

Economic Development Committee

Date: 13 October 1999

Venue: Committee Room 2, National Assembly Building

Title: European Structural Funds – Financing mechanisms

Purpose

1. The Economic Development Committee is invited to note :

- the relationship between European, UK Government and match funding;
- the financial breakdown between the previous and the new ERDF forecast payments for year 1 (2000-01).

Summary

2. The paper describes the European Commission's Regulations governing the budget and payment arrangements for the new Structural Funds programmes; explains the relationship between the Commission's cash and public expenditure as defined by the UK Government; and identifies the likely funding requirement and source of funds for year 1.

Timing

3. The paper is presented at the request of the Committee.

Introduction

4. 'European Funding' encompasses three elements.:-

(i) EC Grant : the Commission's own cash;

(ii) Public expenditure as defined by the UK Government (provision in the National Assembly's Departmental Expenditure Limit); and

(iii) Match funding : the non-EC grant element of project costs – usually project sponsors’ own cash.

EC Grant

5. There are two strands to this –

- Commitments
- Payments

6. The Commission has made clear that it expects a broadly flat profile of **commitments** over the Programme period. The Annex to the Structural Funds Regulations (the Regulations) sets out the profile for the whole of the Community’s budget for the new Programmes as follows –

Structural Funds (million euro – 1999 prices)						
2000	2001	2002	2003	2004	2005	2006
29,430	28,840	28,250	27,670	27,080	27,080	26,660

7. The following commitment profiles for *Objective 1* areas of the UK will apply –

million euros	2000	2001	2002	2003	2004	2005	2006	Total
Sth Yorks	179.8	176.7	173.3	169.9	150.4	162.2	160.2	1172.5
West Wales / Valleys	284.3	279.3	274.0	268.6	237.7	256.4	253.1	1853.4
(£m)	(187)	(184)	(180)	(177)	(157)	(169)	(167)	(1222)
Cornwall	76.4	75.0	73.6	72.2	63.9	68.9	67.8	497.8
Merseyside	204.5	201.0	197.1	193.3	171.0	184.5	181.9	1333.3
Performance Reserve					69.0	70.0	72.0	211.0

NB: For West Wales and the Valleys the top figure is in euros, the bottom figure is in £ sterling at an exchange rate of 0.66 euros to £1.

8. Article 31 of the Regulations sets out the rules for budget commitments, and Article 31.2 (paragraph 2) has a bearing on the EC payments profiling. This states –

‘The Commission shall automatically decommit any part of a commitment which has not been settled by the payment on account or for which it has not received an acceptable payment application, as defined in Article 32.3, by the end of the second year following the year of commitment.....’.

9. The rules do not imply any earmarking of payments to commitments for any particular year. The UK Government is working on the understanding that this rule will be satisfied provided the Commission is sure that the aggregate payment applications, plus any payments on account, are, by the end of year 3, at least equivalent to the level of year 1 commitments.

10. This rule also refers to ‘the payment on account’. Article 32 .2 (paragraph 1), sets the payment on account as 7 per cent of the total contribution from the Structural Funds. It goes on to suggest that ‘in principle’ the payment on account may be sub-divided over two budget years at most, depending on the availability of budget funds.

11. Using the profile of Objective 1 commitments set out at paragraph 7, this translates to a payment requirement as follows -

£m	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	total
Commitment	187	184	180	177	157	169	167	1222
Payment on account	42.7 (3.5%)	42.7 (3.5%)						
Minimum level of payments to be made (by end of year)	144.3 (yr3)	141.3 (yr4)	180 (yr5)	177 (yr6)	157 (yr7)	169 (yr8)	167 (yr9)	
% of commitment	77.2%	76.8%	100%	100%	100%	100%	146%	

NB: This is not a payments profile but describes the parameters within which a profile should be constructed.

12. Points to note

- De-commitment by the Commission kicks in if any part of a commitment for a given year has not been settled by the payment on account or if the Commission has not received an acceptable payment application by the end of the second year following the year of commitment [*Article 31.2 paragraph 2*];
- The first payment on account for Objective 1, will be paid into the National Assembly's Paymaster account when the first commitment is made by the Commission [*Article 32.2*];
- Interim payments are made by the Commission to reimburse expenditure actually paid under the funds as certified by the paying authority. As far as possible, applications for interim payments should be presented to the Commission in batches three times per year, the last application being presented no later than 31 October [*Article 32.3*].

Public Expenditure - provision in the Departmental Expenditure Limit (DEL)

13. In terms of budgeting within the National Assembly, the key issue is not the level of commitments in any particular year, but the level of payments to grant recipients which will need to be made since it is these which will count as public expenditure and will have to be accommodated within the Assembly's Departmental Expenditure Limit. Translating the Commission's own payments profile into public expenditure terms is not straightforward. EC grant money paid into the Assembly's suspense account does not become public expenditure until it is drawn from suspense and paid over to project sponsors. At that point the cash scores against the DEL.

14. Historically, the spending on Objective 1 (particularly the ERDF element) in other areas has been slow to build up. For example, for the current i.e. 1994 - 1999 programme, in both the Highlands and Islands and in the Merseyside models, there was no ERDF expenditure in the first year. In the case of Merseyside, expenditure in the second year was only 15% of the year's ERDF allocation, in the third year 45% of that year's allocation and not until the fourth year did expenditure reach 90%.

15. For the new Programmes, the greater financial discipline which has been introduced by the Commission to try and ensure a consistent level of expenditure, coupled with the fact that in Wales there is already a high level of preparation given to Objective 1 and the approach which the National Assembly has taken is likely to mean that the take-up will be quicker than was the case with the 1994-99 programme.

16. Apart from the payment on account, the Commission will not reimburse the paying authority (the National Assembly) unless expenditure has been incurred and payments made. Thus, using the latest projections (see table at paragraph 11) the profile of public expenditure for Objective 1 (all programmes e.g. ERDF, ESF, EAGGF etc) will need to be such that at least £144.3 million is spent by the end of year 3.

17. However, there can be no guarantee that expenditure on projects will be uniform since many things can influence the speed at which projects progress. For next year (2000) we are working on the level of an overall commitment of £187 million as outlined in paragraph 11 above. It is important to note at this juncture that the Commission operates within the calendar year whereas we operate in financial years. Our current estimate of expenditure for Objective 1 in the financial year 2000-01 is around £25 million but this excludes expenditure on European Social Fund (ESF) projects as this will be covered by the Department for Education and Employment (DfEE) rather than the National Assembly. So the amount which we estimate at the moment will need to be found by the National Assembly for expenditure on the new programme next financial year will be £25 million.

Overhang from the existing ERDF programme

18. The Committee asked in particular for an explanation of how the overhang from existing ERDF programmes will be funded. The National Assembly has an entitlement, subject to Treasury agreement, to draw down from the Reserve either this year or in subsequent years, up to £46 million specifically for ERDF payments. This money is in addition to the forward budget lines and is money which has been budgeted for in previous years and which has not been spent. It can therefore be used to supplement baseline provision this year and next and the existing baselines were set in the knowledge that this money could be drawn down.

19. For 2000-01 our present forecast for ERDF spend on the existing programme is £50 million (although since, historically, the programme has always underspent there must still be some doubt as to whether this level of spend will actually materialise). So the total estimated funding requirement for next year, for the National Assembly, is £75 million.

20. At the end of last year following discussions between the Chief Secretary to the Treasury and the Secretary of State for Wales, the Treasury agreed to supplement the Welsh Office budget by £35m in order to meet unmanageable pressures.. The money was additional to that which had already been allocated through the Barnett formula and was spent during the year as extra provision on Regional Selective Assistance, the NHS drugs bill, the central roads programme and on the Office of Her Majesty’s Chief Inspector (now Estyn). There is sufficient flexibility in the National Assembly budget, this year and next, to accommodate spending on both the old and new programmes at anticipated levels. taking into account the resources available from the baseline provision, from earmarked ERDF carry-forward and from other carry-forward resources which are available to supplement the overall budget next year.

21. The table below sets all this out

Programme Period	1999-00	2000-01
	£m	£m
Pre 2000 programmes	35	50
Post 2000 programmes	nil	25
Total requirement	35	75

To be funded by -		
Baseline provision	9	19
ERDF carry-forward	25	21
Other carry forward	1	35
Total provision available	35	75

NB –

- the table excludes provision for ESF (currently the responsibility of the Department for Education and Employment);
- the table excludes match funding

22. For future years from 2001-02 and beyond, the implications for the National Assembly's budget will be considered as part of the next Spending Review. Officials have begun preparatory discussions with the Treasury.

Match Funding

23. There are two distinct elements of match funding – public sector and private sector.

24. The Regulations are silent on where match funding should originate. There is a view in the Commission that public sector match funding should be at the rate of £1 for each £1 of EC grant with private sector funding an added bonus: private sector match funding should not be used as a substitute for public sector match funding.

25. Under the Regulations however, only the minimum levels of match funding is stipulated. The UK Government believes the overall level of match funds and the division between public and private sector match funds is a matter for the Regional Programmes to decide.

26. The traditional sources of such match funding under existing Programmes are the Assembly itself, local authorities, agencies such as the Welsh Development Agency, Wales Tourist Board, Countryside Council for Wales, TECs, further and higher education, the voluntary sector and the private sector. There is no reason to believe that there will be a material change in these funding sources in the future but officials are currently working with the Welsh European Programme Executive Ltd, who presently administer the Programmes on the National Assembly's behalf, to obtain a more detailed breakdown of these match funding sources. As soon as the information

is received it will be passed to the Committee.

27. It is anticipated that for 2000-01, there will be sufficient match funding from initiating sponsors to cope with the projects expected to come forward in that year. Beyond that, the issues will be considered in the context of the next Spending Review.

European Social Fund

28. At the moment, the National Assembly for Wales administers the European Social Fund in Wales but the payments are made by the Department for Employment and Education (DfEE) and the public expenditure provision therefore lies with them as well. There are operational arguments in favour of the National Assembly taking over complete responsibility at some time in the future. However, the scheme would represent a significant additional commitment, primarily in financing the payments but also in terms of the extra administration and auditing involved. National Assembly officials are discussing with colleagues in DfEE what would constitute acceptable terms for a transfer of responsibility that would be satisfactory both to DfEE and the National Assembly.