

Cyfarwyddwr Cyffredinol, Cyllid a Gwasanaethau Corfforaethol

Director General, Finance and Corporate Services



Llywodraeth Cymru
Welsh Government

Mr Darren Millar, AM
Chair – Public Accounts Committee

2 June 2014

Dear Mr Millar

Report of the Auditor General for Wales – European Union Structural Funds 2007-2013

I am writing in response to your letter of 7 May about the Public Accounts Committee consideration of the Auditor General for Wales' report on the European Union Structural Funds 2007-2013 (published 24 April 2014). The Committee requested a response from the Welsh Government to the Wales Audit Office (WAO) recommendations. In addition, the Committee also requested responses to the Auditor General's recent reports on public funding for Penmon Fish Farm and the Cywain Centre. I am pleased to confirm that all of the recommendations contained within these three reports have been accepted. The progress of the Welsh European Funding Office (WEFO) in implementing the recommendations of each report is summarised below.

European Union Structural Funds 2007-2013

This was a generally positive report and it picked up on a number of points that have been raised previously. Four recommendations (R3[a], R6[a], R7[c] & R12[a]) have already been implemented in full. A further three have been partially implemented (R1, R4[b] & R7[b] and work on these is continuing. The remaining recommendations will either be fully implemented by the end of 2014 (subject to the approval by the European Commission of the UK Partnership Agreement for the 2014 – 2020 funding period and the individual Operational Programmes for Wales) or, for those relating to the monitoring of operations, will be progressed as the implementation of the new Programmes gets under way.

Public Funding of Penmon Fish Farm

We accept all the recommendations from the report. The events are some time in the past and the control environment has been strengthened significantly over the intervening period. The issues raised have now been addressed.

Recommendation 1 is that grant recipients be required to comply with UK law. The Welsh Government highlights key statutory requirements and obligations in its funding agreements but notes that the scale of this requirement is such that it will not be possible for the Welsh Government to monitor compliance across all areas as a matter of routine.



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Recommendation 2 is accepted and WEFO's management verifications have been extended to cover transactions between a grant recipient and a supplier that is a related company. For example, testing transactions between the related companies for reasonableness or treating the related companies as a single entity when testing supplier expenditure.

Recommendation 3 is accepted. WEFO has put in place arrangements to coordinate the provision of expert advice from internal and external sources (e.g. technical and specialist advice on bio-sciences, marine sciences etc) to ensure that project proposals are set up effectively, represent added value and are technically feasible.

Recommendation 4 is accepted. The Grants Centre of Excellence project has already strengthened processes across the Welsh Government for communications on grants management.

Public Funding of Cywain Centre

Recommendation 1 reflects Recommendation 4 from the Penmon Fish Farm report and is accepted. Action is being taken to strengthen processes in line with the Grant Centre of Excellence project.

Recommendation 2 is also accepted, whilst recognising that a clear legal basis will be required for taking the kind of steps proposed. The current Structural Fund regulations (Article 57 of EC Regulation 1083/2006) requires investments in infrastructure and productive investment to be safeguarded for 5 years from the date of completion. Further work is being undertaken to identify the most appropriate and practical approach to extending this protection. This could mean, for example, requiring a legal charge on grant funded assets in the grant offer letter to ensure that the assets continue to be used for the purpose for which they were funded. On balance, we agree that the need to protect public investments means that this should be done, but we acknowledge that some beneficiaries would make a counter argument, saying that this would restrict their use of that asset to secure additional funds and make further investments. The exact nature of the controls that might be appropriate will vary depending on the nature of the project.

Additional Issues

To help in the Committee's consideration of the report before its meeting on 12 June, it has also requested that the Welsh Government address the following issues. Each issue is therefore accompanied by a Welsh Government response.

- **An update on the Welsh Government's approach to setting ESF targets for the new programming round including details of work being undertaken to ensure that targets are appropriately challenging.**

Response:

All targets are set and agreed with the Commission either as part of the negotiation of the Programmes at the outset or during subsequent programme modifications. Our proposals for the 2014-2020 ESF Programmes will see an even greater emphasis on individuals who are at most at risk of poverty, exclusion and disadvantage. The challenge of helping those at greatest disadvantage in the labour market will of course need to be reflected in setting targets for the next round of Programmes. Targets will be negotiated on the basis of historical performance data for Structural Fund and other public investment programmes, drawing on National Statistics where available. Both the Welsh Government and the

European Commission share an interest in agreeing stretching but realistic targets which will demonstrate good value for money in the use of ESI Funds. It should also be noted that the new programmes will have a stronger emphasis on results, including the use of a Performance Reserve mechanism to reward or penalise programmes for over or under performance respectively.

- **Action that the Welsh Government is taking to improve performance on these cross-cutting themes, both for the final period of the 2007-2013 programmes and for the 2014-2020 programmes.**

Response:

WEFO is taking a number of specific actions to address the issues identified:

- Completion of intervention logic tables by applicants, demonstrating precisely how the operation (project) outputs and outcomes and activities will align with stated and specific programme objectives and achieve on all identified Cross Cutting Theme (CCT) indicators.
- The CCT indicators for the 2014-2020 programmes will be more closely aligned with mainstream priority level activity, reducing the requirement on beneficiaries (sponsors) to deliver separate activity to delivery CCT objectives.
- Training workshops on the integration of the CCT's in the 2014- 2020 programmes are being delivered for WEFO staff and those delivering operations. Training needs in this area will be regularly reviewed throughout the life of the programmes.
- In developing the new programmes, emphasis has been on the need for beneficiaries to give more detailed plans on how their activity will contribute to the CCTs.
- The CCT Team has been expanded and will have a broader remit across all European Structural & Investment (ESI) funds, including rural and maritime programmes, and will be better able to identify needs and opportunities.
- WEFO will continue to share good practice examples on CCT integration and encourage operations struggling with their CCT commitments to learn from others.
- **What monitoring arrangements the Welsh Government has in place to determine the extent of larger companies setting up small scale bases in Wales and how procurement processes define a Welsh-based company.**

Response:

Procurement legislation prohibits discrimination on the basis of supplier location. Therefore, the procurement process would not necessarily favour any business setting up a small-scale operation in Wales. For the purposes of monitoring, indigenous Welsh businesses are identified on the basis of Companies House records. In the context of Community Benefits measurement, Wales based businesses are defined as those who perform a significant part of the project in question from an office based in Wales, therefore having a greater prospect of employing and paying people who reside in Wales.

In respect to the Structural Funds, the Welsh Government collects details on those organisations which obtain procurement contracts. Using current data from the 2007-2013 programmes, the private sector has been awarded 60% of all procured contracts. In 2011, WEFO undertook an exercise to establish whether companies benefiting from the procurement of EU projects were: a Welsh Company (wholly based within Wales); a

company with a Welsh Presence (for example a national company that has a presence in Wales); or a company that is based outside Wales (typically national or international companies). This research found that there were a total of 1431 contracts worth £700k, with 69% of these going to Welsh Companies and 13% to companies with a Welsh Presence. WEFO plans to repeat this research exercise later in 2014.

- **A) The Committee is interested in any other measures of prosperity that the Welsh Government may be able to provide or point to that compares the impact of Convergence Programme funding in Wales with the impact of the equivalent funding in other EU regions.**
- **B) Any evidence that the Welsh Government may have to quantify the possible impact of out commuting.**

Response:

Gross Domestic Product (GDP) or Gross Value Added (GVA) is used by the European Commission to determine Structural Funds allocations (which have already been set for the 2014–2020 period) and is a measure of the economic activity taking place within an area. The measure can be particularly misleading in the West Wales & the Valleys (WW&V) region which experiences large out-commuting flows and can depress the GVA estimates, as recognised by Eurostat.

To measure the success of economies it is important to look at a basket of indicators – for example, employment rates and income levels, which particularly matter in people’s well being. Here, our performance is better and since the late 1990s there has been a marked and sustained closing of historical gaps between Wales and the UK. Before devolution, the employment rate in Wales was typically 5-6 percentage points below that for the UK. Over the last few years the gap has generally been less than 3 percentage points, and even less than this over the more recent past. Since 1999, employment in Wales has increased by 157,000 or 13 per cent compared to a 12.2 per cent increase for the UK as a whole.

With disposable income a better indicator of living standards than GDP, Wales compares well or performs better than it does on GDP relative to the EU (based on Eurostat figures for disposable income per capita at purchasing power standard based on final consumption per inhabitant for 2010).

In terms of measuring the potential impact of out commuting across West Wales and the Valleys, the socio-economic analysis undertaken in preparation for the 2014-2020 programming round found that overall GVA per head between 2009 and 2011 was approximately £2,100 less than the average for Wales as a whole. Analysis of this gap in more detail revealed that 25% - 30% of the overall gap is explained by residents of West Wales and the Valleys commuting outside the area for work - GVA created by net out commuters is not attributed to the Programme area.

Yours sincerely



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