

<sup>13</sup> The difference between the rate of commitment for 2000-2006 and 2007-2013 reflects, to some extent, the different nature of the two programming rounds. For 2000-2006, individual projects tended to be of lower value and shorter in duration. For 2007-2013 most projects are at least three years in duration with many lasting six years and involving significant sub-contracting of service delivery.

Government policy. WEFO worked with other Welsh Government departments and Public Services Management Wales to develop project proposals and the Welsh Government created a specific pot of match funding worth up to £1 million. By 31 December 2013 around 76 per cent of the available funds had been committed. However, WEFO considered it unlikely that enough projects of sufficient quality would come through to fully commit the remaining funding and, therefore, re-allocated £4.5 million to other programme areas.

- b *Climate change*: Around £141 million of EU funding has been allocated in the ERDF programmes to mitigate the impact of climate change through flood defences, energy conservation, renewable energy and waste management projects. There was slow progress initially because of the complexity of some projects and because anticipated private sector led projects did not materialise as the economic downturn made it hard to raise funding. In March 2011, following a change in EU regulations, WEFO was able to approve ERDF funding of £33 million towards the Welsh Government's Arbed project to promote energy efficiency and micro-generation in existing housing. WEFO has also now approved grants of £50 million to flood defence projects. As a result, 74 per cent of the indicative allocation had been earmarked by December 2013, albeit with a lesser emphasis on renewable energy than that originally envisaged. The Welsh Government has established a central fund, Ynni'r Fro, to help bring forward more local small-scale energy generation projects by providing grant or loan finance.
- c *ICT infrastructure and exploitation*: the ERDF programmes include around £101 million for this theme, of which only 54 per cent had been committed by May 2011. The Welsh Government is now implementing a major project – Next Generation Broadband Wales – to extend high-speed broadband services to all areas of Wales by 2020. The project will cost a total of £203 million of which £89.5 million will be provided by ERDF, making it the biggest EU-funded project. The development of the project has been time-consuming because of its size and complexity, the need for in-depth research to demonstrate market failure, and the requirement to obtain specific approval as a major project from the European Commission. The project has now been approved and will use all available funds in the relevant priorities of the ERDF programmes.

## The programmes have met EU spending targets, despite the rate of expenditure overall being slower than forecast by project sponsors

WEFO has met all EU spending targets, ensuring no loss of funding to Wales

2.10 The European Commission has set annual spending (N+2) targets for each of the operational programmes in Wales. Each programme must spend its agreed annual budget allocation within two years of the end of the year for which it was allocated<sup>14</sup>. If a programme falls short of its spending target, the unspent balance is de-committed and will not normally be re-committed, meaning a permanent loss of funding.

2.11 Based on this two-year rule, the first spending targets should have related to the position at 31 December 2009. In 2010, to help managing authorities manage the adverse impact of the economic downturn on match funding, the European Commission decided to abolish the 2009 spending target and revised the targets for 2010-2015. The revised targets were significantly less demanding in 2010 and 2011. However, WEFO decided that it would still seek to meet the original targets and has mostly done so.

2.12 Like other UK managing authorities, WEFO met both the original and the revised spending targets for all four of its programmes in 2009, 2010 and 2011, mostly by a substantial margin (Exhibit 9). WEFO met all four of the revised targets in 2012 and 2013 but fell slightly short of the two original ERDF programme targets, and performance generally was closer to target as the targets became progressively more demanding.

Exhibit 9 – Expenditure of EU funds compared with European Commission targets, 2009-2013

Programme and year	Actual expenditure (£ million) <sup>1</sup>	Actual expenditure as a percentage of original target	Actual expenditure as a percentage of revised target <sup>2</sup>
<b>2009</b>			
ERDF Convergence	74.5	110%	N/A
ERDF Competitiveness	15.8	403%	N/A
ESF Convergence	68.9	153%	N/A
ESF Competitiveness	5.3	154%	N/A

<sup>14</sup> Spending target performance is based on claims for reimbursement made by WEFO to the European Commission. WEFO needs to have received and paid a valid project grant claim before it can include the related expenditure in its claim to the Commission. As a result, there can be a time lag of up to six months between expenditure happening 'on the ground' and the WEFO claim.

Exhibit 9 – Expenditure of EU funds compared with European Commission targets, 2009-2013 (cont)

Programme and year	Actual expenditure (£ million) <sup>1</sup>	Actual expenditure as a percentage of original target	Actual expenditure as a percentage of revised target <sup>2</sup>
<b>2010</b>			
ERDF Convergence	206.7	101%	275%
ERDF Competitiveness	21.6	182%	393%
ESF Convergence	165.9	121%	260%
ESF Competitiveness	11.7	112%	239%
<b>2011</b>			
ERDF Convergence	337.7	106%	152%
ERDF Competitiveness	33.6	161%	220%
ESF Convergence	276.9	115%	157%
ESF Competitiveness	23.9	130%	178%
<b>2012</b>			
ERDF Convergence	483.6	97%	110%
ERDF Competitiveness	27.4	95%	104%
ESF Convergence	342.1	103%	115%
ESF Competitiveness	29.7	117%	131%
<b>2013</b>			
ERDF Convergence	637.2	97%	101%
ERDF Competitiveness	37.6	96%	103%
ESF Convergence	466.0	103%	110%
ESF Competitiveness	38.1	110%	118%

Notes:

<sup>1</sup> Figures are as at 31 December for each year and are based on the cumulative expenditure over all previous years of the programming period that is certified by WEFO as being eligible for reimbursement by the EU.

<sup>2</sup> N/A = Not Applicable. In 2010 the European Commission decided to abolish the 2009 spending target and revised all future targets.

Source: WEFO



2.13 Three factors have helped boost WEFO spending of EU Structural Funds:

- a The substantial increase in the average intervention rate at Priority level – the proportion of the total cost that is met by EU funding rather than match funding – that WEFO negotiated with the European Commission, from an average of 49.0 per cent to an average of 59.3 per cent for the four programmes. This change released an additional £187 million of EU funding by 31 December 2013.
- b Some retrospective funding of projects which were wholly or partially complete before they were approved by WEFO. There have been three wholly retrospective transport infrastructure projects under the ERDF Convergence Programme. These projects claimed a total of £12.1 million of retrospective grant. There have also been 10 other projects for which retrospective funding totalled more than £1 million or 25 per cent of the total grant.
- c Wales was one of the first EU regions to establish the JEREMIE and JESSICA financial instruments. These are investment funds that follow the same pattern across the EU and are intended to finance small businesses and urban development ventures on a commercial basis, generating returns that fund further investments. The European Commission pays all of the grant for these funds when the funds are first established (2009 for JEREMIE and 2010 for JESSICA), which boosted grant drawn down on the two ERDF programmes by £73.2 million.<sup>15</sup>

**Project spending has been slower than forecast for a variety of reasons including general over-optimism, difficulties with procurement and staff recruitment and the impact of the economic downturn**

- 2.14 Each project sponsor agrees with WEFO a delivery profile that sets out how much the project expects to spend and what outputs it expects to deliver in each three-month period of its lifetime. The agreed delivery profile and baselined business plan is cross referenced in the offer of grant which is signed by the sponsor. Since June 2010, WEFO has produced monthly reports comparing forecast spend against actual spend for each project. Until November 2013, WEFO considered that any project within 15 per cent of its profiled spend was proceeding broadly to plan, although this threshold has since been reset at five per cent as the programmes draw to a close.
- 2.15 There has been a consistent pattern of projects under-spending against their delivery profile. As at December 2013, around one in three projects in progress were still 20 per cent or more behind their expenditure profile ([Exhibit 10](#)). While the overall shortfall between actual and forecast spending fell from 31 per cent in June 2010 to 19 per cent in December 2013, much of that improvement is due to project sponsors updating their delivery profiles to reflect major slippage, rather than catching-up with their original profiles. Many projects have stuck more closely to their expenditure profile once they have resolved difficulties in the start-up phase. Generally, WEFO permits sponsors one major re-evaluation.

<sup>15</sup> The JESSICA project was cancelled in December 2013 and the £25 million of grant it received was withdrawn from the ERDF programmes at that time, affecting performance against the 2013 N+2 target. However, the money still counted against previous N+2 targets.

2.16 The overall 19 per cent shortfall at December 2013 represented potential project expenditure worth £411 million, of which about £212 million was EU funding. At that point, the programmes had paid out to sponsors around £1.09 billion (58 per cent of the total EU funding allocation) compared with £1.55 billion (69 per cent) at the same stage of the equivalent 2000-2006 programmes.<sup>16</sup>

2.17 The level of project spending against profile is consistent with the pattern in the previous programmes. The level of expenditure forecast by project sponsors is well above the minimum levels required to meet EU spending targets. Based on project forecasts, WEFO estimates that it will meet all the 2014 spending targets, by a comfortable margin for three of the four programmes, and has classified programme expenditure as 'green' in its reports to the

Programme Monitoring Committee. Nevertheless, any under-spending against profile implies that benefits flowing from projects will not feed through to the Welsh economy as quickly as expected. WEFO officials have asked all partners involved in the delivery of projects to focus on timely provision of services to help achieve delivery of the programmes as planned.

2.18 As at 31 December 2013, the level of slippage tended to be higher for capital projects, which typically carry a higher element of financial risk, and for some innovative projects such as those for modernising public services. However, ERDF projects designed to encourage innovation and ESF projects aimed at preparing young people for the labour market have improved their performance overall as the programmes draw to a close. Slippage has been relatively low throughout the programming period for more established

Exhibit 10 – Actual project expenditure compared with profiled expenditure, June 2010 and December 2013<sup>1</sup>

	December 2013
Overall expenditure shortfall against profile ( <i>all projects in progress</i> )	19%
Breakdown of project performance ( <i>percentage of projects in each banding</i> ):	
Red: Project is 20% or more behind its expenditure profile	36%
Amber: Project is 6–19% behind or more than 5% ahead of its expenditure profile <sup>2</sup>	34%
Green: Project is within 5% (ahead or behind) of its expenditure profile	30%

Notes:

1 The analysis in this table is based on actual project expenditure compared with profiled expenditure at 31 December 2013. The analysis includes all projects that were not financially completed at the relevant dates; it therefore excludes investment funds, new projects that had not yet claimed any grant, and completed projects.

2 Twenty of 241 projects were over-profile at 31 December 2013, of which eight were over profile by more than five per cent.

Source: Wales Audit Office analysis of WEFO payment statistics

16 Equivalent programmes defined as Objective 1 ERDF, Objective 1 ESF, Objective 2 (excluding transitional funding) and Objective 3. These programmes are broadly comparable with the ERDF Convergence, ESF Convergence, ERDF Competitiveness and ESF Competitiveness programmes respectively. The amount paid out to project sponsors will not reconcile to the amounts claimed from the European Commission over the same period due to timing differences, and because intervention rates for approved projects may be different from the standard intervention rates used by the European Commission when paying Structural Funds to member states.

areas of the programmes such as measures aimed at reducing economic inactivity and for Welsh Government programmes that continued from the previous programming rounds, such as Modern Apprenticeships and Business Start-up Support.

- 2.19 The reasons for slippage were not always clear from the files for the sample of 36 projects we reviewed. However, common themes included:
- a *Procurement difficulties*: Some project sponsors struggled to adapt to new competitive procurement requirements that WEFO introduced for the 2007 2013 programmes and under-estimated the time needed to establish the necessary procedures. Procurement was cited as a source of delay for nine of the 36 projects that we examined and these issues had a significant impact on some major projects during 2009 and 2010. The main problems seem now to have been overcome after WEFO reviewed its approach and modified its guidance on delivery models.
  - b *Staff recruitment difficulties*: Thirteen of the 36 projects that we examined identified staffing difficulties, particularly recruitment, as a reason for delays. In many cases, it appeared that projects simply under-estimated the time needed to recruit for key posts and to fully staff new or large projects. In other cases, sponsors had specific problems finding candidates with the right skills and experience. For the Welsh Government, staff turnover arising from restructuring and from voluntary severance, has made it difficult to maintain continuity and has led to gaps in project teams.

2.20 Other, less commonly cited issues were:

- a *Lower than expected demand for project services*: arising, for example, from the impact of the economic downturn on demand for business advice and policy changes leading to changes in the market for renewable energy.
  - b *Availability of match funding*: a few projects reported that a shortfall in match funding for joint sponsors or grant applicants had hindered the progress of one or more elements of their project.
  - c *Delays in project approval*: which caused a few education sector projects to miss the start of the academic year. Some delivery agents proceeded at their own risk while awaiting project approval, but others started their activities a year later than originally planned.
- 2.21 Overall, and as in the previous programmes, there also appears to have been an inherent over-optimism in sponsors' delivery profiles. Project delivery profiles do not set out the assumptions made at the outset about milestone dates for key tasks such as recruiting staff and issuing contract notices. In the absence of such information, it is difficult for WEFO staff to assess the realism of business plans and we found no evidence that they had challenged expenditure profiles even where subsequent progress indicated that they were unrealistic. WEFO intends to introduce a 'mobilisation phase' for the 2014-2020 programmes, whereby projects will have a specific period to establish their delivery mechanisms before delivery 'on the ground' is expected to occur. If planned realistically, the mobilisation phase should help to reduce optimism bias in delivery profiles.

**The programmes are on track to meet, and in some cases far exceed, most of their key performance targets but are likely to fall short of most of their environmental sustainability and equal opportunities targets**

**WEFO focuses on between eight and 14 key performance indicators to monitor the delivery of each of the operational programmes**

- 2.22 In 2007, WEFO agreed with the European Commission a series of monitoring indicators for each of the four operational programmes. These indicators reflect the main strategic objectives of the EU and those of the Welsh Government. The monitoring indicators fall into two categories:
- a *output indicators* reflect the activities undertaken by a project, such as the number of enterprises assisted or the number of participants in a training programme; and
  - b *results indicators* are the immediate effects of a project and reflect its key aims, for example job creation or the achievement of specific qualifications.
- 2.23 WEFO uses other indicators to measure the wider overall impact of the programmes. Impacts usually occur over the long term, are more difficult to measure than outputs and results, and are assessed through evaluation at a programme rather than project level.
- 2.24 There are over a hundred monitoring indicators altogether, covering the four operational programmes and their respective priorities. However, WEFO focuses on between eight and 14 key output and results indicators to monitor the delivery of each operational programme. Of these, six key 'dashboard indicators' – jobs created, enterprises assisted, enterprises

created, participants assisted, participants gaining qualifications and participants entering employment – form the basis of WEFO's performance reporting as part of the Welsh Government's wider performance management arrangements. The two ERDF programmes share several of the same key indicators, likewise the two ESF programmes.

- 2.25 Most of the programme and priority level indicators have targets. The targets were set at the start of the programming period based on economic conditions and assumptions at that time about the scale and shape of the programmes (although some targets have since been changed, as has the definition of certain indicators). WEFO provides regular progress reports to the Programme Monitoring Committee, based on returns from project sponsors. **Appendices 3 and 4** describe the overall performance of each of the four operational programmes as at 31 December 2013 and as forecast at that point for the end of the programmes.

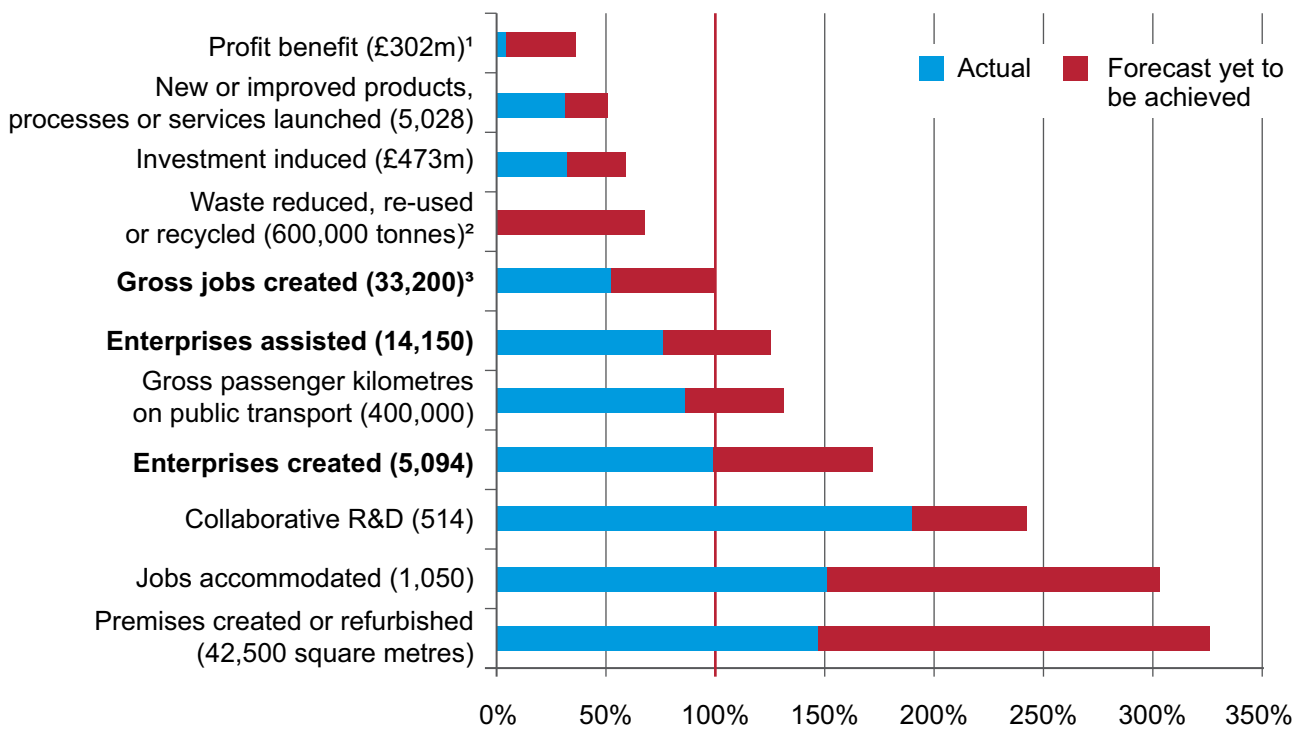
**WEFO expects to meet most key ERDF targets, thanks in part to the increase in the programmes' value because of changes in the exchange rate which have helped to offset the impact of the economic downturn**

- 2.26 The position reported by project sponsors as at the end of 2013 – covering both actual performance to that point and forecast outcome – indicates that WEFO would meet six of its 11 programme level targets for the ERDF Convergence Programme and five of the eight programme level targets for the ERDF Competitiveness Programme (**Exhibit 11**). Several of these targets have already exceeded, or are forecast to exceed, targets by large margins. For example, the Competitiveness Programme has already reported five times as many enterprises created as targeted.

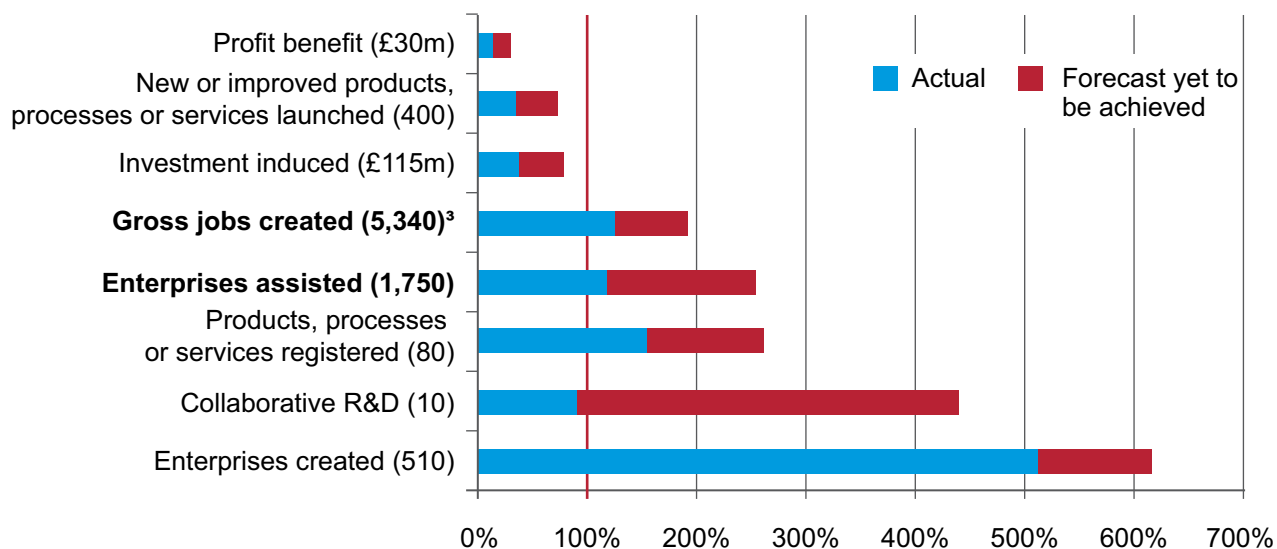
### Exhibit 11 – Actual and forecast performance against ERDF Programme targets at 31 December 2013

The graph shows forecast performance to the end of the programming period for each indicator as a proportion of target. Blue shows actual performance. Red indicates the balance of the forecast that was yet to be achieved at 31 December 2013. The 100% mark indicates the target; dashboard indicators (paragraph 2.24) are shown in bold. The target measure is shown in brackets next to each indicator. Figures are based on project sponsors' returns received by WEFO as at 31 December 2013.

#### Convergence Programme



## Competitiveness Programme



Notes:

- 1 'Profit benefit' is the amount of increased profit enterprises make from savings or productivity benefits, which have resulted from Structural Fund assistance or financial support.
- 2 The target for waste reduced, re-used or recycled has been reduced from one million tonnes to 600,000 tonnes.
- 3 'Gross jobs created' is the number of jobs achieved through ERDF support. Both new and associated jobs (such as construction jobs for capital projects) are included but project administration jobs are excluded. WEFO has updated the definition of 'gross jobs created' to include fixed term appointments of more than one year. WEFO believes that the revised indicator better reflects the current labour market and this has led to a considerable increase in the number of jobs reported to have been created. The targets for job creation remain unchanged.

Source: WEFO

- 2.27 The end of 2013 forecasts indicate that all but one of the ERDF related dashboard indicator targets would be met. However, the achievement of the job creation target for the ERDF Convergence Programme is likely to be particularly challenging, despite a change in measurement which has increased the number of jobs reported. At the end of 2013, the ERDF Convergence Programme had assisted around 10,700 enterprises and helped to create around 5,000 new enterprises and 17,000 new jobs for £1.18 billion of total programme expenditure (including match funding). The ERDF Competitiveness Programme had assisted 2,000 enterprises and helped to create about 2,600 new enterprises and 6,600 jobs for £117 million of total programme expenditure.
- 2.28 The six indicators that would fall significantly short of targets, based on the end of 2013 forecasts, relate to the following four themes:
- a *Investment induced*: project forecasts indicate that the ERDF Convergence Programme will deliver £277 million of private investment (58 per cent of the £473 million target). The economic downturn has made it more difficult to raise private finance than expected. WEFO does not intend to change this target. The Competitiveness Programme is expected to exceed its lower target for investment induced.
  - b *New or improved products, processes or services launched*: WEFO has received feedback that, due to the economic downturn, firms were spending longer in the development phase until they become confident that their new product, process or service would be a commercial success. Despite some improvement since the end of 2011, project forecasts indicate that the Convergence Programme will fall about 50 per cent short of its target. However, research and development activity appears to be progressing well, based on performance against the target for new products, processes, and services registered with the UK Intellectual Property Office<sup>17</sup>.
  - c *Waste reduced, re-used or recycled*: there has been a lack of demand for waste reduction projects as much of the large scale waste minimisation infrastructure was put in place under the previous 2000-2006 Objective 1 Programme. The change in emphasis in the current programmes from recycling to waste reduction in small and medium size enterprises has affected performance. While the European Commission has already agreed to reduce the Convergence Programme target from 1 million to 600,000 tonnes, project forecasts indicate that only 68 per cent of this 600,000 tonnes target will be delivered.
  - d *Profit benefit*: project sponsors are forecasting that they will achieve only 36 per cent of the Convergence Programme target and 29 per cent of the Competitiveness Programme target. The target is intended to capture increases in profits arising from savings or productivity benefits achieved with EU support. WEFO believes that the economic downturn has had an impact, but there is also a major measurement issue, with beneficiaries finding it difficult to attribute and calculate profits to specific EU-funded services. WEFO intends to leave the targets unchanged and to explore this issue through evaluation. WEFO has not prescribed any particular method for calculating profit benefit.

<sup>17</sup> Registrations precede product launches, as the intellectual property created needs to be developed into a commercial proposition before a product can be launched.



- 2.29 The value of total funds committed at 31 December 2013, including match funding, is 12 per cent higher than the original programme allocations for the ERDF Convergence Programme and 38 per cent higher for the Competitiveness Programme. The increase in the programmes' value has made it easier to achieve the programme level targets, offsetting some of the negative effects of the wider economic downturn. Had WEFO increased its programme targets in line with commitment levels then, based on project sponsors' forecasts at 31 December 2013, the ERDF Convergence Programme would still meet six of its 11 targets, but would only achieve 85 per cent of expected job creation. The ERDF Competitiveness Programme would fall short of four of its eight targets including gross jobs created.
- 2.30 At 31 December 2013, the actual performance at that time was behind forecast for 10 of the 19 ERDF programme indicators. Delays in project delivery and resultant under-spending are likely to be a factor and there can also be a significant time lag in the collation of performance information from sponsors and their contractors compared with evidence of project expenditure. Nevertheless, the ERDF programmes would meet the same programme level targets if the same level of slippage continued until the end of the programmes.
- 2.31 Sitting below the programme level indicators, there is mixed performance at a priority level, again due in part to the particular impact on certain priority areas of changes in economic conditions, policy changes (including State Aid rules) and differences in the distribution of funding compared with initial assumptions. For example, transport funding has been focused on road schemes rather than rail schemes to a greater extent than expected, meaning that rail targets are unlikely to be met.
- 2.32 Following a review in 2010, WEFO revised some of its priority-level targets. Only three of the targets were reduced while 23 targets were increased, some by a substantial proportion. WEFO also introduced three new targets to cater for new tourist destination marketing activity. Overall, based on project sponsors' forecasts at 31 December 2013, 72 of the 125 priority-level targets would be met.
- The ESF programmes have performed strongly and are forecast to exceed their key performance targets, many by a substantial margin**
- 2.33 The ESF programmes depend substantially on large and relatively well-established national schemes and have not suffered from the difficulties with state aid, capital projects and policy changes that have affected parts of the ERDF programmes. As a result, the ESF programmes have progressed more smoothly. In addition, the economic downturn has also created more demand for the training and employment support services that comprise the bulk of ESF programme expenditure and the increasing value of the programmes has again made it easier to achieve programme targets.
- 2.34 At the end of 2013, the ESF Convergence Programme had supported 423,430 participants in training and employment support programmes for total programme expenditure (including match funding) of £779 million. The ESF Competitiveness Programme had helped 64,112 participants for total expenditure of around £98 million.<sup>18</sup>

<sup>18</sup> Expenditure claimed by projects, not expenditure claimed by WEFO from the European Commission.

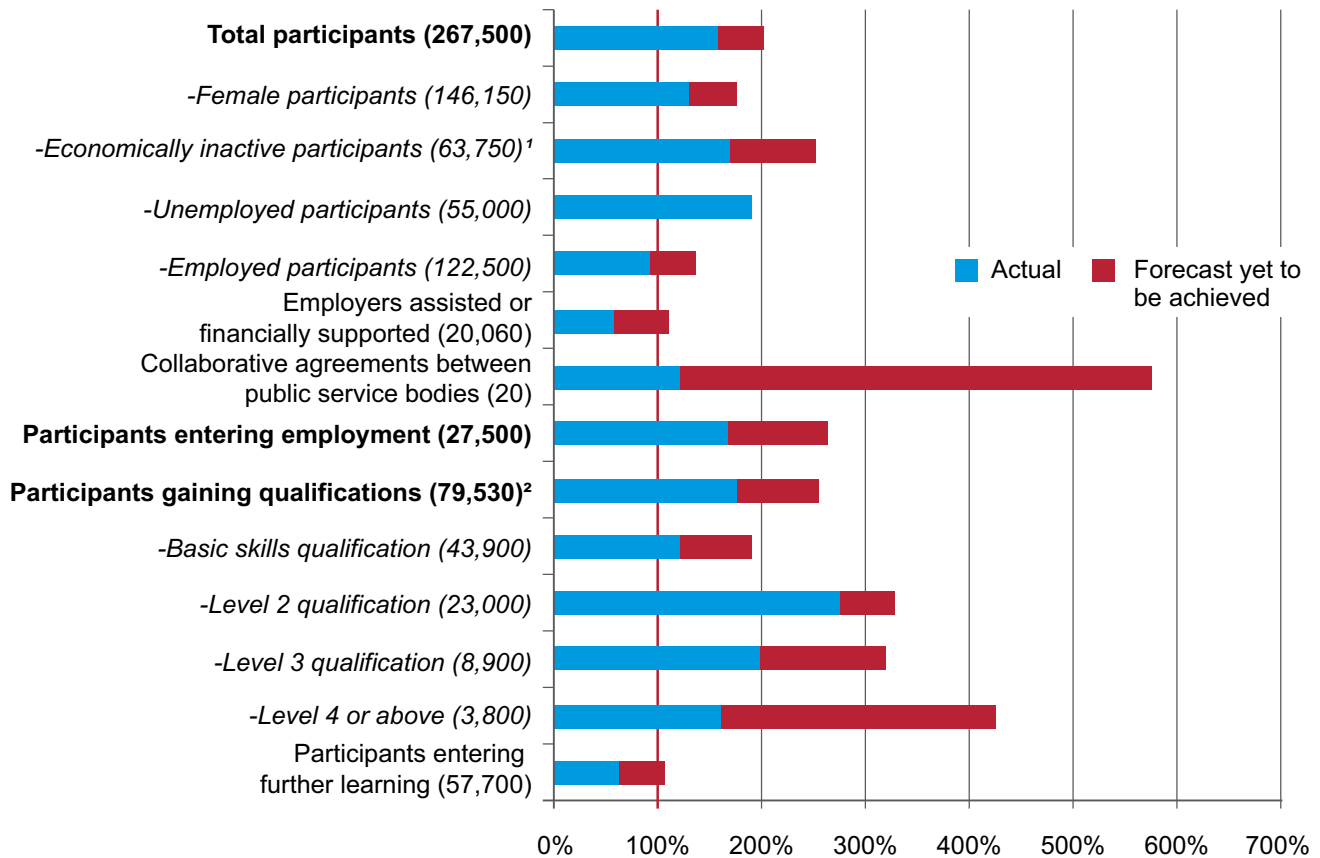
2.35 Project sponsor forecasts at 31 December 2013 indicate that all 27 of the original ESF Programme level targets will be met, many by a substantial margin (**Exhibit 12**). Twenty-two of the 27 targets are already reported to have been met and, overall, around twice as many participants as originally expected are likely to participate in the

programmes. The Competitiveness Programme is performing particularly strongly, and is also forecast to exceed all but one of its 21 priority-level targets. The Convergence Programme is forecast to exceed 30 of its 41 priority-level targets.

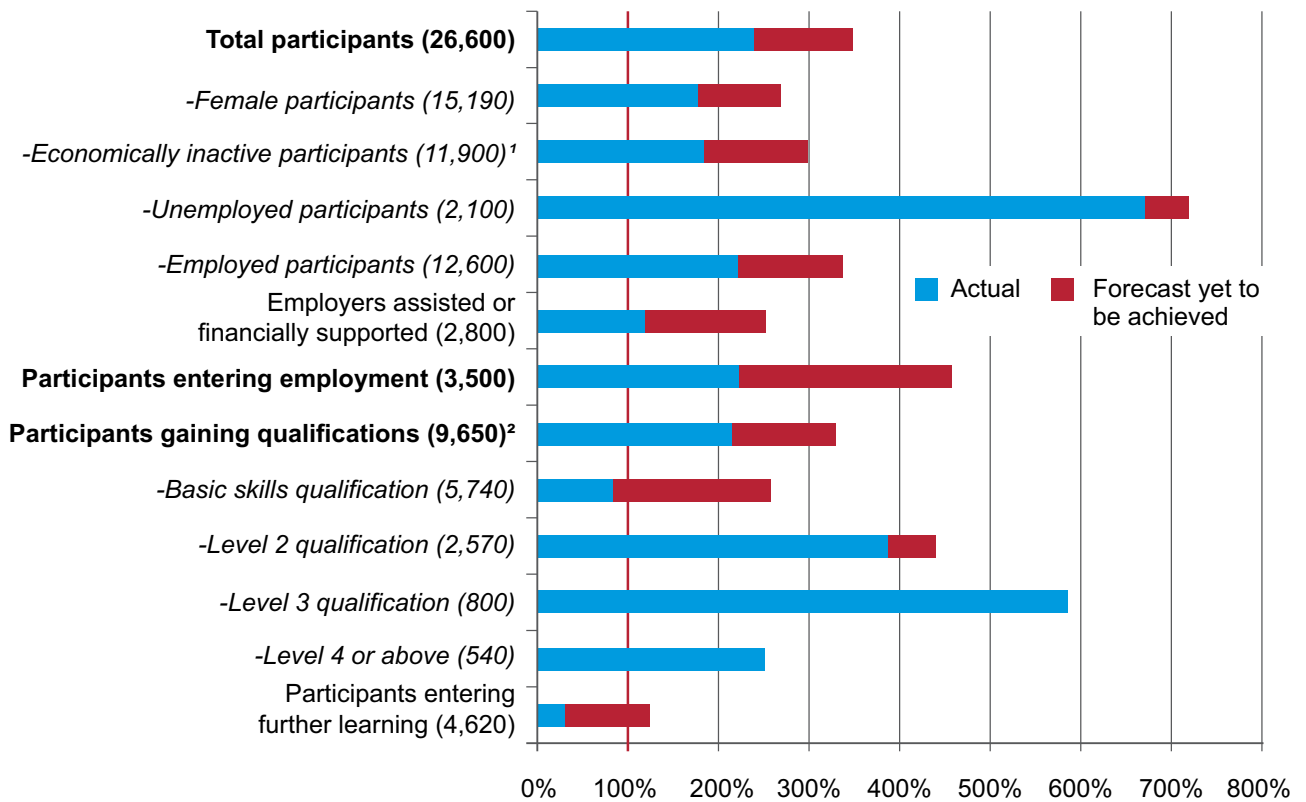
**Exhibit 12 – Actual and forecast performance against ESF Programme targets at 31 December 2013**

The graph shows forecast performance to the end of the programming period for each indicator as a proportion of target. Blue shows actual performance. Red indicates the balance of the forecast that was yet to be achieved at 31 December 2013. The 100% mark indicates the target, dashboard indicators (**paragraph 2.24**) are shown in bold. The target measure is shown in brackets next to each indicator. Figures are based on project sponsors’ returns received by WEFO as at 31 December 2013.

**Convergence Programme**



## Competitiveness Programme



**Notes:**

1 Economically inactive participants are those who are neither employed for more than 16 hours a week nor unemployed (seeking and available for work or under formal notice of redundancy).

2 Qualification levels relate to the Credit and Qualification Framework for Wales. Broadly speaking, level 2 equates to GCSE, level 3 to A-level and level 4 to higher education qualifications.

Source: WEFO

2.36 Despite the strong performance against the programme level targets, as for the ERDF programmes, the rate of progress against indicators has been slower than projected by project sponsors, possibly reflecting general under-spending and any time lag in the collation of performance information. If this shortfall is not met by the end of the programmes, two of the programme level targets (participants entering further learning for both programmes) would be missed, but all of the other targets would still be met by a substantial margin.

2.37 Looking beneath the programme level targets, there have been a number of areas that are not performing as strongly as expected. For example:

- a Priority 1 of the Convergence Programme, which aims to prevent young people aged 11-19 from dropping out of learning or under-achieving, was a new area of activity for the Structural Funds and was relatively slow to start. Around 108,000 young people had participated in related projects by the end of 2013, well above the 35,500 target for the whole programming period. However, the target assumed that project services would be directed at young people most at risk. In practice, projects have attracted a wider range of participants, with WEFO believing that projects are more effective if a wider group of young people take part. The number of young people gaining qualifications gained is forecast to exceed target, but not to the same extent as the number of participants. The number of participants entering further learning is lagging well behind other indicators, partly because sponsors can only count those who proceed to a higher level of non-compulsory education within six months of completing their participation in the project.

It appears that sponsors had expected a looser definition of this indicator when setting their targets.

- b There is likely to be a shortfall in the number of employers assisted or financially supported by the measures designed to increase employment and reduce economic inactivity. Forecast performance is 58 per cent short of target for the Convergence Programme and four per cent short for the Competitiveness Programme. Economic circumstances have made it difficult for projects to engage employers in measures to help the unemployed and economically inactive, and WEFO does not expect the situation to improve significantly before the end of the programmes. In contrast, the forecast for the number of employers assisted to train their existing workers is well ahead of target.
- c As noted previously, progress on Priority 4 of the ESF Convergence Programme (modernising and improving the quality of public services) has been slow and WEFO has withdrawn some of the funding originally allocated to this priority. Project sponsors' forecasts indicate that this priority will fall 75 per cent short of its target for the number of participants and 82 per cent short of target for the number of secondment placements by the end of the programme, but that targets for collaborative agreements between public service bodies, dissemination initiatives and other indicators of collaborative activity will be exceeded. Activity in this area has had a much stronger emphasis on collaboration than originally intended, with a smaller-than-expected proportion of the available funds devoted to leadership and procurement training.

- 2.38 While there are differences in the nature and size of the programmes and the definition of outputs, the targets agreed with the Commission for the 2007-2013 ESF programmes were generally lower than those set for the 2000-2006 ESF programmes. WEFO wanted the 2007-2013 targets to reflect the better control over double-counting that they expected to apply, and the greater emphasis on hard-to-reach groups. WEFO also wanted the programmes to declare only those outputs that involved substantial intervention by the project sponsor that was capable of having a long-term impact on the beneficiary, and set conservative targets to reflect this intention.
- 2.39 Nevertheless, the degree to which they have been surpassed suggests that the ESF programme targets were set too low. In order to keep a clear challenge in place for the remainder of the programme period, in December 2011, WEFO asked the European Commission to increase targets for 23 of the 27 programme level indicators by between 33 and 461 per cent<sup>19</sup>. These changes have not yet been agreed by the European Commission and there is a suggestion that to make this kind of change would cloud the picture of what has been achieved against the original delivery plan. If the targets do change as proposed previously by WEFO, the forecasts as at 31 December 2013 indicate that most of the revised targets would still be met.

**The cross-cutting themes of environmental sustainability and equal opportunities are better established than in previous programmes, but the programmes are likely to fall short of most of their related targets**

- 2.40 Under EU regulations, the two cross-cutting themes of environmental sustainability and equal opportunities must be integrated into all aspects of the Structural Funds programmes. **Exhibit 13** outlines the objectives under each theme. WEFO monitors the cross-cutting themes using a series of indicators agreed with the European Commission, some of which have general application (general indicators) and others that are specific to certain types of activity (specific indicators). The cross-cutting themes must also be addressed in project and programme evaluations.
- 2.41 A WEFO-commissioned process evaluation<sup>20</sup> reported in January 2011 that integration of the cross-cutting themes at the headline level (for example, in project plans) had advanced since the previous programming round. Guidance and support from WEFO specialist advisors was said to be good and most projects scored medium or high against assessment criteria for the two cross-cutting themes. That pattern is also reflected in figures reported more recently by WEFO to the Programme Monitoring Committee.

<sup>19</sup> WEFO has also asked for permission to reduce some priority level targets to reflect particular difficulties in delivering the planned level of performance (notably in relation to public service reform initiatives) or where it expects to withdraw services to avoid the risk of duplication with services provided by the UK Government's Work Programme. Such duplication would be contrary to EU regulations on additionality.

<sup>20</sup> Old Bell 3 Ltd et al, *Effectiveness of Implementation in the 2007-2013 Structural Funds Programming Period*, evaluation commissioned by WEFO, January 2011.

## Exhibit 13 – Cross-cutting Structural Funds objectives on environmental sustainability and equal opportunities

### Environmental sustainability

- reduce emissions of greenhouse gases to help limit the extent of climate change and to help adapt its effects;
- promote sustainable transport;
- promote the efficient use of resources;
- promote the sustainable management of the land, sea and inland waters; and
- improve the quality of the local built environment and opportunities to access green space.

### Equal opportunities

- increase the number of individuals with multiple disadvantages who gain access to employment and self-employment;
- increase the number of women, BME people and disabled people securing training and employment in higher paid and higher skilled sectors and self-employment;
- challenge occupational segregation by increasing the numbers of women and men training or retraining in non-traditional areas, focusing on areas where there are skills shortages; and
- increase the number of employers and training organisations that have equality and diversity strategies, including monitoring systems and methods for building in improvements.

Source: WEFO

2.42 However, the evaluation concluded that project sponsors were making variable progress in integrating the themes into project delivery. Some sponsors still viewed the themes as a compliance exercise and a lack of knowledge and resources meant that sponsors were unable to provide sufficient advice to contractors and project beneficiaries. Some sponsors had deferred specific work on the cross-cutting themes until their projects were well established, which may account for some of the shortfall in performance against the general indicators. Subsequent thematic evaluations<sup>21</sup> found areas of good practice, where projects had actively targeted under-represented groups and monitored the effectiveness of the measures taken, but other areas where a more passive approach had not delivered the progress expected.

### Environmental sustainability

2.43 The ERDF programmes have a general target of ensuring that 20 per cent of enterprises or organisations assisted adopt an action plan to improve environmental performance. At the end of 2013, only 10 per cent of assisted enterprises or organisations had adopted a plan, although the position was expected to improve to 14 per cent by the end of the programmes. The January 2011 process evaluation found that sponsors lacked the capacity to provide the expert support needed to deliver the original target (which was to adopt a formally accredited environmental management system) and the Welsh Government business service centres to which clients were referred were unable to cope with the level of demand. WEFO also believes that the economic downturn has reduced the capacity of the environmental business support sector to deliver services.

<sup>21</sup> Welsh European Funding Office, *Thematic Evaluations of the 2007-2013 Structural Funds Programmes in Wales: Synthesis Report*, Welsh Government, 2013.

WEFO responded by replacing the original target, with a target to adopt action plans that do not necessarily require professional advice. Nevertheless, there are no plans to increase capacity to provide support.

- 2.44 The programmes have made mixed progress against the specific environmental sustainability indicators. Eight of the 15 indicators are forecast to be met or exceeded by the end of the programming period, some by a large margin. At the end of 2013 project forecasts indicated that the ERDF programmes would:
- a Exceed targets for environmental risk management initiatives, initiatives to develop the natural or historic environment, provision of public access to the countryside or coast, reduction in greenhouse gas emissions and people benefiting from flood protection measures. This reflects the good progress made on environmental management projects, the introduction of home energy efficiency measures and the higher than expected funding devoted to flood protection measures.
  - b Fall well short of targets for renewable energy generated, energy saved, waste reduction and enterprises monitoring carbon emissions. There has been slow progress with most energy and waste projects.
- 2.45 The ESF programmes are likely to miss the three priority-level targets for integrating environmental sustainability into awareness raising, education and training, although there was a marked improvement in performance during 2012 following an exercise by WEFO to provide additional support to projects. The programmes were also likely to exceed the target for 10 per cent of projects to provide specialist training in sustainable development.

## Equal opportunities

- 2.46 Evaluations of the 2000-2006 programmes concluded that more needed to be done to support and encourage employers to integrate equality procedures into their operations. The target for 50 per cent of enterprises, organisations and employers assisted to adopt or improve an equal opportunities strategy is a key aim of the 2007-2013 programmes. Performance against the target has been disappointing: forecast achievement is around 21 per cent by the end of the programmes, and actual achievement was 12 per cent at the end of 2013.
- 2.47 Progress on ERDF projects has been hindered by the reprioritisation of funding away from certain support services as a consequence of the Welsh Government's Economic Renewal Programme. For ESF projects, WEFO attributes the under-performance to a combination of under-reporting by project sponsors and the impact of delays in delivery and staff turnover in sponsors' project development teams. In some cases, project staff have been unaware of the commitment to deliver on the equality indicator. WEFO has been meeting sponsors and issuing good practice case studies to raise awareness of the cross-cutting themes and to show how they can be integrated into project delivery. WEFO expects achievement rates to rise as these issues are addressed, and expects project evaluations to uncover other evidence of equality-related benefits. However, a major improvement is unlikely without additional resources to support companies and employers.
- 2.48 WEFO produces extensive data on the proportion of ESF participants in 'key intervention groups' which include gender, age, ethnicity and disability. Output targets are set for the percentage of participants from each group, but not for results (for example, participants gaining qualifications or entering employment). The following patterns are evident from the data at 31 December 2013:



- a *Gender*: around 45 per cent of ESF programme participants were female, compared with an average target of 55 per cent across the two ESF programmes. There was a similar pattern for participants gaining qualifications (43 per cent female) but only 36 per cent of participants entering employment and 37 per cent of those entering further learning were female. Only around two per cent of female participants in in-work training schemes funded by the ESF Convergence Programme were part-time workers, compared with a target of 29 per cent.
- b *Older participants (aged 50 and over)*: were under-represented across the two ESF programmes. Only eight per cent of participants were from this age group, against a target of 36 per cent, although this was forecast to increase to 21 per cent by the end of the programmes. Older workers accounted for a similarly low proportion of participants gaining qualifications, entering employment or entering further learning.
- c *Black minority ethnic (BME) status*: BME participation rates were generally fairly low, at around four per cent for both ESF programmes, but this reflects the relatively small BME population in the Convergence area. The BME participation rate was much higher for the economic inactivity measures in the Competitiveness Programme – 18 per cent against a target of 12 per cent.
- d *People with a work-limiting illness or a disability*: accounted for about 27 per cent of participants in projects aimed at tackling economic inactivity, compared with an average target of 54 per cent and a forecast for the end of the programmes of 39 per cent. These people were less likely than other participants to gain qualifications but more likely than other groups to enter employment. The group was particularly poorly represented on employer training schemes, at around three per cent against a target of 13 per cent.

2.49 Overall the figures indicate that the ESF programmes will not have the expected impact on the 'key intervention groups' compared with other groups. To some extent this reflects the impact of the economic downturn, which has increased the number of unemployed participants relative to those classified economically inactive. A higher proportion of the unemployed are young and/or male. However, the thematic evaluations<sup>22</sup> indicated that project design was also an issue. For projects aimed at increasing employment, there were gaps in the provision of services specifically for older workers, those with caring responsibilities and those facing transport barriers in obtaining employment (these last two being more likely to be women). For projects aimed at raising skills, the evaluation found that projects had been 'fairly passive' in their approach to engaging with targets groups, reflected in the very low proportion of disabled and older participants to date, groups for which no dedicated projects had been commissioned.

<sup>22</sup> Welsh European Funding Office, *Thematic Evaluations of the 2007-2013 Structural Funds Programmes in Wales: Synthesis Report*, Welsh Government, 2013.

2.50 Because the ESF programmes are likely to exceed their participation targets by substantial margins, the overall number of women and BME participants is still likely to be higher than originally expected. But the number of older participants and those with a work-related illness or disability is still likely to fall well short of expected levels (by around 54 per cent and 23 per cent respectively, based on the position at 31 December 2013).

#### Remedial action planned by WEFO

- 2.51 WEFO officials recognise that progress against the equal opportunities and environmental sustainability targets has been patchy and told us that they planned or were undertaking the following remedial measures:
- a meeting sponsors to discuss recovery plans where performance has been patchy;
  - b sharing examples of good practice and encouraging projects that are struggling to learn from others undertaking similar activity;
  - c holding discussions with several organisations about developing a specific project to support delivery of the specific indicators;
  - d for the 2014-2020 programmes, integrating the equal opportunities and environmental sustainability targets more closely with day-to-day project activity, so that they are not seen as an add-on requiring separate strands of activity; and
  - e organising a rolling programme of training events to support the new approach for the 2014-2020 programmes (the first series of events has already been held for WEFO staff and those delivering projects).

While it is too early to fully assess the overall impact of the programmes, there are some positive signs and ongoing evaluations will paint a clearer picture

There is limited evidence available at this stage about the long-term impact of the 2007-2013 programmes, although evaluation work is ongoing

2.52 The direct impact of socio-economic programmes is hard to assess with any precision because it can be affected by other factors in the external environment, such as the recent economic downturn<sup>23</sup>. Moreover, the impact of these programmes can include 'soft' outcomes such as greater personal confidence or better relationships and joint-working between people and organisations.

2.53 Performance against the impact indicators in the operational programmes is assessed as part of programme evaluation. Much of this evaluation work is planned to take place towards the end of the programming period and, as at the end of 2013, the amount of published evidence on impact was fairly limited. However, some evidence of impact is available from the following sources, mainly covering the ESF programmes:

- a *The ESF Leavers' Survey* (a major annual survey of participants leaving ESF provision) and the *ERDF Business Survey* (of firms receiving ERDF support). WEFO uses the findings from these large-scale surveys to estimate the net impact of the ESF programmes on employment outcomes and the net impact of the ERDF programmes on job creation.

<sup>23</sup> One approach that can be taken is to try to calculate the net impact after factors such as 'deadweight' and 'displacement' are taken into account. Deadweight is the amount of reported benefits that would have happened anyway without the assistance of the programme. Displacement is the extent to which benefits are simply transferred from one place to another because of an intervention. This calculation may involve comparison with control groups (a representative sample of beneficiaries who have not participated in the programme), or the use of standardised discount factors to estimate deadweight, displacement and multiplier effects. The multiplier effect is the extra economic activity that is generated indirectly by the assistance, usually through spending on local suppliers.

- b *Interim thematic evaluations.* WEFO commissioned a series of interim thematic evaluations that cover individual programme priorities and published these findings in December 2013. The evaluations focus on policy issues, operational arrangements, the likely effectiveness of services and performance against monitoring indicators rather than impact. However, the two evaluations published by the end of May 2013<sup>24</sup> do draw some inferences on impact from survey evidence and interviews with participants. The interim thematic evaluations will be followed by final evaluations that will consider the programmes' impact in more depth.
- c *Interim project evaluations commissioned by project sponsors.* As at 31 May 2013, WEFO had published 10 project evaluations on its website with around 40 others due to be published later in the year. Most of the 10 evaluations published at that time included some assessment of impact, based mainly on analysis of monitoring data and the results of participant surveys or interviews. Eight of the evaluations were for ESF projects and two were for ERDF projects, with these projects ranging in value from £2 million to £78 million.

- a There was generally good coverage of programme objectives and expected activities across all thematic areas of the programmes. The main gap was in strategic infrastructure, where there was a much greater focus on road schemes rather than the expected balance between public transport and road.
- b There was a high level of satisfaction with the services provided from ESF participants and employers, especially with the quality of provision. Where relevant, participants particularly valued the provision of individually tailored support from mentors and counsellors.
- c Project administration was generally effective, notwithstanding some initial teething problems and delays. Project management capability varied between and within projects.
- d Projects had adapted fairly well to collaborative working<sup>25</sup> and there were many examples in all areas of the programmes, although it had taken some time to establish effective joint working arrangements where the scale of joint working was a new development, for example in regional projects aimed at supplying young people with the skills needed for future employment. Several project evaluations reported concerns that partners were not referring participants to the project as much as they should or commented on the need for greater sharing of good practice between project delivery staff.

2.54 In addition to their findings on impact, there are some common themes arising from most of the evaluations. For example, the evaluations found that:

<sup>24</sup> These two evaluations related to Priority 1 of the ESF Convergence Programme (supplying young people with the skills needed for learning and future employment) and Priority 2 of the same programme (increasing employment and tackling economic inactivity).

<sup>25</sup> Collaborative working between partners and projects is a key aim of the current programming round (paragraph 3.1).

Evidence available for the ESF programmes indicates a positive effect on participants, but the impact on employment rates varies significantly by gender, location and employment history

#### Supplying young people with the skills for future employment

- 2.55 Evaluations in this area were based on in-depth interviews with stakeholders (project staff and others involved in providing or overseeing services) and participants. The evaluations received very positive feedback on the services provided and participants reported beneficial effects on their confidence, social skills, motivation and aspirations. There was a strong feeling among stakeholders that the services added value to existing provision and had a positive impact, a conclusion endorsed by the evaluators themselves. However, due to gaps in data and inconsistent application of the measurement tools available, it was not possible to quantify the 'soft outcomes' achieved, the achievements that indicate progress – 'distance travelled' – on the path to employment.
- 2.56 None of the evaluations were able to quantify the scale of impact on longer-term outcomes. However, the Engage project evaluation sought to calculate the project's effect on some indicators of social exclusion (Exhibit 14).

#### Exhibit 14 – Impact assessment for the Engage project

Engage was a collaborative project between 10 local authorities and further education colleges to help young people aged 14-19 in South-West Wales to improve school attendance and build confidence to maximise career opportunities. Activities included counselling, mentoring, work placements and voluntary work. The project cost £21 million and ran for around three years to the end of 2012.

The evaluation of the Engage project compared trends in the proportion of year 11 school leavers not in employment, education or training (NEET), the proportion of pupils leaving school without qualifications, unauthorised absenteeism from school and school exclusion rates between areas covered by Engage and those not covered by the project. It found that positive trends were significantly higher in Engage areas compared with the rest of Wales and suggested that up to half of the improvement could be attributed to Engage. The evaluation acknowledged that such analysis was 'flawed in many respects' because it was difficult to adjust for the effect of other factors, but concluded that the analysis nevertheless 'gave an insight into the scale of achievement within a relatively short period of time.' However, it was not possible to attribute longer-term outcomes such as employment to the project, given the relatively short period of time during which it had operated.

*Source: Wavehill Ltd for Neath Port Talbot Council, 'Engage Project – Final Evaluation', January 2013*

## Increasing employment and tackling economic inactivity (improving participation)

2.57 The most developed evidence of impact is from the annual ESF Leavers' Surveys. The most recent published survey findings<sup>26</sup> asked 3,544 participants who left ESF programme services in 2011 about the reasons for their participation, its benefits and what had happened to them since. The survey report included an assessment of net impact by comparing career transitions for survey respondents, such as getting a job, with those for a matched sample of non-participants drawn from the Annual Population Survey.<sup>27</sup> Key findings from the Leavers' Survey include:

- a Most participants gained qualifications, and higher qualifications were associated with greater benefits. Around 73 per cent of respondents obtained a qualification and, where able to be established<sup>28</sup>, 13 per cent of respondents reported that the qualification they obtained was at a higher level than their previous qualification(s). Those obtaining a same or higher-level qualification were more likely to report a range of positive impacts from their training than other participants.
- b Participants reported a large increase in employment rates following participation: from 14 per cent to 66 per cent. Only 22 per cent of respondents finding work thought that ESF intervention had been 'vital' in helping them secure their job<sup>29</sup>. However, across different client groups, employment rates were higher than the comparable control groups. Employment outcomes varied by participants' employment history and other personal circumstances:

- Employment outcomes were significantly better for the recently unemployed who received training specifically for those made redundant – 76 per cent were in employment 12 months after completion of their training, 12 percentage points higher than the control group. In contrast, employment rates were 43 per cent for other unemployed participants (six percentage points higher than the control group) and only 17 per cent for economically inactive participants (nine percentage points higher than the control group).
- Employment rates were significantly poorer for those with a work-limiting health condition or disability, for those aged under 25 or over 55, and for those who had been out of work for more than a year.
- Local employment conditions had an effect, with poorer outcomes for participants living in areas with the lowest employment rates (ie, much of the South Wales Valleys).
- Around 85 per cent of participants who had found paid work were satisfied with their jobs. However, earnings and skills levels tended to fall below the Welsh average, especially for the Convergence Programme. Participants who had received redundancy training were nine to 13 percentage points less likely to enter low-paid employment than a control group, but there was no statistically significant effect for other groups.

<sup>26</sup> Cardiff University, Old Bell 3 Ltd and IFF Research Ltd, *The 2011 European Social Fund Leavers' Survey*, WEFO, March 2013.

<sup>27</sup> The matched sample of non-participants (those not participating in ESF) was selected to replicate as closely as possible the characteristics of the respondents to the Leavers' Survey, thereby enabling reliable comparisons to be made between the two groups. The Annual Population Survey asks around 16,000 households in Wales every three months about their own circumstances and experiences regarding a range of subjects including housing, employment and education.

<sup>28</sup> Excluding the 51 per cent of the population for whom qualification levels before and after intervention could not be established.

<sup>29</sup> Similarly high levels of deadweight were reported by participants in the ReAct programme, which provided financial support for re-training to people who had recently lost their jobs through redundancy.

2.58 Project evaluations for careers guidance and graduate placement services reported high levels of satisfaction with the guidance and other services provided, and a perception among participants that the projects had helped them secure employment where this occurred. Employers that provided graduate placements reported commercial benefits from the placements and that they were more likely to recruit graduates in the future.

#### Increasing skills and adaptability of employees in the workplace (supporting progression)

2.59 The ESF Leavers' Survey 2011 found that 73 per cent of participants gained a qualification, but only 17 per cent of those whose qualification transition could be determined gained a higher-level qualification than the highest level they had previously achieved. There was a marginal improvement in the proportion of participants holding qualifications at levels 3 and 4 of the National Qualifications Framework (A-level standard and above). However, a high proportion of participants said they had generic skills (eg, communications, organisation, team building, leadership) and had gained softer benefits such as confidence or motivation.

2.60 For those already in employment, 65 per cent of respondents to the survey reported having more training opportunities, 64 per cent were more satisfied with their work and 56 per cent reported improvement in future pay and promotion prospects, while 27 per cent said they had had a promotion. These benefits were particularly pronounced where participants had changed jobs, and 20 per cent of these participants said that ESF intervention had been vital in helping them

get their job. Generally, however, only seven per cent of participants said that any improvements in their employment had been directly related to ESF intervention.

2.61 Average earnings of respondents (£391 a week) were higher than for previously unemployed or economically inactive participants and they tended to have longer hours and better security of employment.

2.62 There is relatively little information available on the impacts on employers and the wider economy of ESF training provision. The focus of the monitoring indicators approved by the European Commission is very much on the benefits for individuals. An interesting exception is the evaluation of the ProAct project ([Exhibit 15](#)).

#### Exhibit 15 – Impact on employers of the ProAct project

ProAct was a £66.8 million project sponsored by the Welsh Government to provide work-related training to employees at risk of redundancy or short-time working during the recession. It ran between January 2009 and June 2010 to address the severe impact of the recession on many major employers in Wales.

The evaluation of the ProAct project quantified the economic benefits in gross value added (wages and operating profit) at £95.8 million for a cost of £21 million, safeguarding 1,833 jobs at a cost per job of £12,015. The evaluation considered this to be a creditable outcome given the exceptionally difficult circumstances that the project was dealing with. ProAct enabled companies to up-skill their workforce in readiness for the upturn and to avoid the loss of skilled and experienced employees. Employers reported an increase in productivity in two-thirds of cases, indicating benefits that went beyond the immediate safeguarding of jobs.

*Source: Cambridge Policy Consultants for the Welsh Government, 'Impact Evaluation of ProAct', October 2011*



**The 2011 ERDF Business Survey results suggest that the ERDF programmes have created or safeguarded a significant number of jobs, but only a minority of respondents credit ERDF with tangible outcomes for their business**

2.63 The 2011 ERDF Business Survey reported results from 778 businesses that had received support from the research and development and business support priorities of the two ERDF programmes (a response rate of 40 per cent). The survey did not cover business finance, regeneration, infrastructure or other capital projects, was not able to compare the results with a sample of comparable non-assisted businesses and did not adjust for potential double-counting. While the results, therefore, need treating with caution, the survey found that:

- a Around half of the firms receiving support with forming collaborative research and development partnerships had gone on to consolidate these, with most reporting that these partnerships were important to their business strategy.
- b Respondents were 'surprisingly likely' given the economic climate, to report positive changes in their business. Around two-thirds said they had introduced new or modified products or processes and many others reported financial benefits (*Exhibit 16*). However, the extent to which respondents attributed these changes to ERDF was more limited, particularly when asked whether such changes would have occurred in the absence of ERDF.

- c Most businesses were focused on Welsh markets and recruited within Wales, which indicates that assisted companies might displace growth from non-assisted businesses within the programme area. However, this finding was less true of job-creating businesses, and the 38 per cent of respondents who said that ERDF had helped them win new business did not generally associate this with having taken market share from local competitors. The evaluation concluded that the effect of displacement was relatively modest.
- d Only 17 per cent of respondents attributed any job creation to ERDF assistance. Taking into account deadweight, displacement and multiplier factors, the survey estimated that between 275 (75 per cent) and 335 (92 per cent) of the 363 new jobs reported by these respondents could be attributed to the ERDF programmes. This estimate of the proportion of new jobs attributable to the programmes compares favourably with the 29 to 45 per cent ratio estimated for the 2000-2006 programmes.<sup>30</sup> Applying the Business Survey ratios to forecast job creation at the end of 2013 would indicate that the 2007-2013 ERDF programmes would create between 32,300 and 39,600 new jobs. However, this estimate needs to be treated with caution due to the limitations of the sample as noted above.

<sup>30</sup> Old Bell 3 – *Mid-term Evaluation Update for the Objective 1 Programme*, final report, December 2005. Net impact was calculated by discounting the gross results data forecast by WEFO for the end of the programme, using survey evidence and economic benchmarks. WEFO updated the calculations by substituting the final, actually achieved results for the forecast data.



- e The effect of ERDF in safeguarding jobs is at least as significant as job creation, with around 1.25 jobs safeguarded for every job created. The Business Survey calculated that between 350 and 428 net jobs had been safeguarded. WEFO does not collect monitoring information on jobs safeguarded, but they are clearly an important employment outcome of the programmes. Safeguarding jobs was not considered an objective at the beginning of the programme round when economic conditions were more buoyant, so WEFO has not collected data directly on jobs safeguarded over the whole programme period. They do now ask project sponsors to capture this data informally, and the Commission has indicated that it will be interested in this information when the overall impact of the programmes is assessed after the programme period ends.
- f It was not possible to conclude definitively on the pay and skill levels of jobs created relative to the Welsh average, but the evidence suggested that the qualifications required for all jobs within the respondents' businesses was similar to that for Wales as a whole.

**Exhibit 16 – ERDF Business Survey respondents – turnover, profitability, productivity and exports since receiving ERDF support**

	Turnover	Profitability	Productivity	Exports
<b>Change reported:</b>				
Increase	42%	34%	42%	34%
No change	49%	60%	54%	62%
Decrease	9%	6%	4%	4%
<b>Perceived impact of ERDF support:</b>				
% of respondents saying ERDF had a positive effect	41%	37%	40%	24%
% of respondents saying outcome would have been worse without ERDF <sup>1</sup>	32%	29%	29%	18%

Note:

<sup>1</sup> % of respondents saying that outcome was 'very likely' or 'likely' to have been worse.

Source: ERDF Business Survey, Old Bell Ltd in association with Cardiff University and IFF Research Ltd, published by WEFO in 2012.

**Evidence for the 2000-2006 programmes suggests a positive impact on jobs and skills, but the prosperity gap between Wales and the EU average remains significant**

- 2.64 The ultimate aim of the Convergence Programmes is to help close the prosperity gap between the EU average and those regions lagging behind. GDP is usually used as the headline indicator of an area's prosperity and is used by the European Commission to determine which areas receive programme funding, although the programmes are intended to address a wide range of social and environmental objectives that do not necessarily translate into higher GDP.
- 2.65 It is too early to assess the impact of the current programmes on GDP per capita – impacts are likely to occur over the long term and will be difficult to disaggregate from wider economic forces, given that the funding available is a small fraction of the area's economy. Data on regional GDP is also slow to materialise and the latest data is for 2010, when the current programmes had just started to deliver services.
- 2.66 The previous programmes were broadly similar in scale and funded similar activities to the current programmes, albeit in a more favourable economic climate. An analysis by the Welsh Government in 2011<sup>31</sup> reported that GDP had fallen slightly against the EU-15 average<sup>32</sup>, and this negative trend accelerated in the subsequent recession as the whole UK economy declined at a faster rate than the rest of the EU. As a result, the GDP of the Convergence area fell from 75 per cent of the UK average in 2000 to 70 per cent by 2010, after peaking at 78 per cent in 2005.

The Welsh Government believes that some of the reduction is due to an out commuting effect – more people working outside the programme area in Cardiff and Newport, so that their production is counted in East Wales rather than West Wales and the Valleys.

- 2.67 Other key indicators showed more favourable results for the decade to 2010. There was a significant increase in primary income relative to the UK and EU averages; primary income measures the income earned from economic activity by residents of an area rather than what is produced in the area, and offsets the out-commuting effect. Employment and economic activity rates have also increased relative to the UK average, as did qualification rates, although they remain below the UK average. The contribution of the Structural Funds to these changes is hard to establish with any certainty. However, an analysis by WEFO in 2011<sup>33</sup>, which drew on findings from a mid-term evaluation of the previous programmes in 2005<sup>34</sup> and the results reported by projects at the end of the programming period estimated that the programmes had:
- a created between 26,000 and 45,500 net jobs (29 to 45 per cent of the gross figures reported by projects);
  - b created between 1,700 and 2,500 net new SMEs (10 to 15 per cent of the gross figures reported by projects); and
  - c led to between 48,700 and 89,300 ESF programme net participants entering employment or further learning (44 to 80 per cent of the gross figures reported by projects).

31 Welsh Government, *2000-2006 Structural Funds Synthesis Report*, March 2012 and Welsh Government Statistical Directorate (2011): 'Sub-Regional GDP Estimates, paper for the Programme Monitoring Committee,' WEFO, March 2011.

32 WEFO considers the EU-15 (members of the EU in 1999 when Wales qualified for Objective 1 funding) to be the most appropriate comparator for Wales. The economies of the 14 member states that joined from 2004 tend to be growing faster from a lower base, and their inclusion in comparisons would give a less accurate impression of economic performance in Wales.

33 Welsh Government, *2000-2006 Structural Funds Synthesis Report*, March 2012.

34 Old Bell 3 Ltd, *Mid-Term Evaluation Update for the Objective 1 Programme*, WEFO, 2005.

## Part 3

Management arrangements are effective and have improved since the previous programming round, despite some disruption in the early stages of Programme implementation



3.1 This part of the report considers WEFO's management of the 2007-2013 programmes with particular reference to:

- a the adaptability of the programmes to changes in policy and external conditions;
- b greater emphasis on a procurement-based approach to delivery;
- c project appraisal procedures;
- d financial management and control; and
- e project delivery, monitoring and evaluation.

3.2 Our analysis draws, in part, on findings from our survey of project sponsors and WEFO project development officers in 2011<sup>35</sup> (Appendix 1). It also reflects findings from a WEFO commissioned customer survey in 2009 and a 'process evaluation' exercise completed in 2011. WEFO's procedures have remained largely unaltered since this evidence was collected and most completed or live projects to date were approved before 2011. Nevertheless, it is possible that opinions have shifted since these surveys were conducted.

**There have been mixed views about the overall administration of the programmes although stakeholders generally support the action that WEFO has taken to simplify programme structures and reduce the number of projects**

3.3 Our survey of project sponsors and WEFO project development officers included some general questions about the overall design and administration of the Structural Funds programmes. Overall the feedback we received suggested that:

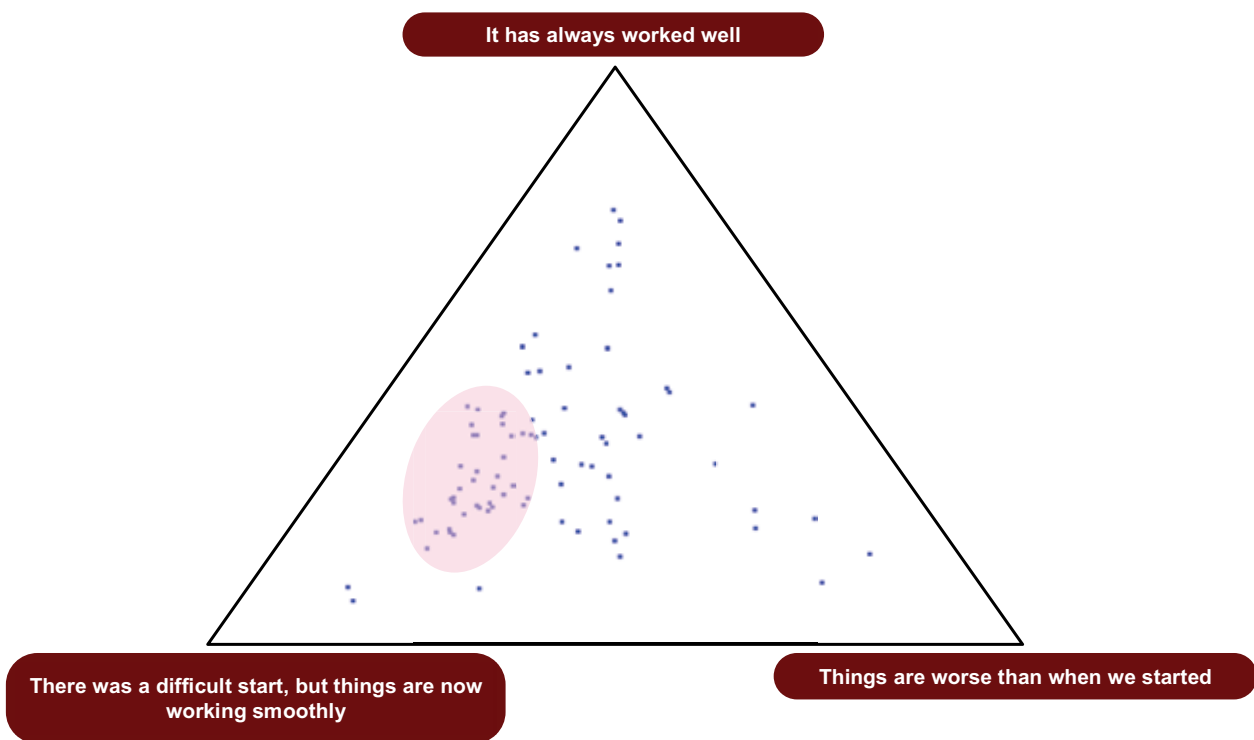
- a the system as a whole was working better after a difficult start (Exhibit 17), but views about its overall efficiency were mixed with project development officers tending to see the system as efficient, whereas project sponsors were fairly evenly divided;
- b decision making by WEFO was seen as slow, but sponsors mainly attributed this to bureaucracy while project development officers tended to attribute it to the complexity of the issues involved;
- c project sponsors tended to view WEFO as being quite rigid in its management procedures and approach to rules and regulations, and to be risk-averse – whereas project development officers were more likely to see WEFO's approach as adaptable and flexible with risks identified and managed;

<sup>35</sup> Project development officers are primarily responsible for appraising grant applications and subsequent monitoring of those projects' progress.

### Exhibit 17 – Views of Wales Audit Office survey respondents on the management and control system

The survey in 2011 asked respondents to choose a position between the three statements below. The dots show the number of responses and the shaded area indicates the greatest concentration of responses. The results indicate the balance of opinion among responses and are not intended to be analysed quantitatively.

Thinking of the whole system put in place to manage the programmes:



Source: Wales Audit Office survey of project sponsors and project development officers

- d where things went well, both sponsors and project development officers attributed this to the people involved rather than the process followed or the resources available; and
- e where problems occurred, this was attributed to processes more than people or resources.

3.4 We asked our survey respondents to provide a narrative commentary about their experience of the Structural Funds programmes. Overall, 49 per cent of our 91 respondents described their comments as negative and 32 per cent described their comments as positive (17 per cent were neutral and two per cent were unsure). There was no discernable difference between project sponsors and the project development officers.

- 3.5 WEFO's 2009 customer satisfaction survey<sup>36</sup> found that 41 per cent of sponsors were satisfied or very satisfied with the overall level of service from WEFO. However, of those who had experience of the previous programming round, 75 per cent said they found the current programmes to be more bureaucratic.
- 3.6 WEFO has sought to streamline administration and reduce costs by simplifying certain programme structures. The main changes, which have had the broad agreement of stakeholders, are:
- a There is now only one Programme Monitoring Committee covering all programmes, rather than the six separate committees that existed for the 2000-2006 programmes.
  - b The 'thematic advisory groups' that previously advised WEFO officials on project selection have been abolished. WEFO now makes funding decisions in the light of appropriate expert advice.
  - c The Operational Programmes are less prescriptive about the allocation of resources than the 2000-2006 programmes. Programme priorities are divided into fewer sub-divisions (known as 'measures' in the 2000-2006 programmes and 'themes' in the current programmes). Previously, the European Commission exercised control over any changes to measure budgets. For 2007-2013, WEFO has flexibility in transferring funds between themes because the funding allocations are indicative only.
- 3.7 WEFO funded 2,463 projects in the comparable programmes<sup>37</sup> under the previous programming round. The administration of so many, relatively small, projects was very resource intensive. WEFO resources were focused on certain core tasks relating to project appraisal, payment of grants and compliance issues rather than more active performance management of individual projects. WEFO has succeeded in reducing the number of projects dramatically in the current programming round, with a much greater proportion of programme expenditure being through higher value projects (**Exhibit 18**). There were 287 projects at 31 December 2013, of which 107 were sponsored by the Welsh Government. WEFO expects the overall number of projects to increase a little by the end of the programmes, with some smaller projects being approved to address particular needs and to use available resources.
- 3.8 Our survey findings, and our wider fieldwork, indicated general in-principle support for the shift towards fewer, larger projects, although the survey findings pointed to some concerns about the practical application of this approach and collaboration and partnership working in general. Comments made by some survey respondents raised a variety of practical concerns about the delivery record of some larger projects, the difficulty of involving the voluntary sector, and the need for WEFO to be more active in encouraging and supporting collaboration.

<sup>36</sup> Databuild Research and Solutions, *WEFO Customer Insight Survey 2009*, WEFO, May 2010.

<sup>37</sup> Objective 1, Objective 2 and Objective 3 programmes in the 2000-2006 programming round.



## The programmes have been flexible enough to respond effectively to the economic downturn and to some significant changes in policy

WEFO re-allocated resources to respond to the economic downturn and used the opportunity of a weaker pound to reduce pressures on match funding

3.9 WEFO took several important measures to ensure that the programmes were best placed to help Wales respond to the challenges of the economic downturn that began in 2008. This action was endorsed by the European Commission and included:

- a The Welsh Government developed and implemented the ProAct project to help employers train their staff during period of down-time and expanded the ReAct project, which provided discretionary grants to unemployed individuals to help them re-train following redundancy. Skills Growth Wales, introduced in April 2010 as the successor to ProAct, has a stronger emphasis on company growth and higher skills to promote economic recovery. ReAct was re-launched in April 2011 to focus more on recruitment of new staff rather than re-training of redundant workers.
- b Re-allocating resources and changing eligible activities to meet specific needs, including:

Exhibit 18 – Change in average size of projects by value of approved EU grant for comparable programmes

	2007-2013	2000-2006
Total number of projects	287	2,463
Average value of project (approved grant, £000)	£6,654	£584
<b>Proportion of programmes delivered by projects with approved EU grant of:</b>		
Below £100,000	0.04%	2.9%
£100,000 – £999,999	1.3%	31.2%
£1 million to £9.999 million	41.9%	57.3%
£10 million or over	56.7%	8.6%

Source: WEFO (approved project databases as at 31 December 2013)



- transferring £37.7 million from ESF Convergence Priority 1 (preventative work with young people) into Priority 2 (increasing employment and tackling economic inactivity) to help tackle the rise in unemployment;
  - making careers advice and guidance an eligible activity to meet high demand for in-depth personal careers guidance; and
  - providing some funding to encourage sustainable tourism initiatives to take advantage of opportunities to increase market share while addressing problems created by the downturn.
- c Negotiating with the European Commission an increased intervention rate for EU funding to reduce pressures on match funding resulting from the economic downturn generally and from the weakening euro/sterling exchange rate. The weakening value of the pound meant that more EU funding, which is paid in euros, was potentially available to Wales. But this, in turn, would have required additional match funding without an increase in the EU funding intervention rate.

**WEFO worked quickly and effectively with other parts of the Welsh Government to reflect policy changes arising from the launch of the Economic Renewal Programme in 2010**

3.10 In July 2010, the then Minister for the Economy and Transport launched *Economic Renewal: a new direction*. The underpinning 'Economic Renewal Programme' is designed to support sustainable recovery from the economic downturn and centres on five priorities:

- a investing in high-quality and sustainable infrastructure;
  - b making Wales a more attractive place to do business;
  - c broadening and deepening the skills base;
  - d encouraging innovation; and
  - e targeting Welsh Government business support on six sectors where Wales can gain competitive advantage (ICT, energy and environment, advanced materials and manufacturing, creative industries, life sciences and financial and professional services).
- 3.11 Following the Minister's announcement, WEFO initiated a review of the two ERDF programmes. Alongside this, the Welsh Government undertook a review of projects it sponsored under the ERDF programmes to ensure they too were aligned with the Economic Renewal Programme. The reviews were completed by September 2010 and, with European Commission approval, led to the following changes to the ERDF Convergence Programme and consequent changes to relevant programme targets:
- a support for business was focused on the six priority sectors identified in the Economic Renewal Programme;
  - b funds originally earmarked for direct support to business (£40 million of EU funding and £50 million in match funding) were re-allocated to transport infrastructure projects, reflecting a change in emphasis from grants to investment and infrastructure; and
  - c funding originally earmarked for technical assistance (£10 million of EU funding and £11 million in match funding), was reallocated to regeneration projects.

- 3.12 There were also two changes to the ERDF Competitiveness Programme:
- a ICT and R&D infrastructure activity (the latter was previously only funded by the Convergence Programme) became eligible for support and, where necessary, relevant indicators were developed to reflect this; and
  - b two programme targets, 'enterprises assisted' and 'new or improved products, processes or services launched' were reduced to reflect the scaling back of specific projects.
- 3.13 Some projects were re-designed and others were terminated or scaled back. Overall, WEFO withdrew £50 million from approved projects, with the objective of reallocating this funding to projects that better supported the aims of the Economic Renewal Programme. The predominance within the current programmes of large scale projects, many of which are managed by the Welsh Government, made the process of redesigning projects and/or withdrawing funds from projects easier than might have been the case under the previous programmes.

**WEFO has modified the ESF programmes to avoid duplicating the UK Government's 'Work Programme'**

- 3.14 The UK Government introduced the 'Work Programme' in July 2011. The Work Programme largely replaces all pre-existing UK Government welfare-to-work schemes and is part funded by ESF.<sup>38</sup> The Work Programme provides tailored support to help people who are long-term unemployed or economically inactive obtain employment. It covers Jobseekers' Allowance and Employment and Support Allowance recipients once they have received benefits for a specified period, ranging from three to 12 months depending on individual circumstances.
- 3.15 The Work Programme targets the same people as many projects across the two ESF programmes in Wales. To avoid duplication and ensure compliance with requirements to demonstrate added value, WEFO decided that it would re-focus most of its ESF programme activity on those who are not eligible for the Work Programme, such as lone parents with young children, 16-17 year olds and Incapacity Benefit claimants, as well as those who, while eligible to join the Work Programme, have not yet done so. WEFO had proposed excluding all those eligible to join the Work Programme, but amended its plans to reflect concerns that the Work Programme would not be able to support all eligible clients and some individuals might not be eligible for support from any programme.
- 3.16 In any case, the Work Programme was considered likely to reduce demand for measures designed to increase employment. WEFO therefore proposed re allocating £26 million of EU funding to measures designed to prevent economic inactivity among young people and workforce skills development, for both of which there has been buoyant demand. These changes were approved by the Programme Monitoring Committee in December 2011 and are currently waiting for approval from the European Commission.

<sup>38</sup> In January 2012, the National Audit Office reported on *The introduction of the Work Programme*. The Work Programme itself is part-funded by ESF paid to the Department of Work and Pensions.

## The greater use of competitive procurement as a delivery model has proved difficult to implement, but if well managed should have positive effects in the longer term

WEFO has placed a greater emphasis on competitive procurement and expects that around a third of all programme expenditure will be spent through procurement by project sponsors

3.17 For the 2000-2006 programmes, competitive procurement<sup>39</sup> was used by project sponsors for some business support and training projects but was not the most common delivery model. For the 2007-2013 programmes, WEFO has required sponsors to procure service delivery unless there is a special relationship between the sponsor or the grant recipient and the target group of beneficiaries, and then only if there is not a genuine market for the services involved.

3.18 Many projects operate mixed delivery models, with some services being procured and others delivered directly or via grant schemes. Overall, WEFO expects at least £1.30 billion or 35 per cent of total programme expenditure to be spent on contracts procured by sponsors. At 31 December 2013, project sponsors had awarded a total of 2,569 contracts worth £1.09 billion through procurement, mostly to the private sector. The amount subject to procurement is likely to be significantly higher due to under-reporting by sponsors.

3.19 The greater emphasis on competitive procurement is intended to deliver the following benefits:

- a A lower risk of non-compliance with regulations, especially:
  - *European Union public procurement regulations*: These regulations require contracts let by public authorities to be let by open competition according to specified procedures.
  - *State Aid*<sup>40</sup> *rules*: To avoid distorting competition between member states, State Aid is illegal unless it has been specifically approved or falls within certain exempt categories. By testing the market and paying the market price through competitive procurement, WEFO minimises the risk that any contractor will be deemed to have received illegal State Aid.
  - *European Commission rules governing the eligibility and accuracy of expenditure*: Once a service has been procured, the contractor's own expenditure does not normally need to be audited. In contrast, project expenditure by grant recipients is fully covered by the rules<sup>41</sup>.
- b Improved and demonstrable value for money, because services are provided after testing the market for the most appropriate suppliers.
- c Wider access to the opportunities provided by EU funding to the private sector and, potentially, to the voluntary sector (although the voluntary sector benefited previously from grant funding and is less familiar with competitive procurement as a source of funding).

<sup>39</sup> A competitive procurement exercise tests the market for suppliers of clearly specified services, tenders are evaluated using pre-defined criteria, and contractors are free to make a profit. Competitive grant schemes award grants to a smaller range of organisations, usually with extensive flexibility as to the form of provision, and rules and procedures are often simpler than for procurement. Grant awards are evaluated against pre-defined criteria. However, grant recipients cannot make a profit from the grant.

<sup>40</sup> State Aid means any subsidy given from state resources (public funds) to any organisation for undertaking a particular economic activity that is traded between member states of the EU.

<sup>41</sup> Grant recipients must keep very detailed records to show that all expenditure is eligible and correctly calculated which often involves the use of timesheets to apportion costs. These requirements are complex, onerous and prone to error. Compliance is audited by a project's external auditor and potentially by WEFO and the Audit Authority too.

**The greater emphasis on competitive procurement has been difficult to implement although some of the early challenges have been overcome**

- 3.20 When the programmes were launched in 2007, WEFO's policy on procurement was not clear to some sponsors and formal guidance was not published until 2008. Even then, many sponsors complained to WEFO that the guidance was unclear. WEFO's 2009 customer satisfaction survey revealed a lower level of satisfaction for advice on procurement and State Aid issues than for other aspects of project development, and similar concerns emerged from our own fieldwork and from WEFO's process evaluation in 2011. Complaints centred on ambiguous advice and frustration at not being able to access Welsh Government procurement expertise directly.
- 3.21 WEFO did not employ its own procurement specialists for the current programmes and had to seek legal advice on the procurement and State Aid risks on a case-by-case basis. Some project sponsors had to re-design their business

plans to adopt a procurement approach, causing difficulties where joint sponsors may have been expecting to deliver services directly. In addition, many project sponsors faced practical difficulties in adopting suitable procedures for competitive procurement due to a lack of expertise or simply because they under-estimated the work involved, leading to considerable delays (Exhibit 19). WEFO has no obligation under European regulations or guidance to provide support for sponsors for procurement or any other management function. Indeed, it is important for WEFO to remain independent of project delivery so as not to compromise its official oversight function. Nevertheless, acting on a recommendation in the Guilford Review, for the next programming round WEFO has decided to enable a degree of arm's length procurement support for those sponsors that, in WEFO's view, might reasonably find the process to involve unsupportable overheads. WEFO's view remains, however, that sponsors in the private and public sectors should have their own procurement capability and not require specialist support.

**Exhibit 19 – Problems faced by sponsors when implementing procurement requirements**

Project sponsors told us about several examples of practical difficulties they faced in establishing effective procurement practices in their projects:

- Difficulties in recruiting staff with the desired skills and experience and delay in training tender assessors.
- Bidders – mainly small voluntary organisations unfamiliar with procurement as a funding route – found it hard to adjust to procurement requirements, with many failing at the due diligence stage because of technical failings unrelated to the underlying quality of their bid, such as not having a data protection policy.
- Reluctance of voluntary organisations to commit to legally binding contracts, leading to delays in commencing delivery.
- Sponsor used competitive dialogue, a process by which a final bid is developed through several iterations until it meets the buyer's objectives. However, the technique is more often used for large capital projects and proved impractical and time consuming, leading the sponsor to switch to a more conventional approach.
- Sponsor did not run a pre-qualification exercise (standard practice for large procurement exercises to restrict the number of full tenders) and had to assess over 200 full tenders. The sponsor subsequently hired procurement consultants to develop a process that included a pre-qualification stage.

Source: Wales Audit Office case studies

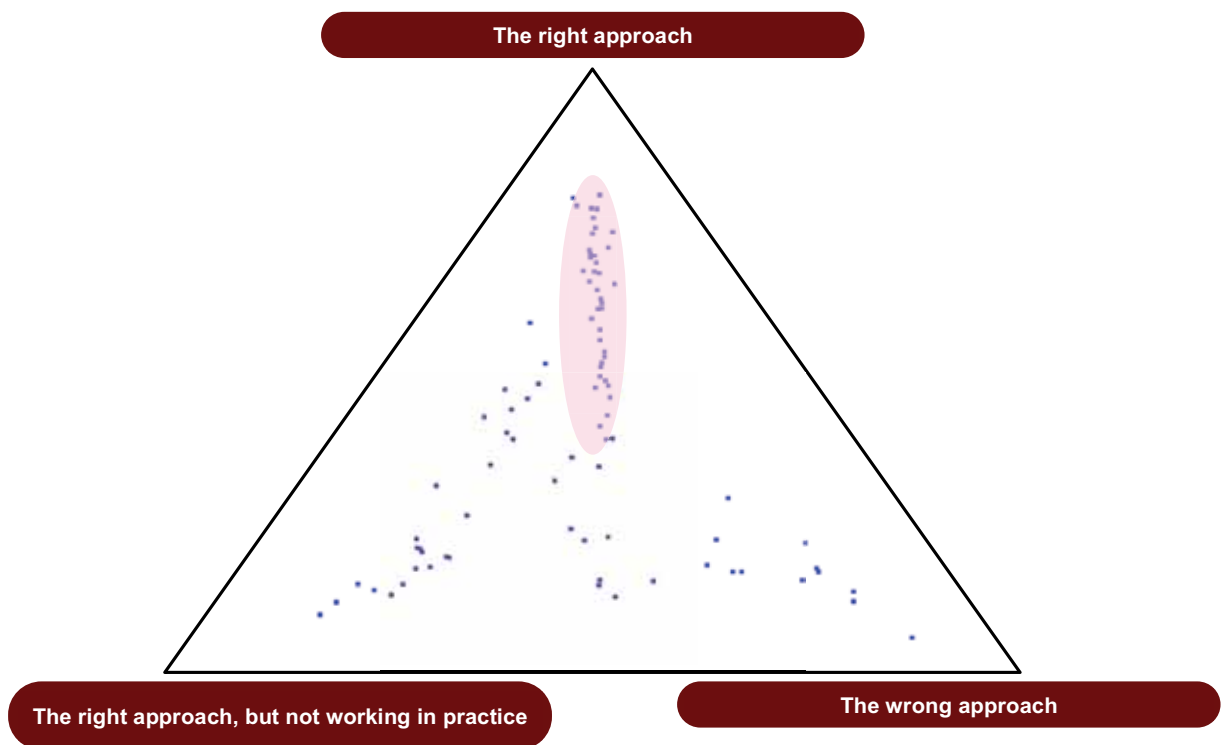
- 3.22 Match funding with procurement has been a particular challenge for some projects. These projects have required bidders to contribute match funding to help meet the overall cost of the project. This raises the risk of cross-subsidy – that European grant paid to the contractor as part of its profit margin is returned to the project as match funding – which would contravene WEFO guidance. Contractors who provide match funding are therefore subject to full procurement and record-keeping requirements as if they were grant recipients. These requirements remove the principal benefits of procurement for delivery agents (profit and streamlined administration) and have made certain contracts largely inaccessible to commercial businesses, since they do not have the resources or the mandate to provide match funding.
- 3.23 Some sponsors have complained about what they felt were unduly onerous procurement requirements, including guidance on the use of the ‘buy4wales’ website run by Value Wales (the procurement arm of Welsh Government). Value Wales guidance recommends only that contracts over £25,000 in value should be advertised on buy4wales. WEFO guidance required project sponsors to advertise all contracts through buy4wales regardless of their value. While the guidance permits other forms of advertising where buy4wales is ‘not the best mechanism’, exactly what this means in practice is not made clear. In reality, project sponsors appear to have felt obliged to procure through buy4wales for even the smallest contracts.
- 3.24 WEFO issued clearer guidance on delivery models in 2010. While there has been no fundamental change in approach, WEFO has modified its guidance to allow competitive grants in a wider range of circumstances. As a result, several projects have switched from procurement to joint sponsorship or grants, which they have found much simpler and easier to use. One notable change has been WEFO’s decision to allow the Wales Council for Voluntary Action (WCVA) to adopt a competitive grant scheme for its Engagement Gateway projects<sup>42</sup> from March 2011. WCVA reports that the switch in approach has substantially increased the number of applications and dramatically reduced the time between the selection of successful bidders and the conclusion of legal agreements, as the organisation returned to a familiar and less bureaucratic process.
- 3.25 Despite the challenges, our survey of project sponsors and project development officers indicated that a majority of both project sponsors and project development officers supported the move towards competitive procurement in principle, although a significant number felt it was not working in practice (Exhibit 20).

<sup>42</sup> The Engagement Gateway is a scheme run by the WCVA that provides grants to voluntary organisations to help individuals outside the labour market to become more employable and, if possible, find paid work.

**Exhibit 20 – Survey respondents' views on competitive procurement**

The survey asked respondents to choose a position between the three statements below. The dots show the number of responses and the shaded area indicates the greatest concentration of responses. The results indicate the balance of opinion among responses and are not intended to be analysed quantitatively.

**Formal competitive procurement as the normal way to select delivery agents for projects is:**



*Source: Wales Audit Office survey of project sponsors and project development officers. Each dot represents one respondent.*



**WEFO has achieved a high level of compliance with procurement regulations, but the extent to which the increased emphasis on competitive procurement has delivered better value for money and wider access to EU funding is less clear**

- 3.26 To date, WEFO has achieved a high level of compliance with EU procurement and State Aid regulations across the 2007-2013 programmes. In contrast, the European Commission has reported that procurement has, more widely, been a major cause of error across EU expenditure on Structural Funds, leading to large financial penalties for some member states. Procurement compliance issues were also a significant cause of error in the 2000-2006 programmes in Wales.
- 3.27 WEFO's 2011 process evaluation found that most project sponsors interviewed thought it was too early to judge whether procurement had improved value for money<sup>43</sup>. However, several believed that testing the market through procurement had had a positive impact on service quality, for example by enabling the project to recruit a greater range and depth of expertise. A few sponsors also reported that the emphasis on competitive procurement had resulted in a more outcome-focused culture.
- 3.28 Project sponsors had issued almost 2,600 procured contracts worth a total of £1.09 billion by the end of 2013, of which £644 million had gone to the private sector (Exhibit 21). The value of these contracts far exceeds the £22 million of EU funding awarded to project sponsors in the private sector. Direct comparisons with the 2000-2006 programmes are not possible because data on contracts was not collected, but it seems

likely that the extension of procurement as a delivery model has enabled the private sector to deliver a greater proportion of programme funding.

- 3.29 The extent to which SMEs or Welsh-domiciled businesses have been able to benefit from the programmes by partaking in their delivery (as opposed to receiving support as a direct beneficiary) is less clear. WEFO reported to the National Assembly's Finance Committee in September 2012 that 78 per cent of contracts let under the programmes had gone to firms with an address in Wales, but the number of contracts issued to firms head-quartered in Wales, as well as the proportion of programme expenditure accounted for by such contracts, could be significantly lower. WEFO does not routinely monitor the number or value of contracts or sub-contracts going to SMEs or Welsh-based businesses<sup>44</sup>.
- 3.30 Many of the larger sponsor organisations have their own policies to encourage SME participation in public procurement and WEFO's guidance asks sponsors, as a minimum, to complete a sustainability risk assessment based on Value Wales guidance<sup>45</sup>. This guidance requires the sponsor to consider opportunities for SMEs to deliver the contract and to consider practical measures to help SMEs apply. The sustainability risk assessment also promotes the adoption of measures relating to the cross-cutting programme themes of environmental sustainability and equality of opportunity. However, WEFO does not monitor the extent to which such measures are adopted for EU-funded contracts.

<sup>43</sup> Generally, comments about procurement in our own survey of project sponsors and WEFO project development officers focused on the difficulties that had been faced applying competitive procurement rather than perceived benefits. Any short-term assessment of value for money benefits arising from competitive procurement needs to take account of the difficulties that have been experienced in implementing that approach.

<sup>44</sup> In August 2012, the Welsh Government commissioned 'McLelland Review' reported that the Welsh public sector as a whole had made good progress in tackling many barriers to SME participation in public procurement. The review found that the value of contracts going to companies with a base in Wales had increased from around 30 per cent in 2005 to 52 per cent in 2010-11, but concluded that performance was inconsistent across Wales and further progress was possible. John F McLelland CBE, *Maximising the Impact of Welsh Procurement Policy*, August 2012.

<sup>45</sup> While it is illegal under EU public procurement regulations to discriminate against suppliers on the basis of nationality or locality, there is a lot that can be done within the regulations to help locally based SMEs secure contracts.



Exhibit 21 – Procurement contracts let by project sponsors as at 31 December 2013

	ERDF	ESF	Total
<b>Number of contracts</b>	<b>1,196</b>	<b>1,373</b>	<b>2,569</b>
Of which: Public sector	9%	17%	13%
Private sector	86%	45%	65%
Third sector	5%	38%	22%
<b>Total contract value (£ million)</b>	<b>£565.3 million</b>	<b>£521.5 million</b>	<b>£1,086.8 million</b>
Of which: Public sector	13%	37%	25%
Private sector	75%	42%	59%
Third sector	12%	21%	16%
<b>Average contract value (£000)</b>	<b>£473</b>	<b>£380</b>	<b>£423</b>

Source: WEFO

3.31 As at 31 December 2013, project sponsors had let contracts valued at £178 million (around 16 per cent of the £1.09 billion total value of contracts awarded at that time) to voluntary organisations. In addition, at 31 December 2013 WEFO had approved projects with a total cost of £185 million (£102 million EU funding) to third sector organisations.<sup>46</sup> The voluntary sector delivered a substantial part of the 2000-2006 programmes and it is not clear whether its overall participation in the 2007-2013 programmes has decreased. The transition to more competitive procurement has also been more difficult for the voluntary sector and the cultural shift from partnership (emphasised in the previous programmes) to competition created some uncertainty about the extent to which organisations could cooperate during the bidding process.

3.32 The average contract value was £388,000 for the private sector and £308,000 for the voluntary sector for the period to 31 December 2013. The relatively modest size of many contracts is likely to have made the majority of contracts accessible to most SMEs and voluntary organisations, subject to their ability to comply with tender requirements.

<sup>46</sup> The £185m will include money passed on to other voluntary organisations in the form of procured contracts.

## WEFO has established a robust system to support project development and selection but sponsors can find the process challenging and time consuming

### WEFO has effective mechanisms for ensuring that projects align with strategic objectives, but there is scope to develop a more sophisticated approach for the next round of programmes

3.33 The strategic frameworks that support the operational programmes are one mechanism through which WEFO seeks to ensure that projects address the strategic objectives of each programme. The purpose of the strategic frameworks is twofold: to guide project sponsors in developing projects that meet the programmes' strategic objectives, and to help WEFO select and prioritise projects. Each framework has a strategic framework coordinator who is a Welsh Government official outside WEFO responsible for developing, reviewing and promoting the framework in consultation with partners.

3.34 Our survey findings indicated that project sponsors and WEFO project development officers had a generally positive view of the fit between the programmes and other official policies and strategies, but some felt that the programmes were not always well aligned to local needs. However, a more detailed assessment of local needs would greatly lengthen the strategic frameworks and require more regular updating.<sup>47</sup>

3.35 WEFO's 2009 customer survey found that 94 per cent of respondents used the relevant framework to prepare their applications and 77 per cent found it easy or very easy to determine the relevant framework for their project. WEFO's 2011 process evaluation reported that the strategic frameworks had been invaluable in helping project development officers assess project applications, especially in the early stages of the programmes. The process evaluation also found that the frameworks had helped guide project sponsors towards desired areas of activity and that many stakeholders thought the frameworks had helped establish a more collaborative approach, although they were not the main influence.<sup>48</sup> However, the evaluation concluded that the frameworks had not, in themselves, fundamentally altered project design and that they had not played a major role in targeting activities towards particular locations.

3.36 The Welsh Government reviewed all the strategic frameworks in 2009 and further changes to some frameworks were made in early 2011. While the process evaluation recommended that they be maintained, the strategic frameworks are seen by many key stakeholders as having served their purpose, and play no significant role in WEFO's on-going programme management and monitoring. We found that some framework coordinators were unclear about the scope of their responsibilities and did not see ongoing monitoring as part of their role, or considered that they did not have the time to undertake such duties. Overall, we found that the coordinators of the smaller thematic frameworks were better engaged with WEFO than spatial framework coordinators.

<sup>47</sup> Only the spatial strategic frameworks specify local priorities or projects in any detail; the thematic frameworks each have a section on the 'spatial context' which identifies needs and priorities at a high level and is of limited practical use when designing projects.

<sup>48</sup> The main influences being existing Welsh Government policies, other relevant evaluations, experience with the previous programmes, early messages from Ministers emphasising the need for collaboration and the efforts of WEFO officers during the project selection process.

- 3.37 Several of the framework coordinators that we interviewed commented on the information available from WEFO to track the progress of the frameworks. Most received information on projects approved and in the pipeline, but not on their progress in terms of expenditure and outputs. Consequently they were not always aware of any problems, for example delays, gaps in provision or duplication in activity.
- 3.38 Acting on a recommendation from the Guilford Report, WEFO is developing an *Economic Prioritisation Framework* to support the targeting of the 2014-2020 programmes on key areas of economic opportunity. The draft framework, published in November 2013, lists the main areas of opportunity, existing and planned investments in each area, and the potential for using Structural Funds to maximise the impact of these investments. The aim is help sponsors develop projects that will improve the synergy between existing investments in the Welsh economy and the Structural Funds, thus maximising the impact of the programmes through a more targeted approach. WEFO intends to update the framework regularly to reflect the changes in the economic and strategic context, emerging economic opportunities and progress made on the implementation of the EU programmes.
- WEFO has established a robust system to select projects based on sound criteria, which has improved the quality of project proposals**
- 3.39 WEFO adopted a new approach to prioritise, develop and select projects for the 2007-2013 programmes. Compared with the previous programmes, there is now much closer engagement between the project sponsor and WEFO to help sponsors develop high-quality proposals that meet the requirements of a more demanding assessment regime.
- 3.40 WEFO encourages potential applicants to publish their project ideas on WEFO's website and to collaborate with other interested parties (the pre-expression of interest stage) and considers proposals at an early stage through an expression of interest<sup>49</sup>. The strongest proposals progress to a project development stage and are invited to submit a detailed business plan, which is then subject to further appraisal. In reality, both the EOI and business plan evolve over several iterations. The required content of the business plan (**Appendix 5**) provides a solid framework for assessing the business case of each proposal. An audit by the Audit Authority in 2010 found that procedural weaknesses (with some key documents incomplete or lacking sufficient information or explanation) identified in an earlier audit in 2009 had been addressed. The final decision to approve, reject, or hold in reserve a project is made by a senior WEFO official.
- 3.41 WEFO and the Welsh Government established several forms of support to underpin project development:
- a Starting from the expression of interest stage, WEFO allocates a project development officer to each project to act as the primary point of contact, help the sponsor develop the project and to take the lead on project appraisal.
  - b Other WEFO staff provide expert advice on the cross-cutting themes of environmental sustainability and equality of opportunity, monitoring and evaluation, financial appraisal, communications and compliance issues. Project development officers can also access Welsh Government specialist advice on estates, procurement and legal issues.

<sup>49</sup> Initially, there were two expression of interest stages but WEFO streamlined the system after employing a business change specialist in 2008 and undertaking a review of the process. That review identified inconsistencies in the approach adopted by project development officers and differences in the time taken to respond to queries or new information.

- c 'Spatial European Teams' encourage collaboration, provide independent support and advice to potential applicants during the development phase, assist sponsors during the implementation phase ('aftercare'), and advise organisations on bidding for delivery contracts in procurement exercises. These outreach functions are provided by a specialist team within the WCVA and 17 teams based in local authorities.<sup>50</sup>
  - d The Welsh Government's Strategic Framework Coordinators also provide specialist policy advice to WEFO staff and project sponsors.
  - e Written guidance is available on WEFO's website.
- 3.42 WEFO assesses project proposals by scoring them as high, medium or low against each of 12 selection criteria (**Exhibit 22**). A project does not need to reach a defined threshold to be approved, although WEFO would not approve a project with several 'low' scores or a low score for one of the key criteria assessed at the expression of interest stage. Following project approval, WEFO will use the scores to identify risks that may need to be managed as part of the monitoring process.

#### Exhibit 22 – WEFO project assessment criteria

Criteria (type)	Criteria (specific) <sup>1</sup>
<p><b>Contribution factors</b></p> <p>The likely contribution that a project will make to programme objectives.</p>	<ul style="list-style-type: none"> <li>• Fit with and contribution to agreed strategy</li> <li>• Extent of partnership engagement</li> <li>• Meeting market needs (evidence of specific market failure or gap in provision)</li> <li>• <i>Contribution to cross-cutting themes</i></li> <li>• <i>Value contribution (value for money)</i></li> <li>• <i>Legacy contribution (sustained impact beyond the funding period)</i></li> </ul>
<p><b>Certainty factors</b></p> <p>The likelihood that the project will be successfully delivered.</p>	<ul style="list-style-type: none"> <li>• <i>Achievement of projected indicators</i></li> <li>• Certainty of funding package</li> <li>• Reliable delivery plans in place</li> <li>• Organisational competency and capability to deliver</li> <li>• Clear and sustainable exit strategy</li> <li>• <i>Compliance with relevant rules and regulations</i></li> </ul>

Note:  
<sup>1</sup> Following a business process review in 2008, WEFO decided that only those five criteria shown in italics would be assessed at the expression of interest stage. All criteria are assessed during the project development stage.

Source: WEFO

<sup>50</sup> These teams, and a further five teams based within the Welsh Government, were also intended to contribute towards the development of strategic frameworks, liaise with stakeholders, raise awareness of the Structural Funds, and engage with Strategic Framework coordinators on the monitoring and evaluation of projects.

3.43 In our view, the selection criteria are comprehensive and appropriate. In particular, they represent an improvement on the much more rigid scoring system used to assess ESF projects in the previous programming round, which had a pre-defined threshold for project approval and left much less scope to exercise judgement on the merits of the project plan. In addition, the European Commission has identified WEFO's approach as an example of good practice. WEFO plans to maintain similar criteria for the 2014-2020 programming round.

3.44 Our case studies indicate that WEFO applies the 12 selection criteria flexibly but in sufficient depth to reach a broad-based judgement on the strength of each project proposal. We found several examples where the appraisal process had led to cost reductions, quality improvements or other benefits<sup>51</sup>. These included:

- a Scaling back the capital works of a new development without compromising the key benefits of a project. WEFO considered the cost per job excessive when compared with similar projects and negotiated a planned cost reduction of £1.2 million against an original construction cost estimate of £3.9 million. WEFO's also secured several changes to improve the environmental performance of the building concerned, for example through the recycling of 'grey water.'
- b Advising at an early stage on how to integrate equality and environmental sustainability into a project providing support for the marine science industry in Wales.

3.45 However, our review of WEFO's grants to AWEMA found mixed evidence on the effectiveness of appraisal procedures in that particular case. The report found that WEFO had challenged the costs of the three projects that it appraised in 2009 and 2010 and had scaled them back considerably, but had not adequately challenged the organisation's governance and capacity to deliver given previous problems with both WEFO-funded projects and projects managed by other parts of the Welsh Government.

**Project sponsors are generally satisfied with the support provided by WEFO, but some find the overall length and complexity of the appraisal process difficult to manage**

3.46 The introduction of project development officers, providing a single and continuing point of contact throughout a project's lifetime, has been broadly welcomed by project sponsors. WEFO's 2009 customer satisfaction survey found that 73 per cent of respondents were satisfied with the knowledge of their project development officer and 68 per cent were satisfied with their efficiency. Comments made by project sponsors responding to our own survey were also broadly positive, although some negative experiences were reported regarding inconsistent and inaccurate advice, a general lack of guidance, a level of scrutiny and challenge that did not take account of project sponsors' experience, and the speed of response where project development officers needed to access specialist advice from other WEFO or Welsh Government officials. WEFO's 2009 customer survey found that satisfaction rates were over 50 per cent for all of WEFO's specialist teams, with a relatively high proportion of neutral responses and very low dissatisfaction rates<sup>52</sup>.

51 Responding to our survey, one project sponsor from the higher education sector commented that: *'As a result of the interactions with WEFO during the business plan development stage, we have ended up with a far superior project to the draft project originally submitted'*.

52 Project sponsors are encouraged to direct all enquiries through the project development officer. The advice of WEFO teams for the cross-cutting themes of environmental sustainability and equality appears to have been particularly well regarded by sponsors and project development officers. Those teams have been well-resourced. Advice from other specialists has usually taken longer to obtain, often due to resource constraints. Legal advice on compliance with State Aid and public procurement regulations often took several months to finalise as discussions took place on permissible delivery models.

- 3.47 Opinions about other aspects of the support system have varied:
- a Spatial European Teams – An evaluation by WEFO in 2010 concluded that, overall and despite some concerns about capability, the outreach teams based in local authorities and the ESF team based in the Welsh Government had had a positive impact. The teams had extended collaborative working, developing stronger national and regional projects, and had helped potential suppliers bid for procurement contracts. However, the teams based in the Welsh Government had an unclear role and had not added the same value. Acting on the review, WEFO abolished these SETs and maintained support through the outreach teams.
  - b Strategic framework coordinators – WEFO's customer survey in 2009 found that 45 per cent of respondents were satisfied with the service that they received when they sought advice from a strategic framework coordinator advice and 11 per cent were dissatisfied, but such advice was sought for only 42 per cent of projects at the pre-EOI stage and 51 per cent at the EOI stage.
  - c Written guidance – WEFO's 2009 customer insight survey found that satisfaction rates varied between 39 per cent and 77 per cent depending on the specific guidance, with the lowest satisfaction for the guidance on delivery models, which was subsequently amended.
- 3.48 Changes in programme administration, with many project sponsors and WEFO staff unfamiliar with the new systems, made it particularly difficult to provide effective support during the early stages of the programmes. Some sponsors, particularly in local government and the voluntary sector, were unsure about the type of projects that would be acceptable to WEFO in terms of size, the degree of collaboration expected, and whether WEFO expected the Welsh Government rather than other organisations to sponsor projects in particular policy areas. Guidance on these matters was not always readily available. There were also some early concerns among project sponsors about the time taken by WEFO to process applications, the amount of information requested and the number of versions of business plans that they had to write to address WEFO feedback. In 2009, WEFO issued new and comprehensive guidance to sponsors and project development officers and provided training events on how to write a business plan.
- 3.49 Overall, responses to our survey highlighted mixed views about the design and operation of the system for administering the 'pre-approval' phase, although perhaps unsurprisingly WEFO project development officers were more likely to tend towards a view that the system was well designed and well run. The process leading up to project approval typically takes between at least nine months and often much longer to complete. One private sector project sponsor responding to our survey commented that, as a result of the time taken, their project was already partially complete prior to final approval and that this made it difficult to manage the finance and expectations of sponsors for swift approval of their projects.



3.50 Although WEFO monitors the number and value of projects in the pipeline, it does not formally monitor the duration of each stage of the project development and selection process. The duration of each stage is dependent to a large extent on factors outside WEFO's direct control, and WEFO therefore considers firm targets for appraisal times to be inappropriate. However, the overall efficiency of the process, and the speed with which Structural Funds are mobilised, depends to a considerable extent on the timeliness of the project development process.

3.51 While the length of the process, its administrative requirements, and the extent of feedback from WEFO during the process, have been a source of frustration for project sponsors, we have not identified any clear consensus on improvements that could be made. The process has evolved over time and, in our view, there is no need to fundamentally change the project development and appraisal system for the next programming round, although certain specific aspects of the process could be improved. This should also help to ensure a smooth transition. The Guilford Review similarly concluded that it was preferable to build on existing processes rather than make substantial changes, but suggested testing a project's eligibility and fit with identified economic opportunities at a very early stage. Acting on the recommendations of the report, WEFO plans to introduce a revised approach for the 2014-2020 programmes. Eligibility and strategic fit will be discussed with a sponsor a part of a planning phase before the formal process begins, with more detailed assessment, focusing on delivery risks, taking place once a business plan is received. The planning phase will replace the formal expression of interest and will be a structured conversation between the sponsor and WEFO on the key requirements for the project. The application may be terminated at any point

if WEFO believes that it will not fulfil essential appraisal criteria.

## Financial management is sound

### WEFO arrangements for managing programme finances operate within a framework of controls set out by the EU

3.52 The European Commission has issued detailed guidance on how financial controls should operate in practice. While not legally binding, there is a risk that the Commission would suspend payments if WEFO did not follow this guidance in any material respect. In addition, the Commission may apply 'financial corrections' (withdrawals of funding from a programme) where it discovers serious infractions of the regulations. It is therefore in WEFO's interest to identify and correct irregularities itself. WEFO also needs to pay grants on a timely basis, obtain reimbursement from the European Commission and ensure that the highest possible proportion of programme funding is spent before the programmes close. This involves managing the risk of fluctuating exchange rates and under-spending projects.

### The development of a new IT system has made it much easier for WEFO to manage the programmes' finances

3.53 To support its management of the 2007-2013 programmes, WEFO commissioned a new web-enabled IT system, known as PPIMS.<sup>53</sup> The system was introduced in June 2008 as the first projects were being developed. Some of the functionality of the system had to be scaled back initially following substantial cost over-runs, but most of these functions have now been restored and the system is working smoothly. The system enables:

<sup>53</sup> We have not examined the procurement or any other aspect of this project in detail as part of this study. Further detail on the PPIMS project is available in the Wales Audit Office report, *The Delivery of ICT Services and ICT Projects under the Merlin Contract*, August 2011 (Case Study 1, page 42).



- a applicants to submit expressions of interest, business plans and delivery plans electronically;
- b sponsors to submit grant claims electronically, with many of the calculations now automated, and receive funds much more quickly than before;
- c WEFO staff to file documents electronically in a standardised system, largely doing away with paper files, and to save time by processing grant claims and other information electronically; and
- d WEFO managers to obtain a wide range of management information more quickly than before, helping them to improve forecasting and draw down money from the European Commission more quickly than before.

3.54 WEFO estimates that the new system has led to annual efficiency savings in its own administration of just under £277,000 compared with the one-off capital cost of £18.1 million and annual running costs of around £1.25 million per year. Savings for project sponsors have not been assessed, and are difficult to evaluate given other changes that have made reporting requirements more onerous generally. WEFO considers that the main benefit of the PPIMS system has been to strengthen programme management by improving the quality and timeliness of important management information. This in turn has practical benefits for forecasting, reporting and claiming reimbursement from the European Commission. The European Commission cites the system as a benchmark for other managing authorities because of the range of functions that it has. WEFO is confident that it will be able to continue using the system for another eight years with little additional investment required.

### WEFO pays grants on a timely basis after making appropriate checks and has recently strengthened controls over advance payments

3.55 The WEFO payments team is responsible for checking claims, making payments and chasing overdue claims to ensure that programme funding is paid out on a timely basis. Payments are normally made in arrears but voluntary organisations may receive advances against future claims based on estimated expenditure. Basic verification checks are automated through the PPIMS system. There are two levels of additional checks:

- a WEFO's payments team undertakes desk checks to ensure that claims appear reasonable. Each claim is supported by a list of transactions that is reviewed for any items that may be ineligible, and since mid-2012 sample checks are made to supporting documentation to confirm that costs are genuine and have been paid.
- b Each sponsor contracts with an independent external auditor, known as a reporting accountant, to perform an annual audit and report to WEFO on the adequacy of controls and whether claimed expenditure in the period was eligible and correctly stated. The Wales Audit Office undertakes these audits for most projects. On receipt of the auditor's report, WEFO will seek to resolve any issues raised by the auditor and adjust the next payment of grant to adjust for any errors found.

- 3.56 The level of scrutiny is much higher than during the previous programming round, helped by the smaller number of projects in the current round. The Audit Authority (the Welsh Government's European Funds Audit Team, which exercises audit functions on behalf of the European Commission) has reviewed the payments system and concluded that it is effective.
- 3.57 In 2012, WEFO strengthened controls over the payment of advances to third sector organisations after losing most of the £300,000 of European funding provided to AWEMA, which became insolvent after receiving advances but not spending the money on approved project activity. This is an inherent risk with advance payments. WEFO now requires a voluntary organisation to prove that it needs advance payments in order to fund the project and had tightened approval procedures and conditions of grant to reduce the risk that funding will be lost or not passed on to contractors on a timely basis.<sup>54</sup>
- 3.58 The process of compiling a claim that meets the standards required by the regulations is quite onerous for sponsors and there is a risk that late or understated claims reduce the amount that WEFO can claim from the European Commission, affecting performance against spending targets and potentially resulting in the de commitment of programme funding. Overall, however, the record is reasonably good: sponsors make around 80 per cent of their claims on time (within three weeks of the end of the quarter to which the claim relates) and most of the rest are no more than a few weeks late. The payments team chases overdue claims regularly and pays around 90 per cent of claims within its target period of four weeks from receipt. WEFO's customer survey in 2009 found that 72 per cent of respondents were satisfied or very satisfied with the time taken to pay grant claims.
- 3.59 The 'Certifying Authority' is a division within WEFO that is responsible for submitting reimbursement requests to the European Commission after making appropriate checks to ensure that only legitimate expenditure is included. The Audit Authority has reviewed the Certifying Authority's systems and controls and is content that they are effective.
- WEFO is in a good position to manage fluctuations in the exchange rate and other financial risks as the programmes draw to a close**
- 3.60 Because WEFO makes commitments and payments to project sponsors in sterling, but is reimbursed by the European Commission in euros, WEFO realises a gain or loss based on the difference between the exchange rate when a payment is made to a project sponsor and when the EU funds are actually drawn down. These gains and losses can be considerable due to the volatility of the exchange rate and the time that elapses, which can be several months. WEFO did not start making payments until 2009, after the value of the euro had reached its lowest point and, since that time, the trend of a strengthening pound has tended to result in losses totalling £5.9 million in 2010, £6.6 million in 2010 and £5.8 million in 2011. However, WEFO made a gain of £655,000 in 2012, reflecting the benefit of a weakening pound in the second half of the year and WEFO's decision to make more frequent reimbursement requests to the European Commission. The trend continued into 2013 with exchange gains of £4.6 million expected for the whole year.

<sup>54</sup> Wales Audit Office, *The Welsh Government's Relationship with the All Wales Ethnic Minority Association*, October 2012, paragraphs 3.37 (loss of funding) and 3.49 (strengthening of controls). Paragraph 3.37 reports that WEFO paid £301,614 more than was claimed, and irrecoverable ineligible expenditure raised the total loss to around £405,705.

3.61 Should the value of the pound weaken during 2014 and 2015, WEFO could find it difficult to ensure that the programme budgets (set in euros) will be fully used by the time the programmes close in 2015. Conversely, should the pound strengthen, WEFO may have to cancel or scale back some projects or find money from Welsh Government resources to meet the full cost of approved projects. This would be difficult to deal with if it occurred at a very late stage, but WEFO could, if necessary, fund ongoing operations through the new 2014-2020 programmes provided that project approval procedures are in place. That projects have a tendency to under-spend against their original budgets, further complicates the task of ensuring that the programmes are fully spent.

3.62 WEFO's current policy is to commit more than the current sterling value of the programme allocations to allow for under-spending by projects and the implications of any significant strengthening of the value of the pound. Based on experience of the 2000-2006 programmes, WEFO plans to over-commit the ERDF programmes by five per cent and the ESF programmes by 10 per cent. The ERDF programmes have more capital projects that are considered much less likely to under-spend than revenue projects. WEFO used a similar approach successfully for the 2000-2006 programmes, ensuring that 97 per cent of available EU funding was spent despite the unexpected strengthening of the euro in the two years before the programmes closed in 2009.

**WEFO has generally effective financial management systems to ensure compliance with EU regulations, but they can be a heavy administrative burden for sponsors**

3.63 The Audit Authority has concluded that WEFO's management and control system provides for effective controls and that WEFO's organisation and procedures complied fully with the relevant EU regulations. The Audit Authority has an audit strategy that involves assessing all of WEFO's important management systems over the programming period to ensure that they are operating effectively in practice. The outcome of the systems audits to date has been good: most systems were found to be working well and recommended improvements were made within 12 months. The Audit Authority has issued unqualified audit opinions (in other words, that controls are effective) in each of its annual control reports to date.

3.64 The Audit Authority is itself subject to audit by the European Commission. The Commission issued three mostly positive audit reports for the current programmes, but has recently raised concerns over the sampling methodology used by the Audit Authority to select projects and transactions for audit testing and the basis on which it had calculated the projected error rate. In common with several other regions of Europe, the Audit Authority has hitherto used a random non-statistical sampling methodology, but the European Commission is now enforcing recently issued guidance that recommends a statistical approach based on monetary unit sampling. Work to recalculate error rates on the basis of statistical sampling is ongoing. Pending completion of this work, and as a precautionary measure, the Commission temporarily interrupted

ERDF payments to WEFO in December 2013. Latest indications are that error rates remain low overall in Wales and the Welsh Government is optimistic that the issue will be speedily resolved.

3.65 WEFO's systems include a series of 'management verifications' to ensure that projects are complying with their obligations and to detect errors before the related expenditure is declared to the European Commission. As required by EU regulations, these verifications comprise:

- a 'administrative verifications' on all claims to ensure that they are correctly calculated, match funding has been received and costs are eligible and supported by invoices; and
- b 'on the spot' verifications to confirm that projects are taking place in line with the conditions of the grant and to confirm compliance with requirements that cannot practically be assessed at claims stage, for example full compliance with procurement and publicity regulations.

3.66 The administrative verifications comprise the work of the Payments Team and external auditors, known as reporting accountants (usually the Wales Audit Office) acting under WEFO's instructions. WEFO's project inspection and verification (PIV) team undertakes the 'on the spot' verifications. The PIV team also reviews the sponsor's system of controls and tests transactions in a similar way to the external auditors. The PIV team aims, over the programming period, to visit the first project of each project sponsor and to assess 50 per cent of the remaining projects on a risk-based sample basis. The PIV team has strengthened its procedures and is in the process of up-skilling staff in response to criticism from auditors

about its sample selection, documentation, quality of work and procedures for following up recommendations.<sup>55</sup> In addition, the PIV team now reviews general financial controls, governance arrangements and financial viability in those projects in which WEFO has identified a specific risk in these areas.

3.67 In addition, the Audit Authority audits a sample of projects each year to confirm that expenditure claimed by WEFO is valid and correct. The sample covers all projects that account for more than two per cent of the funds drawn down by WEFO and at least 10 per cent of other projects. The EU's own auditors and the European Court of Auditors may also audit WEFO's management systems and individual projects, although such audits are uncommon and much less extensive than the work of the Managing and Audit Authorities.

3.68 These controls are supplemented by extensive written guidance and by training courses for project sponsors on the audit process and how to comply with the main regulations. Training was originally restricted to Welsh Government staff but has since been extended to other sponsors.

3.69 The qualification rate – the rate of errors or potential errors found by reporting accountants – was 0.44 per cent of audited expenditure up to 30 September 2013, an encouraging reduction from the 1.09 per cent when the figures were first reported in August 2011. This was the residual error rate once any corrective work, which is sometimes extensive, had been undertaken. The total error rate identified by WEFO's management controls was 0.65 per cent up to the end of September 2013. Common problems found in management verifications<sup>56</sup> include:

<sup>55</sup> Concerns raised in reports by European Commission auditors (November 2009) and the Audit Authority (April 2010). A follow-up report by the Audit Authority in June 2010 found that the recommended improvements to procedures had been made, and the team was assisting most of its staff to obtain professional audit and accountancy qualifications.

<sup>56</sup> WEFO's Delivery and Compliance Group, report to the Programme Monitoring Committee, June 2013.

- a **Ineligible expenditure:** relatively small amounts claimed for services that are not covered by the Programmes or for payments that had not been made or were outside the project period.
  - b **Indirect costs** calculated incorrectly. The process of apportioning overheads to projects can be complicated and must be done using a method approved by WEFO, with overhead rates updated throughout the project. WEFO has tried to simplify the process for sponsors by approving flat-rate overhead costs for sponsors in the higher education sector [and plans to extend this practice to other sectors].
  - c **Timesheets** are required to support the costs claimed for staff who work part-time on a project, but are sometimes not kept, meaning that the related staff expenditure is deemed to be ineligible.
  - d **Document retrieval:** there has been an increasing problem of projects failing to retain all the documents that are needed to support their grant claims.
- 3.70 Recently, WEFO has identified an emerging problem of some sponsors not being able to provide adequate evidence that they have complied with EU procurement regulations, and some others not being able to support their claimed outputs. Nevertheless, the overall error rate is relatively low and the problems outlined above do not reflect fundamental weaknesses that would jeopardise the delivery of the programmes. The management verifications are effective in reducing the rate of errors in expenditure declared to the European Commission (i.e. after correction of errors found by reporting accountants): the projected error rate identified by the Audit Authority's testing

of project expenditure was only 0.36 per cent for 2012 (the latest year for which figures are available), a reduction from 0.46 per cent for 2011 and well below the materiality threshold of two per cent set by the European Commission. This position contrasts favourably with managing authorities elsewhere in the UK and the EU, some of which have suffered suspensions of payments and/or major financial penalties because of errors found by audit authorities. The current programmes have not been the subject of any financial corrections to date, unlike the previous programmes for which financial corrections of around £19 million in grant were made by the European Commission in 2005<sup>57</sup>.

- 3.71 While WEFO's system of financial control is effective, it imposes a heavy administrative burden on sponsors. The requirements are significantly more demanding than for wholly Welsh Government-funded programmes and the audit regime is more stringent. For example, the Audit Authority checks compliance with public procurement regulations in much greater depth and any infractions identified by the European Commission attract a fixed financial penalty for the relevant managing authority, which may be passed on to the sponsor.
- 3.72 Our survey of project sponsors and PDOs indicated some frustration among sponsors with the nature and extent of the rules and the time-consuming audit and inspection processes. Several respondents commented on the difficulty of getting useful and timely answers from WEFO on compliance questions, for example on whether particular costs were eligible. The survey responses indicate that both sponsors and WEFO are anxious about making a wrong decision that could result in funds being reclaimed by the EU, but the resulting caution can lead to frustrating uncertainty and delay.

<sup>57</sup> A financial correction is a reduction in grant claimed from the EC to reflect errors or procedural weaknesses. The correction may be requested by the managing authority itself, in which case the total funding available is not reduced and the money lost through the correction can be recycled into other projects, or imposed by the European Commission following an audit, in which case the funding allocation for the programme is normally reduced. In 2005 WEFO self-reported and the EC accepted the correction without reducing the funding available to the programmes.



- 3.73 There was also some concern about the duplication of audit procedures by the PIV team, the external auditors and the Audit Authority. While the focus and purpose of each of these control mechanisms is different, they all involve assessment of controls and many of the tests they perform are the same or similar. The largest projects will be audited at least twice each year, once by the Audit Authority and again by the project's own reporting accountant. Other projects will be audited by their reporting accountant annually but are much less likely to be inspected by the Audit Authority or the PIV team as part of their sample testing of expenditure.
- 3.74 WEFO's scope to resolve this duplication and to reduce the overall administrative burden is constrained by the EU regulations and the guidance produced by the European Commission. Nevertheless, there is some scope to reduce overlap. For example, the tests undertaken by the payments team since 2012 (introduced following a recommendation by the Audit Authority) duplicates some of the work done by the reporting accountants. The guidance specifies the type of management verifications that need to be done, but it does not specify that they need to happen more than once. It should be possible, therefore, to reconsider how this recommendation for an improvement in front-line controls can be implemented so that inspection work is not in danger of being duplicated.
- 3.75 In response to WEFO's consultation in February 2013 on implementation arrangements for the next programming period, we suggested a number of practical measures to improve the audit regime arising from our experience as reporting accountants, such as tailoring the level of testing more closely to risk, better exchange of information between WEFO and the reporting accountants, and ensuring the timely provision of training to all appropriate staff at project sponsors.

## Performance is better managed than under the previous programmes but could be tighter in some respects

- 3.76 WEFO has a clear system to manage performance at the programme level. The Programme Monitoring Committee meets three times a year to consider overall progress and receives comprehensive reports covering the progress against commitment, expenditure and output targets for each programme and any 'significant implementation issues', such as the challenge of managing exchange rate risks and ensuring that sufficient match funding is available. Indicator data is reported in great detail, but the monitoring reports do not assess the results in depth, for example to consider the extent to which the programmes are succeeding in increasing participation among disadvantaged groups.
- 3.77 Day-to-day management is the responsibility of the Programming and Performance Board, which comprises the Director of WEFO and four other senior WEFO officials. The Board reviews progress against the main performance indicators at both a programme and project level, including consideration of any irregularities identified through audit and inspection work, and makes operational decisions on the management of the programmes. Key decisions are subject to Ministerial approval where appropriate.
- 3.78 The Project Development Officer takes the lead in monitoring the progress of individual projects. WEFO guidance stipulates that an inception meeting should be held with each sponsor within three months of project approval followed by regular progress reviews no more than six months apart. The review process may ultimately result in funds being withdrawn from a project if it is consistently under-performing and unlikely to recover ground before the end of the programmes.

3.79 WEFO makes frequent use of special conditions in grant approval letters to deal with risks that are specific to a particular project. For example, WEFO might require an interim project evaluation or make approval for a capital project subject to planning consent or an environmental assessment. Special conditions are monitored as part of the project review process and help WEFO to manage project risks effectively by highlighting key issues for the project sponsors and WEFO officials.

3.80 Overall, performance management is more robust at a project level than the previous programmes, where WEFO did not have the capacity to closely monitor the progress of the many projects that came to exist over the life of the previous programming round. However, our review of project files indicated that problems with slow progress in delivering projects was not always adequately explained or consistently recorded on PPIMS during the early stages of programme delivery in 2009 and 2010. Inception and progress meetings were not always held within the timescales envisaged in WEFO's own guidance and progress reports did not explain in any detail the reasons for project slippage and how the situation would be recovered. In some cases, action by WEFO was restricted to asking the project to re-profile their expenditure and outputs to account for slippage, and some projects re-profiled several times until WEFO decided to limit re-profiling to twice during a project's lifetime.

3.81 Nevertheless, matters appear to have improved as WEFO's systems and projects themselves have become better established. A report by the Audit Authority in December 2011 found that system of progress reporting and monitoring was essentially sound but recommended improvements in documentation and more regular

monitoring of special conditions with a long time-span.<sup>58</sup> In its response to the Auditor General for Wales' report on AWEMA, in which similar issues were raised, WEFO undertook to review the application of its guidance and to ensure that all substantive contact was recorded consistently. This is important as the frequency of meetings may be reduced if projects are well established and performing well, or communication may be in writing rather than face-to-face.<sup>59</sup>

### **WEFO has strengthened monitoring and evaluation arrangements and developed more robust approaches to measuring impacts, but data quality remains a concern**

**There is clear accountability for monitoring and evaluation, with appropriate expertise and resources**

3.82 WEFO has developed a Monitoring and Evaluation Strategy for the 2007-2013 programmes that is supplemented by an evaluation plan that is regularly updated. The key features of the strategy are:

- a Regular monitoring of outputs and results at programme level.
- b Programme level evaluations, focusing initially on processes and systems, and later on the effectiveness and impact of activities.
- c Strategic framework and project-level evaluation. Each strategic framework will be required to implement a monitoring and evaluation plan, while all projects will be required to undertake their own evaluations in accordance with a business plan agreed with WEFO.

<sup>58</sup> The Auditor General's report on AWEMA also noted that special conditions were recorded as open on WEFO's project management system long after they should have been closed.

<sup>59</sup> Welsh Government, Written evidence for the Public Accounts Committee on the Wales Audit Office's Report on the Welsh Government's relationship with the All Wales Ethnic Minority Association (AWEMA), Public Accounts Committee of the National Assembly for Wales (PAC (4) 28-12 paper 1), December 2012.



- d Resources in the form of a dedicated Research, Monitoring and Evaluation (RME) team, which includes several staff with specialist research skills. WEFO has also established an independent group of experts, the Evaluation Advisory Group, to advise and assist WEFO in undertaking these functions. Evaluations are part-funded by the Structural Funds: in the form of technical assistance for programme-level evaluations, and as an allowable cost for project evaluations.
- e Specific reports required by the European Commission for each programme. These include an ex-ante evaluation (an assessment of the socio-economic needs of the area at the start of the programming period), annual implementation reports covering prescribed topics, and an ex-post evaluation summarising the effect of the programmes.

**There is a coherent set of indicators for measuring the success of the programmes at each stage of development but the full employment impact of the programmes is not captured**

3.83 Effective evaluation depends largely on access to reliable data about the outputs and results of the programmes as they are delivered. WEFO has also agreed a series of impact indicators with the European Commission to complete the 'logic chain' (outputs leading to results, leading to impacts) to measure the long-term impact of the programmes. The indicator set provides a comprehensive framework for assessing the progress and impact of the programmes at each stage. A study in 2010<sup>60</sup> concluded that 'WEFO's monitoring data represent a valuable source of data for undertaking some sophisticated evaluation work, in particular at project level' and

that the structure and content of the monitoring database 'appears to be comprehensive and is continuously improving.'

3.84 WEFO has reduced the number of indicators considerably compared with the previous programmes, in line with European Commission guidance that a streamlined indicator set is more manageable for project sponsors and more likely to yield consistent, high quality data. The smaller number of indicators does not fully capture the progress or impact of the diverse range of activities funded, especially for the ERDF programmes. For example, physical regeneration schemes are often multi-faceted projects and certain aspects, such as environmental improvements, will not be captured by the approved indicators. European Commission guidance emphasises the importance of projects using their own indicators, in addition to those prescribed by the operational programmes, to assess how well they are meeting objectives.

3.85 WEFO has clearly defined most of the monitoring indicators in published guidance, including setting out related record keeping and reporting requirements. Definitions have been tightened for some indicators for the current programmes to set minimum levels of provision and prevent inflated claims on project outputs; for example, a project cannot count a business against the 'enterprise assisted' indicator unless it has provided at least £2,000 worth or 14 hours of support. The guidance remedies a weakness noted in evaluations of the 2000-2006 programmes, when many projects were uncertain about indicator definitions and evidence requirements.

<sup>60</sup> DTZ Consulting, *A feasibility study of methodological approaches to undertake impact evaluation of 2007-13 Structural Fund Programmes in Wales*, report commissioned by WEFO, September 2010 (p102 and p104).

- 3.86 A key indicator for the ERDF programmes is jobs created, as both a result (gross jobs created) and an impact (net jobs created, after adjusting for the effect of external factors). As in the previous programmes, there are some problematic issues with jobs created:
- a It is not always clear whether jobs have been achieved through Structural Funds support, especially for business support projects which account for around 80 per cent of jobs attributed to the programmes. Sponsors count all jobs created by business start-ups and most other jobs created by firms that have received advice or financial assistance. The RME team reviews the data submitted by sponsors and removes claimed jobs that do not appear to be realistically attributable to ERDF although it is still likely that a significant proportion of the remaining jobs would have been created without ERDF support. WEFO uses the ERDF Business Survey to assess the net impact of the Funds.
  - b WEFO does not count jobs safeguarded, temporary jobs that are expected to last less than 12 months, or jobs in project administration; and until March 2012 did not count fixed term appointments of more than 12 months on the basis that the Structural Funds aimed to create sustainable, permanent jobs. These restrictions mean that, other factors being equal, the full effect of Structural Funds on overall employment will not be captured by the indicators. The ERDF Business Survey in 2012 found that the number of safeguarded jobs was significant, while temporary jobs (eg, in construction) and jobs in project administration are also likely to be as significant. Subsidised job placements provided by ESF projects may also have a sizeable impact on overall employment levels, albeit temporary. It is important, however, to measure these categories of jobs separately as they are of variable social and economic value, with new permanent employment having the highest value.
  - c The quality and sustainability of employment is not measured on an ongoing basis, although quality is assessed through evaluation. Sponsors must report on each post (not the individual who fills the post), which is appropriate, but there is no check to ensure that the post is sustained, for example that it still exists after 12 months. Salary information is required as a proxy for job quality but skill level is not reported.
- 3.87 The profit benefit indicator was introduced for the current programmes to measure the additional profit arising from savings or productivity benefits achieved with EU support. However, performance has been disappointing, and WEFO attributes this largely to difficulties in measuring profit benefit – figures will often depend on estimates and accounting judgements – and a reluctance on the part of small businesses to pay for professional help in calculating the profit. More detailed guidance with specific examples would be helpful to encourage beneficiaries and sponsors to measure profit consistently and comprehensively. An alternative indicator like gross value added or increase in turnover might be more easily measurable for most beneficiaries and would better capture the financial benefit of general business support.

- 3.88 Result indicators for the ESF Convergence public service reform measures are inconsistent with other results indicators as they are more akin to outputs than outcomes. For example, the indicators include participants completing courses, progression schemes for women, secondment placements, workforce planning and development strategies developed.
- 3.89 Several ESF projects are designed to improve the employability of participants and this often involves developing personal attributes such as confidence, self-esteem, interview skills and softer workplace skills such as communication and teamwork that are not captured by the 'hard outcomes' measured by the monitoring indicators. Such improvements or 'soft outcomes' may not lead to 'hard outcomes' such as employment or qualifications immediately, but it is expected that they will do so in due course.
- 3.90 Soft outcomes can be difficult to measure but WEFO has a target that 50 per cent of ESF projects in the relevant Priorities<sup>61</sup> should use soft outcome measurement systems. However, at the end of 2013, only 14 of the 50 approved projects had such systems in place. Furthermore, WEFO does not require a measurement system to cover all relevant activities within a project. An independent evaluation of ESF Convergence Priority 1 in 2012 found that missing data and inconsistent use of measurement tools (both between and within projects) made it difficult to assess soft outcomes, although participants had highlighted significant benefits to their confidence and softer skills.
- 3.91 WEFO reports against the tracking indicators (for example, overall employment and unemployment rates in the programme area) in each Annual Implementation Report. The tracking indicators have limited value as a monitoring tool because it would be misleading to compare gross monitoring data (rather than net impact data) with changes in each tracking indicator, which are caused by a wide range of factors. However, it would be more valuable to compare estimates of net impact derived from evaluation with the movements in the key tracking indicators to assess whether the programmes have made a significant positive contribution to socio economic trends.
- WEFO has improved the collection of monitoring data but some aspects of data quality remain a concern**
- 3.92 **Data is collected on a consistent basis for all projects.** Projects are required to select all relevant indicators in the operational programme for the priority under which they are funded, thus ensuring that information is collected on a consistent basis across the programmes. Data on both outputs and results are collected regularly and reported to WEFO by project sponsors using WEFO's online claims system, which is connected to PPIMS and enables efficient data collection and analysis. All output data for projects run by the Department of Economy, Science and Transport is drawn from a single database that was re-designed at around the time the 2007-13 programmes were launched, and the system uses the same definitions for outputs and results as those specified for the EU programmes.

<sup>61</sup> ESF Convergence Priority 1 (supplying young people with skills for learning and future employment) and ESF Convergence Priority 2 and ESF Competitiveness Priority 1 (increasing employment and tackling economic inactivity)

**3.93 The accuracy of monitoring data is audited by WEFO's project inspection and verification team and indicates that reported data is accurate at project level, but problems remain in some respects of data quality:**

- a **The quality of participant level data:** WEFO now requires projects to submit information about each organisation or individual supported by the programmes. These details include the age, gender and labour market status of ESF participants and the size, ownership and staffing of companies supported by ERDF. However, the quality of detailed records is variable and many of the necessary details are missing or inaccurate. This has made it problematic to analyse monitoring data by category of participant or business and has hampered the conduct of the ERDF Business Survey because it has not been possible to match assisted companies to databases maintained by other Government departments.
- b **Double counting of outcomes:** evaluations for the previous programmes found that double-counting was a significant concern because many beneficiaries received support from several EU-funded projects, and there were no controls to prevent each project claiming the same outcome. WEFO has issued guidance to ESF projects where individuals take part in more than one ESF project. Each project should count all their participants, but only one project may claim for the same result (eg, a qualification gained or entry into employment) and the relevant

projects need to liaise to establish which one claims the outcome. However, the mechanism for enforcing this guidance at project level is unclear. There is no guidance for ERDF projects, although the risk for business support projects, where firms may receive support from several sources, is similar to that for ESF participants. The participant database should allow WEFO to identify and correct double-counted outcomes, but the work is likely to be laborious especially if data quality is poor. At present the extent of double counting is unclear.

- 3.94 WEFO has developed its own participant and business databases from the records provided by sponsors, which may be uploaded from spreadsheets or from links with the bigger sponsors' own databases. Whilst the databases function reasonably well, a database that allowed sponsors to submit individual records directly and online would reduce administration costs for WEFO (although the initial development would be costly) and help improve data quality. An interactive database could be programmed to require all relevant details before records could be submitted and to alert sponsors if another project was claiming a result for the same individual. WEFO decided not to develop such a database at the outset of the current programmes in response to feedback from sponsors that wished to maintain existing systems that adequately met their own needs. An interactive database would need to be compatible with these systems to avoid costly double-entry of data, and would need to operate within the constraints of data protection legislation that restricts data sharing.

WEFO has strengthened evaluation arrangements, but comprehensive information on project-level impacts is likely to emerge only towards the end of the programmes

3.95 **WEFO plans a series of thematic evaluations that will cover the main aspects of programme administration and delivery.** The European Commission requires managing authorities to evaluate the programmes on an ongoing basis in response to policy and programming needs. As part of its commitment to ongoing evaluation, WEFO has commissioned:

- a A series of studies on the process and systems for implementing the programmes. These include a customer satisfaction survey; a process evaluation that looked at strategic frameworks, cross-cutting themes and communications; a review of the Spatial European Teams; and research into the feasibility of various approaches to evaluating the impact of the programmes.
- b Eight evaluations, known as priority or strategic framework evaluations, to evaluate key areas of programme activity. The interim evaluations consider the extent to which the relevant strategic frameworks are relevant to the needs of the programme area, how well the programme is working as a mechanism for delivering programme objectives and progress against monitoring indicators. Two interim evaluations and a synthesis of the remaining evaluations was published in 2013. The interim reports will be followed by final evaluations towards the end of the programmes which consider impact in more depth than is possible at interim evaluation stage.

3.96 In addition to these programme evaluations, all projects are required to undertake their own evaluations, which must be commissioned from an independent and external source if the project receives more than £2 million in grant or is otherwise considered high risk. The vast majority of projects will, therefore, need to commission external evaluations, in contrast with the previous programmes when most projects did not commission external evaluations and many did not evaluate at all. Some larger projects are asked to provide interim evaluations as a special condition of their grant approval letter, but WEFO does not always enforce such conditions effectively. At 31 December 2013 WEFO and the Welsh Government had published 36 project evaluations on their websites.

3.97 WEFO has issued generic guidance on evaluation and provides advice on each project's monitoring and evaluation plan at project development stage. Each strategic framework has a set of common evaluation questions that each project evaluation is expected to answer, to help ensure that evaluations seek to answer the same questions when projects have similar objectives. WEFO also reviews project evaluations for quality before publishing them on its website. All these were new developments for the current programmes and represent a strengthening of procedures on evaluation.

WEFO has developed a more sophisticated approach for assessing the net impact of the programmes

- 3.98 WEFO seeks to evaluate impact on an ongoing basis through the ESF Leavers' Survey and the ERDF Business Survey. The Leavers' Survey is annual and has taken place since 2010. It asks a sample of participants who have completed ESF provision within the year before the survey about the skills and qualifications they have gained and their employment history since they left their course or placement. The ERDF Business Survey was conducted in 2011 and WEFO intends to repeat it every two years. It asks businesses that have received ERDF support about the nature of their business and the effect that ERDF support has had on their turnover, employment, profitability, exports and degree of innovation.
- 3.99 Impacts will depend on a range of external factors that will tend to reduce the results reported by projects and the measurement of these impacts is often difficult and complex. Historically, the impact of economic programmes has been evaluated using a combination of primary research (asking recipients about their perception of impact) and estimating wider economic effects using standard discount factors derived from input-output tables.<sup>62</sup> However, input-output data is often dated and self-reported perceptions of impact may also be unreliable as a guide to actual impact.
- 3.100 To overcome these problems, WEFO commissioned research from DTZ consultants in 2010 on the feasibility of adopting different approaches to evaluating impact at the programme level. Based on the findings of the research, WEFO has piloted the use of econometric analysis for the ESF Leavers' Survey and the ERDF Business Survey. Econometric

analysis compares outcomes between a treatment group (those receiving EU funding) and a control group (as similar as possible to the treatment group but not receiving EU funding). Any difference in performance between the two groups, after adjusting for any structural difference, would be attributable to the impact of the Structural Funds.

- 3.101 The econometric analysis has worked reasonably well for the ESF Leavers' Survey. Despite some methodological difficulties, the evaluation has been able to compare the results of leavers with a control group drawn from the Labour Force Survey and to estimate net impact on that basis, yielding results that the evaluation contractors consider reasonably robust. As the volume of data has increased WEFO has been able to extend the analysis to examine the impact by gender, labour market status and for particular types of intervention.
- 3.102 On this basis, it is theoretically possible to extrapolate impacts across the programmes using WEFO's monitoring data. However, WEFO uses a narrower definition of unemployment (Jobseekers' Allowance claimants) than that used by the ESF Leavers' Survey and Labour Force Survey, which both adopt a broader definition that encompasses people seeking work but not claiming benefit. This broader definition, which is used to calculate the headline unemployment rate, typically increases the number of unemployed by around two-thirds. The broader definition is more appropriate to distinguish between those who are actively seeking work and those who are, in reality, economically inactive. By adopting a narrow definition of unemployment, WEFO's monitoring data is likely to overstate the proportion of participants who are economically inactive and most difficult to bring into the labour market.

<sup>62</sup> Input-output tables are official statistics that show how each industrial sector consumes the outputs of every other sector, in other words where each sector sells its products and where it buys its materials (inputs) from. Together with survey evidence, the tables enable an evaluation to estimate the scale of displacement, deadweight and multiplier effects and to reduce the reported gross results accordingly, giving an estimate of net impact.



3.103 The econometric approach has been less successful for the ERDF Business Survey. The aim was to compare the performance of ERDF recipients with a group of similar businesses from the Inter-Departmental Business Register (IDBR) and Financial Analysis Made Easy (FAME) databases – both major databases of companies trading in the UK. To make an effective comparison, the evaluation needed to identify the ERDF recipients within each database to obtain details of their financial and employment history, and compare that with a control group drawn from the same database. However, the analysis was hampered by several problems:

- a the contractors could not find many of the ERDF recipients within the databases because important details such as company name, address or VAT number in WEFO records were missing or inaccurate;
- b many ERDF recipients were small firms that did not have to file full accounts, so there was not enough financial information on them to make a comparison with a control group using FAME; and
- c many start-up companies assisted by ERDF had not yet appeared in the IDBR, meaning that a control group could not be created for a large proportion of ERDF supported businesses.

3.104 These major hurdles could not be overcome and the Survey had to rely on self reported impacts as described in [paragraph 2.63](#). Nevertheless, the Survey concluded that it was feasible to use the databases over time to compare the performance of larger businesses and to compare survival rates of a much wider range of businesses, provided that the quality of WEFO's records improved.

3.105 Overall response rates were 34 per cent for ESF and 40 per cent for ERDF. Much of the non-response was due to incorrect contact details for sampled participants. In addition, both surveys had significant refusal rates (respondents refusing to take part) and non-recall rates (respondents who could not remember receiving any assistance), especially for the ERDF Business Survey. European Commission guidance recommends that employment effects are monitored on an ongoing basis so that evaluation data is captured as soon as reasonably practical after the programmes' support is provided (time needs to be allowed for the support to have an impact). WEFO undertakes the ESF Leavers' Survey annually, and it may be worth conducting the ERDF Survey at annual intervals also in order to improve the reliability of survey data.

3.106 Much of the value of the two surveys lies in linking the findings to particular types of intervention so that the relative benefits of each type can be assessed. WEFO has been able to do this for the ESF Leavers' Survey, but the ERDF Business Survey is not yet at the stage where this would be possible. At present, there is no mechanism to feed the results of the Surveys into project evaluations, although the ESF Leavers' Survey has been used in the evaluation of ESF Convergence Priority 2 (tackling economic inactivity).

3.107 Project-level evaluation remains necessary to gain a more detailed insight into the impact of particular services and how they lead to impacts. Projects have autonomy in selecting evaluation contractors and deciding on evaluation methods. Such autonomy makes it easier to design an approach that suits a particular project and to compare different approaches. However, a more coordinated approach has



many potential benefits: greater economies of scale by commissioning bigger evaluations and/or using more ambitious research methods, more scope to share good practice and compare projects on a consistent basis, and greater ability for WEFO to control quality and facilitate sharing of data with programme evaluations. Seven sustainable tourism projects (known collectively as Environment for Growth or E4G) have commissioned Cardiff University Business School to coordinate the evaluation of all seven projects using a common evaluation framework, but this appears to be the only example of such collaboration.

- 3.108 The ESF Leavers' Survey provides ongoing evidence of the degree of impact achieved by ESF interventions. Some project evaluations, particularly for ESF, have also considered evaluated impacts. However, most evidence on impact at the project level or for particular types of activity is likely to emerge from evaluations in 2014 and 2015 when the programmes are closing and well into the 2014-2020 programming period. It will therefore be difficult to incorporate the findings into the design of the new programmes. A key benefit of the ESF Leavers' Survey is that increasingly robust information on impact is emerging on an ongoing basis and can be used both to manage the programmes and to assess impact over the long term. Such long-term evaluation is particularly important in assessing strategic impacts, such as the impact of Government intervention on innovation in the economy, but most evaluations are commissioned to focus on a particular project over a particular timeframe, normally linked to funding cycles.

## Appendices

Appendix 1 - Audit Methods

Appendix 2 - Strategic frameworks

Appendix 3 - Programme level indicator data for ERDF programmes

Appendix 4 - Programme level indicator data for ESF programmes

Appendix 5 - Information required from project sponsors in business plans



# Appendix 1

## Audit Methods

We used a range of methods to gain evidence for our review.

### Literature review

We reviewed a wide range of published reports and other documents, including:

- The operational programmes for each of the four programmes managed by WEFO
- EU regulations governing the use of the Structural Funds
- WEFO's guidance notes for applicants
- Minutes and papers of the all-Wales Programme Monitoring Committee
- Notes and minutes of WEFO's senior management team
- Programme evaluations, in particular:
  - *Effectiveness of Implementation in the 2007-2013 Structural Funds Programming Period*, evaluation commissioned by WEFO, January 2011
  - Databuild Research and Solutions, *WEFO Customer Insight Survey 2009*, WEFO, May 2010
  - WEFO, *Spatial European Teams: an evaluation*, WEFO, November 2010
  - Cardiff University, Old Bell 3 Ltd and IFF Research Ltd, *The 2011 European Social Fund Leavers' Survey*, WEFO, March 2013
  - Old Bell Ltd in association with Cardiff University and IFF Research Ltd, *ERDF Business Survey*, published by WEFO in 2012
- Project evaluations published by WEFO and the Welsh Government, as at 31 May 2013
- Key reports published by other organisations:
  - National Assembly for Wales Finance Committee, *The Effectiveness of Structural Funds in Wales*, December 2012
  - Dr Grahame Guilford, *Investing in Growth and Jobs: an independent review of arrangements for implementation of European Structural Funds programmes 2014-2020*, WEFO, March 2013
- Audit Authority reports, in particular annual control reports and reports on WEFO's systems for appraising project applications, monitoring the progress of projects, paying grant claims and project verification and inspection.

## Survey of project sponsors and project development officers

We conducted a survey of all project sponsors and project development officers as at January 2011 to establish their views on the European Structural Funds at that time. The survey used the 'Sensemaker' technique, which asks respondents to describe their experience of a particular issue (in this case, of their involvement with Structural Funds) and then to interpret their experience through a series of questions that cover all aspects of the management of the programmes. Two types of questions were used:

- 'triads', where the respondent indicates their opinion in balancing three conflicting statements; and
- 'polarities', where the respondent chooses a position between two opposing statements.

The survey covered the following areas:

- key principles such as the greater emphasis on competitive procurement and the shift to a smaller number of projects;
- WEFO's management procedures at both pre-approval and post-approval stages;
- WEFO's approach to risk and regulation;
- enabling and hindering factors in bringing a project to fruition; and
- risks to the programmes.

We used a mix of thematic analysis of the narrative answers and quantitative analysis of the specific questions to interpret the results of the survey.

We circulated the survey to 102 project sponsors (project managers) and 42 project development officers. We received 91 responses, an overall response rate of 63 per cent. Three respondents delinked to say whether they were project managers or PDOs. The response rate for the remaining 88 responses was 53 per cent for project sponsors and 78 per cent for project development officers.

## Interviews

During the course of our study we interviewed the following WEFO staff:

- the Director and other senior managers of WEFO;
- Head of Finance;
- Head of the Certifying Authority;
- managers in the Research, Monitoring and Evaluation (RME) team, Project Inspection and Verification (PIV) team and Payments team;
- priority controllers, who oversee particular areas of policy within the programmes;
- strategic framework coordinators; and
- Heads of the Spatial/Specialist European Teams (SETs).

We also met:

- the Chair and two other members of the Programme Monitoring Committee; and
- the 'desk officers' (officials) responsible for the Welsh programmes at the European Commission.

### Case studies and file review

We assessed the business plan, appraisal procedures, evaluation arrangements and progress to date for a sample of eight projects. We met the project manager and project development officer for each of these projects to discuss their assessment of the project and WEFO's procedures.

We reviewed a sample of 36 projects (including the case studies) to consider progress following approval and the application of WEFO's monitoring and performance management procedures. We examined project claims, progress reports and notes of progress meetings for each of the selected projects.

### Data analysis

We analysed the progress of the programmes for key monitoring indicators, comparing reported achievements as at 31 December 2013 against overall programme targets and profiled achievements at that date.

# Appendix 2

## Strategic frameworks

### ERDF

#### Thematic frameworks:

Framework	Priorities and themes covered
Business finance	Convergence – Priority 2, Theme 2 Competitiveness – Priority 2
Climate change	Convergence – Priority 4, Themes 1 and 2 Competitiveness – Priority 3
Community economic regeneration	Convergence – Priority 5, Theme 2
Enterprise	Convergence – Priority 2, Theme 1 Competitiveness – Priority 2
ICT infrastructure and exploitation	Convergence – Priority 1, Theme 2 Competitiveness – Priority 1
Innovation, R&D and technology	Convergence – Priority 1, Theme 1 Competitiveness – Priority 1
Materials efficiency	Convergence – Priority 4, Theme 2
Sustainable transport	Convergence – Priority 3, Theme 1

#### Spatial frameworks – sustainable regeneration:

Framework	Priorities and themes covered
Central Wales	Convergence – Priority 3, Theme 2 – Priority 4, Theme 3 – Priority 5, Theme 1 Competitiveness – Priority 4
North Wales	
Pembrokeshire Haven	
South-east Wales	
Swansea Bay	



## ESF

Framework	Priorities and themes covered
Improving public services	Convergence – Priority 4
Improving skills levels and adaptability of the workforce	Competitiveness – Priority 2
Increasing employment and tackling economic inactivity	Convergence – Priority 2, Themes 1 and 2 Competitiveness – Priority 1
Promoting gender equality in employment	Convergence – Priority 3, Theme 3
Raising the skills base of the workforce and supporting progression in employment through basic and intermediate level skills	Convergence – Priority 3, Theme 1
Skills for the Knowledge Economy: Higher Level Skills and Systems for Workforce Development	Convergence – Priority 3, Theme 2
Supplying young people with skills and learning for future employment	Convergence – Priority 1
Sustainable transport	Convergence – Priority 3, Theme 1

Source: WEFO

# Appendix 3

## Programme level indicator data for ERDF programmes

Indicator	Unit of measurement	End of programme			Up to 31 December 2013		
		Forecast (F1)	Target (T)	% (F1/T)	Achieved (A)	Forecast (F2)	% (A/F2)
<b>Convergence</b>							
<b>Enterprises assisted</b>	<b>Number</b>	<b>17,622</b>	<b>14,150</b>	<b>125%</b>	<b>10,666</b>	<b>10,890</b>	<b>98%</b>
Collaborative R&D	Number	1,245	514	242%	974	873	112%
<b>Gross jobs created</b>	<b>No FTE</b>	<b>32,877</b>	<b>33,200</b>	<b>99%</b>	<b>17,011</b>	<b>17,336</b>	<b>98%</b>
<b>Enterprises created</b>	<b>Number</b>	<b>8,707</b>	<b>5,094</b>	<b>171%</b>	<b>4,971</b>	<b>5,100</b>	<b>97%</b>
Profit benefit	£ millions	108	302	36%	10	26	39%
Investment induced	£ millions	277	473	58%	152	137	111%
Jobs accommodated	Number	3,185	1,050	303%	1,582	1,386	114%
Premises created or refurbished	sq metres	136,608	42,500	326%	62,474	79,049	79%
New or improved projects, processes or services launched	Number	2,531	5,028	50%	1,536	1,262	122%
Gross passenger kilometres on public transport	000 km	523,452	400,000	131%	339,583	339,983	100%
Waste reduced, reused or recycled	000 tonnes	406	600	68%	0	100	0%

Indicator	Unit of measurement	End of programme			Up to 31 December 2013		
		Forecast (F1)	Target (T)	% (F1/T)	Achieved (A)	Forecast (F2)	% (A/F2)
<b>Competitiveness</b>							
<b>Enterprises assisted</b>	<b>Number</b>	<b>4,416</b>	<b>1,750</b>	<b>252%</b>	<b>2,037</b>	<b>2,123</b>	<b>96%</b>
Collaborative R&D	Number	44	10	440%	9	15	60%
<b>Gross jobs created</b>	<b>No FTE</b>	<b>10,175</b>	<b>5,340</b>	<b>191%</b>	<b>6,638</b>	<b>6,464</b>	<b>103%</b>
Profit benefit	£ millions	9	30	29%	4	4	105%
Products, processes or services registered	Number	208	80	260%	123	119	103%
New or improved projects, processes or services launched	Number	286	400	72%	135	150	90%
Investment induced	£ millions	88	115	76%	42	38	111%
<b>Enterprises created</b>	<b>Number</b>	<b>3,142</b>	<b>510</b>	<b>616%</b>	<b>2,603</b>	<b>2,530</b>	<b>103%</b>

Source: WEFO programme and project database (PPIMS)

# Appendix 4

## Programme level indicator data for ESF programmes

Indicator	Unit of measurement	End of programme			Up to 31 December 2013		
		Forecast (F1)	Target (T)	% (F1/T)	Achieved (A)	Forecast (F2)	% (A/F2)
<b>Convergence</b>							
<b>Total participants</b>	<b>Number</b>	<b>536,256</b>	<b>267,500</b>	<b>200%</b>	<b>423,430</b>	<b>443,028</b>	<b>96%</b>
Female participants	Number	258,000	146,150	177%	0	n/a	n/a
Economically inactive participants	Number	161,000	63,750	253%	108,225	n/a	n/a
Unemployed participants	Number	93,000	55,000	169%	104,995	n/a	n/a
Employed participants	Number	168,000	122,500	137%	113,122	n/a	n/a
Employers assisted or financially supported	Number	22,043	20,060	110%	11,678	12,615	93%
Collaborative agreements between public service bodies	Number	115	20	575%	24	38	63%
<b>Participants entering employment</b>	<b>Number</b>	<b>72,333</b>	<b>27,500</b>	<b>263%</b>	<b>46,012</b>	<b>55,321</b>	<b>83%</b>
<b>Participants gaining qualifications</b>	<b>Number</b>	<b>203,655</b>	<b>79,530</b>	<b>256%</b>	<b>139,993</b>	<b>143,153</b>	<b>98%</b>
Participants gaining a basic skills qualification	Number	83,700	43,900	191%	53,201	n/a	n/a
Participants gaining a qualification at Level 2	Number	75,400	23,000	328%	63,120	n/a	n/a
Participants gaining a qualification at Level 3	Number	28,400	8,900	319%	17,532	n/a	n/a
Participants gaining a qualification at Level 4 and above	Number	16,200	3,800	426%	6,140	n/a	n/a
Participants entering further learning	Number	61,321	57,700	106%	36,128	45,422	80%

Indicator	Unit of measurement	End of programme			Up to 31 December 2013		
		Forecast (F1)	Target (T)	% (F1/T)	Achieved (A)	Forecast (F2)	% (A/F2)
<b>Competitiveness</b>							
<b>Total participants</b>	<b>Number</b>	<b>92,971</b>	<b>26,600</b>	<b>350%</b>	<b>64,112</b>	<b>76,247</b>	<b>84%</b>
Female participants	Number	41,000	15,190	270%	27,264	n/a	n/a
Economically inactive participants	Number	35,500	11,900	298%	21,969	n/a	n/a
Unemployed participants	Number	15,100	2,100	719%	14,105	n/a	n/a
Employed participants	Number	42,500	12,600	337%	28,010	n/a	n/a
Employers assisted	Number	7,062	2,800	252%	3,381	4,284	79%
<b>Participants entering employment</b>	<b>Number</b>	<b>16,021</b>	<b>3,500</b>	<b>458%</b>	<b>7,769</b>	<b>12,020</b>	<b>65%</b>
<b>Participants gaining qualifications</b>	<b>Number</b>	<b>31,741</b>	<b>9,650</b>	<b>329%</b>	<b>20,854</b>	<b>22,719</b>	<b>92%</b>
Participants gaining a basic skills qualification	Number	14,900	5,740	260%	4,870	n/a	n/a
Participants gaining a qualification at Level 2	Number	11,300	2,570	440%	9,957	n/a	n/a
Participants gaining a qualification at Level 3	Number	4,200	800	525%	4,674	n/a	n/a
Participants gaining a qualification at Level 4 and above	Number	1,300	540	241%	1,353	n/a	n/a
Participants entering further learning	Number	5,757	4,620	125%	1,324	3,821	35%

Source: WEFO programme and project database (PPIMS)

# Appendix 5

## Information required from project sponsors in business plans

Sponsors submit business plans with information under the following headings:

- 1 Project description  
*Aims, objectives, contribution to Government policy, activities, beneficiaries, location*
- 2 Project management and delivery  
*Record of project management, organisation of the project, resources available, procurement*
- 3 Need and demand for the project  
*Research that identifies need and quantifies demand, feasibility studies, details and justification of any duplication or displacement of existing activity*
- 4 Options for delivery  
*Analysis of options for delivering the project, including the 'do nothing' option*
- 5 Outputs and results
- 6 Financial profile  
*Detailed breakdown of costs and cash flows with any assumptions used*
- 7 Financial package  
*Explanation of match funding sources and justification for level of funding sought*
- 8 Value for money  
*Evidence to support the case for economy (cost of inputs), efficiency (relationship between costs and outputs), effectiveness (how the outputs and results will create the impacts required)*
- 9 Added value  
*How the project will create new benefits and support activity that would otherwise not take place or be reduced/postponed*
- 10 Monitoring and evaluation  
*Selection of indicators, how data will be collected, data quality, evaluation timing and methods*
- 11 Post funding/continuation strategy  
*Exit strategy and project legacy*
- 12 Risk management  
*Approach to management of key risks*
- 13 Publicity  
*Public acknowledgement of EU funding, publicity activities, dissemination of good practice*