

15 July 2013

Rt Hon Michael Fallon
Minister of State for Business and Enterprise
Department of Business Innovation and Skills
1 Victoria Street
London
SW1H 0ET

Dear Minister

We write to you on behalf of three professional associations of university officers supporting research, innovation and economic development (ARMA, AURIL and PraxisUnico). Universities are valuable contributors to the local and UK economies and, over the last twenty years, have also been very active in ERDF programmes. As we debate the future of ERDF in the UK in anticipation of the 2014-20 Structural Funds Programmes it is timely to bring together some of the issues with ERDF support which are compromising the university sector's engagement in local economic development. We will also be bringing these issues to the attention of Sir Andrew Witty as he examines universities' contributions to their local economies.

When the initials ERDF are mentioned in a university context they are usually followed by a sharp intake of breath. An increasing number of finance officers are concerned about the level of risk involved in securing ERDF support and the significant risk of clawback for minor non-compliance issues. Clawback can occur several years after expenditure has been originally validated as eligible, adding to the burden and uncertainty (and frequent long delays in processing claims can also cause problems). Thus, clawback issues are a major disincentive for universities to play a full role in ERDF.

To understand the universities' responses it is first necessary to understand why universities engage in ERDF supported activities. Universities, for the most part, engage in ERDF as a way of contributing to local economic development, strongly influenced by their civic missions. There is also a considerable value to institutions in demonstrating the broader value and utility of the research and innovation which they deliver, i.e. the Impact agenda. ERDF co-resourcing is important in supporting important collaborative R&D work between universities working in conjunction with SMEs, larger companies and other innovation partners in the public and third sectors (although we note that greater scope for the use of ERDF in working with larger companies would be hugely beneficial). Universities are for the most part subsidising ERDF projects through waiving large portions of indirect costs and often including cash contributions,

PraxisUnico
Jeffreys Building
St John's Innovation Park
Cowley Road
Cambridge CB4 0DS
www.praxisunico.org.uk

AURIL
c/o University of Strathclyde
50 George Street
Glasgow
G1 1QE
www.auril.org.uk

ARMA
Sheraton House
Castle Park
Cambridge
CB3 0AX
www.arma.ac.uk

while a significant benefit can be the additional resourcing of HEI knowledge exchange teams to which this funding stream can contribute (albeit on a fixed-term basis).

We see six broad challenges arising from ERDF support. For each challenge we include a recommendation for action.

- 1) An unwillingness to accept that the UK has a nationally agreed costing regime through TRAC for calculating indirect costs in the university sector. Even when costing methodologies are agreed in advance these are then re-examined during audit, changes can be imposed and funding lost and clawback imposed. Indirect costs are real but difficult to render direct. They are accepted across the public and private sectors as an efficient accountancy mechanism for dealing with the real costs of organisations without putting in place burdensome and inefficient administrative systems. Time and again ERDF auditors approach the analysis of indirect costs as if they were direct and in complete absence of recognition of the nationally approved TRAC system.

Recommendation: For the 2014-20 Programmes we recommend that a nationally approved university indirect cost rate for ERDF projects should be established, based on TRAC methodology. This should be set at a sensible and realistic level, to be determined, but with no requirement for specific project by project justification of the rate. We also recommend that a maximum length of delay should be established for payment of uncontested claims.

- 2) State Aid rules create major difficulties not just for universities but for many other organisations. The interpretation of State Aid rules is highly specialised. Each university has, at most, only a few ERDF projects. It is wholly inappropriate to expect each organisation in receipt of ERDF support to understand the intricacies of State Aid Rules.

Recommendation: Administering authorities (DCLG and the devolved governments in Northern Ireland, Wales and Scotland) should accept responsibility for the State Aid test at programme level and for giving advice on mechanisms to be used in projects to ensure State Aid compliance. Compliance with these defined mechanisms would then be accepted as the basis for audit.

- 3) There needs to be a clear recognition that economic development projects addressing difficult economic development issues are high risk projects. We agree with a focus on economic development output targets for ERDF projects but expecting 100% achievement leads to conservative expectations and unambitious projects which in turn are unlikely to play to a university's strengths or deliver step changes in regional innovation. We are aware of projects which have been subject to financial clawback when all but one set of outputs was over-achieved, i.e. a shortfall on one metric under an otherwise highly successful project has resulted in a financial penalty. Where a university has been negligent we would, of course, wholly accept the expectation of clawback.

Additionally, the need often arises to support projects which are adventurous, early stage and lack proximity to market. Nevertheless, these projects may have significant future commercial potential in markets which are themselves immature and emerging. Administering authorities and programme managers for ERDF supported projects need to ensure that such early stage projects, which may in some cases be led by universities, are not burdened with inappropriate and unreasonable output targets.

Recommendation: auditors should rightly focus on financial performance and eligibility of expenditure. They should take into account effort and commitment to projects and broader positive achievements, and should not place undue emphasis on what can, at best, only ever be estimated outputs. Administering authorities should manage output targets intelligently and at portfolio or programme level in order to ensure that adventurous, early stage projects with great future potential are not placed at a relative disadvantage or overlooked entirely.

- 4) Narrow definitions of geographic boundaries lead to sub-critical economic development projects relating to innovation. Universities work locally and nationally. For many economic development activities relating to innovation and technology, any individual university may be well placed to deliver positive outcomes across more than one ERDF eligible area. Furthermore, universities outside of an ERDF eligible area are able to deliver considerable benefits to recipient organisations within the eligible area and expenditure rules should provide the flexibility to accommodate this. In England this is a critical issue due to the large number of individual LEPs, each with a relatively limited ERDF budget. There is thus a real risk that major projects might be compromised through a fragmented approach by the LEPs.

Recommendation: innovation projects should be able to work with organisations across all ERDF eligible areas in the UK. Universities and other project participants located outside of an ERDF eligible area should be allowed sufficient scope to incur project expenditure which deliver benefits to economically active entities within an eligible area. DCLG needs to provide an effective framework for flexible co-financing of activities which span more than one LEP.

- 5) A key feature behind many ERDF projects is to ensure that an activity which supports economic development and innovation can operate on a self-sustaining basis. However, revenues generated within a project may lead to a reduction in eligible grant. These revenues need to be built up over time as the project progresses, in order that a fighting fund thus generated can be used to bridge the transition between a public to private revenue funded activity.

Recommendation: projects should be allowed to build financial reserves providing that there is a commitment to use such reserves in a ringfenced fashion wholly and solely for the purposes of the project even if this is beyond the original, funded project period.

- 6) It is not uncommon for ERDF developments to be required to generate a long term business plan, in some cases for up to 25 years. Whilst this is maybe appropriate for major infrastructure investments it is not appropriate for revenue based or small building projects.

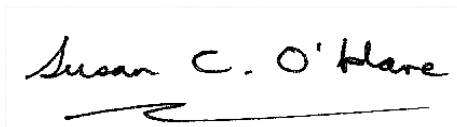
In addition, it is recognised that business plans are speculative and predictive and variation is expected. In many ERDF projects small changes to the project necessitate re-casting the business plan and seeking approval for changes. This is administratively burdensome, constraining and wasteful.

Recommendation: the business planning period be reduced to a maximum of ten years other than for recognised capital infrastructure projects and that only significant variations to the business plan require approval.

We recognise that some of these issues will not be resolved in the short term and would require discussions with your colleagues in the European Commission. However, we believe that this time spent on simplification of ERDF would be an excellent investment with benefits for both the organisations involved in project delivery across Europe and for managing authorities for ERDF.

We would like to assure you of the commitment of our university members to support economic growth on both a local and national basis. We believe that, through the delivery of pragmatic solutions to what can seem insurmountable problems, much can be achieved and the commitment of universities to our economy can be enhanced.

Yours faithfully



Dr Sue O'Hare
Chair of PraxisUnico and Director
of Enterprise,
City University London



Dr David Bembo
Chair of AURIL and Deputy
Director of Research
Innovation & Enterprise
Services, Cardiff University



Dr Ian Carter
Chair of ARMA and Director of
Research and Enterprise,
University of Sussex

Note: This letter will be published as an open letter on the websites of PraxisUnico, AURIL and ARMA

cc: Mark Holmes, Rt Hon David Willetts, Dr Graeme Reid, Dr Carolyn Reeve, Sir Andrew Witty, BIS; Rt Hon Eric Pickles, DCLG; Alice Frost, HEFCE; Howard Partridge, TSB; Damien O'Brien, Welsh European Funding Office; Nicola Sturgeon, Scottish Government; David Sterling, DETI, Ireland; Greg Wade, Universities UK

For info: Ken Skates, Welsh Government; Sue Price, Welsh European Funding Office; Tove Oliver, HEFCW; Gordon McLaren, ESEP Ltd; Alastair Hamilton, Invest Northern Ireland; Tracy Meharg, Invest Northern Ireland, Ireland