OPERATIONAL PROGRAMME

EUROPEAN REGIONAL DEVELOPMENT FUND:
2007-2013

LOWLANDS & UPLANDS SCOTLAND

<u>FINAL</u>

CONTENTS

1   INTRODUCTION

The following Operational Programme provides the framework for the spending of the European Regional Development Fund (ERDF) for the Regional Competitiveness & Employment Programme for Scotland for 2007-13. The Programme covers the 'Lowlands & Uplands Scotland' area, defined as the whole of the NUTS II areas for Eastern Scotland, North-East Scotland and South-Western Scotland (that is, all of Scotland apart from the Highlands & Islands, which are covered by programmes under the Convergence Objective). It will complement the European Social Fund Programme under the Regional Competitiveness & Employment Objective for the same area.

In March 2000, the EU leaders agreed the Lisbon strategy, which committed the EU to become by 2010:

> *"The most dynamic and competitive knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion, and respect for the environment."*

The achievement of this goal is seen as essential if Europe is to respond to the challenges of globalisation and competition from other parts of the world. Scotland is no less ambitious in its goals aimed at ensuring that the Scottish Executive and its partners work together to make a real difference to the lives of all the people living and working here to ensure they fulfil their potential and contribute to and benefit from a high-earning, knowledge-based economy.

The Programme aims to achieve this through the following overall vision:

> **To encourage the growth of the region's economy within a sustainable development framework and thereby enable all parts of the region to contribute to achieving the Lisbon Agenda goals**

It will do so through a set of co-ordinated priorities, working in tandem with the existing priorities of Scottish policy but also catalysing the Scottish Government's commitment to improving the main sources of competitiveness in the economy of all parts of the region. It does so fully within the context set by the Community Strategic Guidelines, the UK National Strategic Reference Framework and the UK National Reform Programme. The Programme brings an EU value of €375.958 million to achieving these goals and has been developed within a framework of partnership with the partners and stakeholders who will be delivering the projects that will make the Programme vision concrete.

The Programme document is divided into several sections following this Introduction:

- Socio-economic background: A summary of the key strengths, weaknesses, challenges and opportunities for the eligible area within the context of the Structural Funds contribution to achieving the Lisbon Agenda goals, setting out the main challenges for the Programme to address.

- Policy background: A summary of the policy context for addressing the challenges identified in the socio-economic analysis and how the 2000-06 Structural Funds programmes provide lessons for tackling these issues in the 2007-13 Programme.

- Strategy, Objectives and priorities: A detailed description of the Programme's overall vision and how the Programme will act on the identified challenges, setting out the Programme's objectives and the priorities, as well as the use of Programme technical assistance and the categorisation of activities in line with Lisbon 'earmarking'.

- Financial arrangements: The financial allocation tables for the Programme.

- Co-ordination with other funds: A description of how the European Regional Development Fund will complement other key EU funding in the region, particularly the European Social Fund, the European Agricultural Fund for Rural Development, the European Fisheries Fund and financial instruments available through the European Investment Bank.

- Implementing provisions: A description of key aspects of managing and delivering the Programme, including the roles and responsibilities of the Managing, Paying and Audit Authorities, key intermediary bodies and the Programme Monitoring Committee.

- Cross-cutting themes: A description of how Equal Opportunities, Sustainable Development and Social Inclusion will be mainstreamed as underpinning horizontal themes throughout the Programme.

- Evaluation, monitoring and reporting: The evaluation strategy for the Programme, setting out how the Programme will be monitored and the processes for reporting and evaluation.

In addition, there are a number of Annexes covering:

- acronyms and references;

- summary of the drafting of the Programme and engagement with partners;

- summary of the ex-ante evaluation report for the Programme;

- summary of the Strategic Environmental Assessment of the Programme and the environmental situation;

- summary of the Equal Opportunities Impact Assessment for the Programme;

- an indicative description of major projects envisaged by the Programme; and

- an indicative breakdown of actions by category of activity.

2. SOCIO-ECONOMIC BACKGROUND

The report provides an evidence base to educate the development of the new European Regional Development Fund Programme in Lowlands & Uplands Scotland for the period 2007-13. The analysis examines the underlying challenges in the Scottish economy in contributing to the achievement of the EU's ambitious targets for jobs and economic growth under the Lisbon Agenda. Key issues facing Scottish economic development through the programming period are identified, although inevitably, these may alter over so long a time period. However, the trends identified are part of more fundamental features of the Scottish economy which have shaped domestic policy as well as the issues highlighted in the Community Strategic Guidelines (CSGs) as central to improving regional competitiveness across the EU. These include challenges that face the region as a whole, particularly with regards to the enterprise sector and its key sources of competitiveness, as well as more localised challenges that face distinctive parts of the region.

The analysis is not meant to be a comprehensive review of the Scottish economy, but a focus on a specific set of market failures which Structural Funds can help to address within the framework of the Lisbon goals on growth and jobs. Some important elements of wider economic development have not been examined in detail because Structural Funds under the Convergence Objective cannot provide significant support to address the issues adequately. For example, although transport infrastructure and access continue to be major issues for much of the Lowlands & Uplands Scotland region, it has not been covered in the analysis owing to the limited scope for ERDF funding to tackle these problems. The role of the Lisbon Agenda as the key driver in the development of the Programme should be emphasised – the Structural Funds have to make clear, value-added contributions to the EU's goals of improving economic growth and jobs within challenging timescales. Moreover, the analysis focuses on aspects of socio-economic development where limited Structural Funds support can make significant differences.

Similarly, there are other analyses that have informed the development of the Programme, not least the Strategic Environmental Assessment and the summary of the environmental situation, which provides the key baseline environmental data for the Programme area and recommendations for addressing environmental sustainability issues. This is contained in annexes.

The analysis begins with a general section setting the demographic and economic context of the region. Following this, and reflecting the focus on region-wide and territorial issues within the CSGs, the analysis concentrates on two sets of areas of particular importance to the region's underlying competitiveness:

- region-wide challenges: given the importance of the enterprise base to the Lisbon Jobs and Growth Agenda, the analysis examines the overall health and trends in the enterprise base of the region and key bottlenecks in wider economic growth, particularly the innovation and RTD performance and capacity of the region; and

- **sub-regional challenges**: the region contains areas that have quite distinctive sets of challenges, particularly <u>urban</u> areas where socio-economic deprivation are particularly concentrated, and <u>rural</u> parts of the region which face different sets of competitiveness challenges.

The analysis covers both Scotland as a whole and at a regional level. Using Scottish figures is unavoidable in many cases because of the level at which figures are collected – however, as the Lowlands & Uplands Scotland (LUPS) region includes the bulk of population and economic activity, it remains a strong indicator of the issues facing the region. Regional statistics are given at NUTS 2 and NUTS 3 level. The NUTS 2 regions are:

- <u>North-East Scotland</u> (including Aberdeenshire, City of Aberdeen and North-East Moray);

- <u>Eastern Scotland</u> (including Angus and Dundee City, City of Edinburgh, Clackmannanshire, East Lothian, Falkirk, Fife, Midlothian, Perth and Kinross, Scottish Borders, Stirling and West Lothian); and

- <u>South-Western Scotland</u> (including parts of Argyll & Bute, City of Glasgow, Dumfries and Galloway, East Ayrshire, East Dunbartonshire, East Renfrewshire, Inverclyde, parts of North Ayrshire, North Lanarkshire, Renfrewshire, South Ayrshire, South Lanarkshire and West Dunbartonshire).

Where specialised sources of data/research are used, these are cited in the text with the full references listed in the annex. General sources of statistics used in the analysis include: the Scottish Economic Statistics series, the Scottish Economic Report and the General Register Office for Scotland (GROS).

2.1 Demographic and Economic Context

Before providing a detailed analysis of the region's main development issues, the overall demographic and economic context are set here for the region.

Demographic context

In 2004, the <u>population</u> of the LUPs region was 4.711 million people, or 93% of the population of Scotland as a whole, an upward trend over the previous decade. Nevertheless, in terms of population change, there has been considerable variation: areas that have shown significant population growth since 1995 include West Lothian (10%), East Lothian (6%) and Stirling (5.5%), while those showing contraction include Aberdeen City (8%), Inverclyde (7.3%) and Dundee City (6.7%). The majority of the population is concentrated in the so-called Central Belt area around and between Glasgow and Edinburgh.

According to the General Register Office for Scotland, the population for Scotland as a whole is set to continue to rise to a peak of over 5.1 million in 2019 before slowly declining. At present, children aged 15 and under accounted for 19% of the population, as do people of retirement age. However, the number is projected to decrease by 15% from just under a million in 2004 to 790,000 by 2031 for Scotland as a whole. This is contributing to the number of working-age people falling by 7% from 3.18 million in 2004 to 2.96 million in 2031. At the same time, the number of people of pensionable age will increase by 35% from 0.97 million to 1.31 million over the same time period. The combined trends will increase labour demand pressures in the regional economy and suggest that policy will need to focus on how the labour market can be expanded.

One counter trend to population decline has been migration. Again, according to General Register Office population estimates for Scotland as a whole, in the year to mid-2005, there was a net migration gain of around 19,000, reflecting a net gain of around 12,500 people from the rest of the UK, a net gain of around 7,300 from overseas (including asylum seekers). The latter gain has represented a new trend in recent years with significant numbers of migrants coming from new Central and Eastern European Member States of the EU, particularly Poland. Migrants tend to be much younger than the general population with 69 % of overseas in-migrants aged 16-34 as compared to 24% of the Scottish resident population. Although potentially representing an injection of new skills into the regional labour market, many of the overseas migrants have substantial skills challenges relating to English language and 'converting' overseas skills qualifications into recognisable qualifications for Scottish employers (an issue relating as much to employer attitudes as to the nature of the qualifications themselves).

Economic context

GDP at basic prices for the LUPS region in 2003 was £74,298 million. The main contributing regions to GDP have been the major metropole areas, particularly the cities of Aberdeen, Edinburgh and Glasgow. In recent years, GDP growth has been improving, but the economy as a whole continues to perform less well than the wider UK economy.

The region's labour market has been performing well in recent years, with more individuals in employment than ever before. Employment rates are, and will remain partly dependent on broader global economic cycles and UK macro-economic factors. Both the employment rate and the economic activity rate (those in employment or seeking employment) for the region are at historically high levels. The employment rate for the period March-May 2006 stood at 75.3%, with the economic activity rate at 79.9%. The employment rate has increased by around four percentage points since 1999 with over 180,000 more people in employment than in 1999. Currently Scotland is fifth highest out of the 12 UK regions in terms of employment rates and also fifth in terms of economic activity rates. Moreover Scotland has higher economic

activity and employment rates than England, Wales, Northern Ireland and the UK as a whole.

Within the region, employment rates vary significantly as Table 1 shows. Above-average rates have been recorded in rural areas such as Aberdeenshire, Dumfries & Galloway, Midlothian, Perth & Kinross and Scottish Borders as well as Aberdeen City, East Dunbartonshire and East Renfrewshire, although the figures for rural areas do not take full account of levels of under-employment in these areas. The lowest rates of employment tend to be concentrated in urban areas such as Dundee City, East Ayrshire, Glasgow City, Inverclyde, North Ayrshire, North Lanarkshire and West Dunbartonshire, suggesting that the key cities of the region are not acting fully as economic drivers for labour market growth.

Table 1: Employment rates at Local Authority level

Local Authority	Employment rate (2006, %)
Aberdeen City	78
Aberdeenshire	80
Angus	77
Argyll & Bute (whole area)	77
City of Edinburgh	77
Clackmannanshire	73
Dumfries & Galloway	78
Dundee City	72
East Ayrshire	70
East Dunbartonshire	80
East Lothian	78
East Renfrewshire	79
Falkirk	76
Fife	77
Glasgow City	60
Inverclyde	71
Midlothian	79
Moray (whole area)	76
North Ayrshire (whole area)	72
North Lanarkshire	71
Perth & Kinross	78
Renfrewshire	74
Scottish Borders	78
South Ayrshire	74
South Lanarkshire	74
Stirling	76
West Dunbartonshire	71
West Lothian	76
Scotland average	75

Key messages

- Long-term population decline represents a potentially significant labour market challenge to the region.

- Inward migration, particularly from overseas, could bring new skills and dynamism into the regional economy.

- Overall, the region's levels of economic activity and growth remain relatively low, though there have been notable improvements in recent years.

- Employment rates for the region have improved in recent years, but there remains significant variations in employment rates across the region, particularly for the region's cities and urban areas.

2.2 Regional Challenges

Against the economic and demographic background, there are a number of challenges that affect the region as a whole. Foremost among them is the region's below-average productivity performance, but there are also constraints on the region's economy related to new firm formation rates, bottlenecks in enterprise development and the lack of full exploitation of the research and innovation centres in the region. At the same time, the region has key sectoral strengths that offer opportunities for economic growth.

Productivity

Productivity performance lies at the heart of regional competitiveness. As Chapter 3 will show, it has also been identified as the key challenge for economic development by the Scottish Executive. If Lowlands & Uplands Scotland is to be able to contribute to Lisbon Agenda targets, productivity growth will be a key aspect of economic development actions.

Productivity in Scotland is low and declining relative to the UK. In 2003, for Scotland as a whole, gross value added per head of population was 96% of the UK average, having fallen from 101% in 1995. Within the LUPS region, there is considerable variation in gross value added, ranging from 160% of the UK average in the City of Edinburgh, reflecting a concentration of high-value economic activities, especially financial services, to 62% in East and West Dunbartonshire and the eastern parts of Argyll & Bute. Other areas with low figures include Clackmannanshire/Fife, East and North Ayrshire, East Lothian/Midlothian, and the Scottish Borders – all are areas whose performance relative to the UK average had decreased since 1995. The worst performing regions share similar traits. These are areas that have lost more employment in manufacturing and agriculture than the rest of the Scottish economy; and manufacturing and services in those areas have systematically under-performed the Scottish average in terms of GVA per employee over the past decade.

Table 2: Gross value added relative to the UK average (%, 2003)

	1995	**2003**
Scotland	**101**	**96**
Aberdeen City/Aberdeenshire/North East Moray	140	131
Angus/Dundee City	97	86
City of Edinburgh	152	160
Clackmannanshire/Fife	78	70
East Ayrshire/North Ayrshire mainland	80	68
East & West Dunbartonshire/eastern Argyll & Bute	65	62
East Lothian/Midlothian	70	64
Dumfries & Galloway	85	75
Falkirk	101	84
Glasgow City	123	138
Inverclyde/East Renfrewshire/Renfrewshire	100	88
North Lanarkshire	73	75
Perth & Kinross/Stirling	96	83
Scottish Borders	86	68
South Ayrshire	93	86
South Lanarkshire	80	80
West Lothian	119	91

Source: Scottish Economic Statistics 2006.

Enterprise challenges

The Scottish corporate stock is relatively small. While Scotland had almost 130,000 enterprises registered for VAT in 2002, this was less than the average for the UK and the EU when measured per 10,000 population. In addition:

- The corporate stock is highest in the more prosperous North-East and East of Scotland, and lowest in the South-Western area. According to NOMIS data, it is particularly low in the Glasgow conurbation and, outside the South West, on Dundee, Fife, Falkirk and Clackmannanshire.

- Between 2000 and 2004, Scotland's corporate stock increased by 1.2%. This is lower than the UK average and substantially lower than in South East England.

Table 3: Scotland's corporate stock (2000-04)

	2004 stock per 10,000 population	**% change in stock 2000-04**
Scotland	250.4	1.2
LUPS region	236.6	1.5
- NE Scotland	363.8	-3.0
- Eastern Scotland	244.7	3.1
- SW Scotland	205.2	1.6
United Kingdom	305.6	3.5
South East England	355.4	4.2

Source: NOMIS, VAT Registered Companies.

In large part, this relates to the region's poor performance in replenishing its corporate stock with new enterprises. An indication of the number of new enterprises (ie. the enterprise birth rate) is given by the Global Entrepreneurship Monitor (GEM) data. These show the proportion of the working-age population either in the process of setting up a enterprise or having set up an enterprise in recent years, resulting in a figure called the Total Entrepreneurial Activity (TEA) index. While higher than countries such as Germany, Italy, Finland and Sweden, the Scottish TEA is below the UK, and countries such as France, Ireland and Spain. However, the Scottish average has been improving in recent years.

On the basis of VAT registrations, almost 11,850 new enterprises were set up in Scotland in 2004. The enterprise birth rate is below the UK average – although compared to other parts of the UK <u>apart</u> from the South-East, Scotland's performance is relatively good. Within the LUPS region, the lowest enterprise birth rate is in South-West Scotland (21 per 10,000 population) and the highest in the North East (27 per 10,000 population).

The LUPS region's relatively low enterprise birth rate has contributed to the region's economic growth lagging behind the UK average. There is limited evidence on whether the 'problem' is a low enterprise birth rate as such or a failure to generate high-growth new starts, resulting from a combination of factors discouraging entrepreneurship (eg. more difficult access to start-up capital) and encouraging employment with larger, existing organisations (eg. a relatively large public sector). Studies for Scottish Enterprise (Botham and Gallagher, 2000) using Dun & Bradstreet data suggest that to generate more high-growth new starts, Scotland requires an increase in the number of new starts overall, but particularly in sectors that are likely to generate increased economic growth. The Fraser of Allander Institute (2002) review of Scottish Enterprise's Business Birth Rate Strategy concluded that resources remained more usefully targeted at high-growth enterprises – recognising this issue, Scottish Enterprise established a dedicated High Growth Unit.

The higher and further education system is a particular potential source of high-growth start-up enterprises.

- The Scottish higher and further education sector protect more intellectual property than universities elsewhere in the UK. For the two academic years 2001/02 and 2002/03, they received 11% of all UK disclosures and made 17% of applications for new patents. They hold 20% of UK active patents in this sector.

- With 131 licenses, they have a disproportionately large share of the UK total (17%). Over these two years, they earned 23% of UK university earnings from licenses and spin-out companies.

In particular, Scotland's universities generated 9.6% of the UK's university spin-outs (ie. 50) in the two years 2001/02 and 2002/03. Per head of population, this is marginally above the UK average. However, the average spin-out remains relatively small with 11 employees and sales per employee of just £25,314, somewhat lower than the UK average of £28,130.

Key sectors

The region has seen a very significant structural change across industries in the last two decades. The transfer of jobs from the primary and manufacturing sectors to services has been highly significant, and will continue. Similarly, employment in professional and personal sector services has grown substantially and more than outweighs the fall in manufacturing and in skilled trades. These trends are expected to continue with the numbers of higher skilled and professional jobs rising and lower skilled jobs falling. Estimates suggested there will be half a million job openings expected between 2003 and 2008. Of these 36,000 will arise due to economic growth (an increase of 1.4%). The remaining 464,000 will arise to replace existing workers who leave the workforce or change their industry or occupation (Futureskills Scotland, 2004).

Services employment has been strong in certain sectors, particularly construction, retail, hotels/restaurants and financial intermediation (in the case of the latter two, reflecting Scotland's overall strength in tourism activity and financial services). With respect to manufacturing, Table 4 lists the key industries with respect to overall employment size and highest gross value added per employee (the economy-wide average for the latter is £42,200 to show comparisons). From this perspective, the largest sectors are the food and drinks industry, general engineering and machinery/equipment manufacture – of the significant employment sectors, only general engineering shows below-average productivity. High productivity is evident in the computer/ICT and chemicals sectors.

Table 4: Scottish employment/gross value added in selected manufacturing (2004)

Industry	Employment ('000s)	Gross value added per employee (£)
Food products/beverages	49	55,600
Chemical products/artificial fibres	14	76,300
Fabricated metal products	22	38,600
Machinery/equipment manufacture	20	44,400
Office machinery/computers	8	162,700
Radio/TV/communications equipment	9	55,500
Precision/optical instruments	11	55,200
Non-motor vehicle transport equipment	12	65,800

Source: Scottish Economic Statistics 2006.

Within the economy, there are a number of sectors whose future growth potential has been identified as key to overall regional development. Given the strong links between specific industries and business RTD investment, the industries and clusters fostered in Scotland will have a major impact on Scotland's RTD performance. Scottish Enterprise has identified the following important areas for growth.

- aerospace: with competitive advantages built on its airport links and historical links of key companies to the region;

- **chemicals**: with strong research links into the main universities, particularly in pharmaceuticals;

- **digital media and creative industries**: bolstered by the presence of regional TV/radio broadcast bodies and with strengths in software development, games industry and TV/radio programme content;

- **electronics**: based on the presence of a strong manufacturing presence of computer/ICT firms, despite the decline in foreign investment over the past decade, and strong research expertise in the region's academic institutions;

- **energy**: with the well-established oil/gas industry based on North Sea assets and the emerging growth of renewable energy technologies (as discussed below);

- **financial services**: through the strength of several regionally-based but globally-operating banks and expertise in specialist financial services, especially in Edinburgh;

- **food and drink**: drawing on the competitive advantage of distinctive drinks products (especially whisky) and food products linked to the region's marine and landscape assets;

- **forest industries**: based on the strong forestry assets of the region and concentrated in the more rural parts of the region;

- **life sciences**: a growing sector with a world-class research base in the region's universities, supported in large part by previous Structural Funds investment, and concentrated around the metropoles;

- **micro-electronics**: building on the research strengths of the region in semiconductor fabrication and system-level integration technology and concentrated in the Central Belt area;

- **opto-electronics**: again, supported by a strong research presence across the region;

- **textiles**: an industry that remains dynamic with strong export performance, despite global challenges, with a large concentration in the southern areas of the region; and

- **tourism**: a key sector for the region – particularly its rural areas, as discussed in more detail below – building on diverse cultural and natural assets.

Within these priority industries, it is worth drawing attention to the renewable energy sector, both because of the industry's growth potential in the region, its role as a driver of technology and innovation development in the region and its significance in wider issues such as climate change and reduced energy consumption. The sector's potential as a major export industry is significant for the whole of Scotland: according to Scottish Enterprise, potential renewable resources have been estimated at 59.1 GW, although domestic energy usage is only 10.5 GW.

Renewable energy potential in Scotland is diverse. The combined potential for offshore and onshore wind generation has been estimated at 36.5 GW while wave power could produce 14 GW and tidal, a further 7.5 GW. While there are infrastructure limitations to the development of UK markets – notably the lack of transmission capacity – there is significant scope for enterprises in the region developing technological competitive advantages in these areas. Moreover, scope exists for developing other forms of renewable energy potential, particularly biomass, which the Scottish Executive has estimated as having a potential to develop capacity of 0.45 GW.

In addition, other industries with local and national importance to the regional economy include the high-quality engineering sector, particularly areas such as marine engineering, and construction, especially in the wake of a number of major construction projects, such as the Clyde Gateway development.

Main Barriers and Constraints to Enterprises

Low productivity and corporate stock suggest a number of underlying weaknesses in the region's enterprise sector that require more in-depth analysis. Chief among these is the region's under-performing new firm formation rate, which is partly linked to the absence of critical resources for entrepreneurs and new firms, such as access to finance. At the same time, enterprises in the region have been slow to make full use of new technologies that can improve the efficiency of their businesses, particularly e-commerce and resource and energy efficiency. These separate issues are treated in the sections that follow.

New firm formation

The challenges of increasing enterprise growth in Scotland are manifold, but one of the critical areas of weakness is new firm formation, where Scotland trails UK and EU averages. The weakness here has contributed over time to a weakened enterprise stock that does not have sufficient capacity to generate the economic and employment growth that the region needs to make full contribution to the Lisbon Growth and Jobs Agenda.

There remain large numbers of 'would-be' entrepreneurs in Scotland. The Small Business Service (2003) found that 10% of the Scottish adult population (compared to 13% in England) are, or have recently been, thinking about setting up their own enterprise. Using a wider definition of 'would-be' entrepreneurs, household surveys for Scottish Enterprise show that up to 20% of the adult population are interested in entrepreneurship. However, the 'problem' is that Scotland's 'would-be' entrepreneurs are less likely to take action than those in England. Consequently, the key requirement is to stimulate action and to ensure the population has the skills and resources to convert their interest into action rather than to generate interest *per se.*

There are many inter-dependent factors which stimulate or constrain the willingness and ability of individuals set up their own enterprise. Some of these reflect Scotland's history and economic structures. At the level of the

individual enterprise, the perceived constraints have traditionally related to access to finance. This has several dimensions.

- Many enterprises are set up using the founders' personal finance, but some do not have the necessary savings to enable them to set up in business.

- Raising external finance (ie. from the banks) also requires that 'would-be' founders have access to personal savings or wealth to offer as security or meet bank 'gearing ratio' requirements.

- There is a some fear of taking on debt (presumably aggravated by the need to provide security from personal assets) and concerns about security (eg. leaving a job and concerns over potential enterprise failure).

For those who have decided to set up their own enterprise, there is a well-developed public sector support system, although there continues to be scope for addressing key bottlenecks in high-growth enterprises expanding, especially in capital because of the limits of the venture/equity capital market in Scotland. However, the key market failures are the number of individuals coming forward to establish enterprises and some gaps in the availability of development finance for enterprises. For the first need, the critical issue is to 'persuade' more people to set up their own enterprise, especially in sectors which are likely to contribute to wider economic growth. This focuses attention on the pre-start stage of the enterprise life-cycle. For the second need, there is a case for financing medium-sized development finance deals for SMEs.

Access to finance

Access to finance is not simply an issue affecting new enterprises. An evaluation of the West of Scotland Loan Fund – a public sector supported fund to finance SME growth in the West of Scotland area – identified the main reasons why companies of different sizes and maturities approach the Loan Fund for finance. The main reasons were that companies could not obtain finance elsewhere because they did not have collateral (28%), were unable or unwilling to give personal guarantees (25%) were at the limit of their available finance (20%) or did not have a track record (16%).

According to the survey of small businesses in Scotland report (Institute for Employment Studies, 2005), 18% of individuals faced obstacles in accessing finance. Over the past year, 11% of enterprises had sought finance – of those, 76% did not have any problem obtaining finance from the first source they approached, while 13% were unable to obtain any finance from their first source. In only 1% of cases was the business being considered 'too risky', the reason behind finance being refused. More common reasons for finance being turned down were a lack of security (26%) and poor business performance (23%). Access to, and the cost of, finance has diminished in terms of importance over the last 20 years to historically low levels. The current relatively low and stable interest rate environment is a major factor and also, with an increasingly competitive UK finance market, banks appear to be paying more attention to the needs of small and growing firms – although how

long term this will be may depend on the continuing stability of UK monetary policy.

Nevertheless, in the region, access to venture capital and loan finance was recognised as a key market failure in the 2000-06 programming period and was consequently supported by ERDF interventions. In 2006-07, in part to identify whether there remained a continuing market failure in the region and to examine the performance of existing funds, the Scottish Executive commissioned a major evaluation of ERDF-supported Venture Capital and Loan Funds (VCLFs) in Scotland by the consultancy, CSES.

The evaluation produced a number of interesting results of importance to the 2007-13 Programme. First, it underlined the different types of impacts produced by different types of funding. Loan finance tends to produce greater increase in the number of <u>jobs</u> provided, while venture capital tends to support increases in the <u>turnover</u> of companies in which investments are made. This is to some extent a result of their respective investment policies and the nature of the firms they support, with venture capital finance going particularly to innovative companies and those exploiting academic research commercially.

Second, and more importantly, the evaluation highlighted the need for continuing targeted support of SMEs at particular stages in development. Until the establishment of the Scottish Co-Investment Fund – part supported by funding from 2000-06 ERDF Programmes in the LUPS area – only 8% of companies financed by venture capital were based in Scotland. As with elsewhere in the UK, there had been a substantial fall in venture capital investment in the region combined with a re-orientation away from early-stage to later-stage investments.

- Taking early-stage investments, just £7 million was invested (2.7% of the UK total) in 22 enterprises (5.1% of the total).

- While 'business angel' activity has been relatively healthy in Scotland, institutional venture capital has largely withdrawn from the start-up market and joint investments with business angels. Increasingly joint private-public sector early stage funds are having to fill the gap (Don and Harrison, 2006).

The CSES evaluation confirms the view that ERDF-supported VCLFs have addressed areas of market failure, but that there remains market failure for enterprise finance in the region – not only for the size of deals addressed by the existing VCLFs, but for deals of higher amounts as well. As part of the evaluation, discussions with the financial community, and with the Investment Partners of SCF, suggested that the decline in availability of venture capital in Scotland arising from the effects of the 'dotcom bubble' of the 1990s continues. In particular, the Investment Partners of SCF considered that there was a market failure above the deal level at which SCF now operates. Most partners said that a market failure remains for deals over £2 million (the SCF deal ceiling), which could be addressed through an investment vehicle with a limit of up to £5 million. The recent launch of the Scottish Venture Fund

provides such a vehicle, but its scope remains limited given the size of market failure identified in the CSES evaluation.

CSES made several policy recommendations. In particular, the primary focus of future funding should be on the following areas:

- providing funding for the continuing operation of SCF or alternative venture capital funds, subject to satisfactory financial performance which should be monitored as shown below – if the fund meets its targets it should become self-sustaining after the 2007-13 period of ERDF funding;

- providing funding, subject to other priorities, to cover the market failure gap between the £2 million and £5 million deal level; and

- considering the introduction of further finance into the micro finance area, possibly aimed at special groups such as are served by the Princes Scotland Youth Business Trust source of finance.

E-commerce

Another important constraint on the region's enterprises is their take-up of ICT and full participation in the knowledge economy. With the accelerating developments in internet technology and e-commerce applications of that technology, it is essential that enterprises are able to make full use of the nearly universal broadband coverage in the region (to which investment infrastructure by past Structural Funds programmes have made significant contributions). Enterprises are making increasing use of broadband in Scotland – the share of business activity transacted through e-business rose from 17% in 2001 to 20% in 2004, higher than the UK average (DTI, 2004). However, Scotland continues to lag behind key competitor countries in other parts of the EU and North America, with continuing challenges in enterprises recognising the potential of e-commerce and having the skills to exploit the technology. This challenge is particularly relevant for new enterprises, especially in non-ICT sectors, where enterprise growth and survival could be improved through a better use of e-skills and opportunities.

Energy and resource efficiency

Enterprise growth is increasingly shaped by a sustainable development framework which recognises the need for industry to contribute to overall reductions in CO_2 and pressures on traditional energy sources such as oil and gas. Under the Kyoto Protocol, the UK Government is committed to reducing the UK's 1990 CO_2 emission levels by 12.5% by 2010, and has an 'internal' target of a 20% reduction. At the level of individual enterprises, increasing energy and resource efficiency, while not only contributing to climate change goals for Scotland, can also have clear benefits to reducing overall costs – for example, Scottish Executive figures suggest that the 157 enterprises using the Loan Action Scotland scheme (an initiative to encourage greater carbon savings through loans to enterprises) to reduce energy consumption are estimated to make total estimated savings of £7.1 million and lifetime carbon savings of 40,000 tonnes of carbon. Encouraging new enterprises in particular

to develop energy and resource efficiency processes could promote a wider enterprise culture that would embed such sustainable development approaches. As the need to adapt business practices and processes to the challenges of climate change increases, it is critical that enterprises address any barriers to making these changes.

Research and innovation

Research and technology development (RTD) and wider product and enterprise innovation have been a key focus of economic development policy efforts to improve regional competitiveness. European Structural Funds are expected to make a significant contribution to the objectives of the Lisbon Strategy, which identifies RTD and innovation as fundamental drivers of economic growth. The Strategy calls for the increased leverage of business RTD funding – this is particularly important in Scotland, where business RTD lags significantly behind the UK and EU averages.

While in terms of policy interventions RTD/innovation should not be separated from wider support for enterprise growth and development, it is worthwhile examining the region's performance in this area in detail. This section reviews available evidence to establish the need for intervention by:

- outlining the region's innovation and enterprise development performance in both a UK and European context; and

- describing, where possible, regional variations in performance.

On the basis of this evidence, it identifies areas of market failure where ERDF intervention can add value, not least because Scotland's overall RTD and innovation performance remains poort.

- Compared to much of Europe, the proportion of UK and Scottish companies introducing product and process innovation is low. On the other hand, the firms which do innovate obtain a much higher proportion of income from their new or improved products than most of Europe.

- UK firms are near the top of the list for innovation in the areas of management/strategy/organisation (or at least management change). This applies to both innovators and companies not undertaking product or process innovation.

The relative number of innovating enterprises in Scotland compared to the UK average, and especially the high-performing South-East England, is low.

- Scotland has only 70% of the national (GB) average number of product innovating firms.

- For process innovation, the number of firms is 20% below the UK average.

This is confirmed by Eurostat data on patent applications. The number of applications per million population in Scotland (95) is well below the EU-25

average (135). Moreover, gross expenditure on RTD in Scotland in 2003 only amounted to 1.53% of GDP. This is below the UK average and the figure for the EU-25 (as seen in Table 5). Per capita expenditure in Scotland lags both the UK and EU-15 figures.

Table 5: Gross expenditure on RTD (2003)

	Scotland	**UK**	**EU-25**
% of GDP	1.53	1.81	1.85
Euro per capita	0.40	0.51	0.41

Source: Scottish Executive (2005c) Research and Development Expenditure and Employment by Business: Comparisons with the UK.

The structure of Scotland's RTD differs greatly from both the UK and the EU.

- Business RTD accounts for 38% of Scotland's RTD. In the UK and EU-25, business expenditure accounts for 68%, and 64% of gross expenditure.

- In contrast, research expenditure in Scottish universities is an above-average proportion of RTD (42% of expenditure) compared to the UK (22%) and the EU-25 (22%).

- Expenditure in the government sector also accounts for a relatively high proportion (20%) of Scottish RTD (allocated to Scotland on a per capita basis). This compares with 10% in the UK and 14% in the EU-25.

Table 6 shows the absolute level of expenditure and Scotland's share of UK expenditure. Gross expenditure in 2003 was £1.36 billion or 6.8% of the UK total. There have been substantial increases (25%) since 2000, accounted for by growth in enterprise, higher education and Government RTD (in the latter case, potentially as a result of devolution). However, as a share of UK expenditure, enterprise RTD in Scotland remains considerably below what might be expected on the basis of population or GDP shares.

Table 6: Research and development expenditure by source

	2000		**2003**	
	Amount (£m)	*% of UK*	*Amount (£m)*	*% of UK*
Enterprise	400	3.5	523	3.8
Government	238	11.2	271	13.5
Higher Education	440	12.1	595	13.9
Total	1,078	6.2	1,367	6.8

Source: Roper et al. (2006).

Business RTD is a critical input to the innovation process (especially within manufacturing). Internal corporate RTD is also an important determinant of a company's capacity to absorb and utilise externally generated knowledge and technology. Over recent years, Business RTD has risen considerably from £269 million (or 2.9% of the UK total) in 1997 to £521 million (3.8% of the UK total) in 2003. Nevertheless, the table below shows it remains well below the

European (and UK) average. Scottish enterprises spend £319 per employee on RTD. This compares with the UK figure of £702. They also spend less per employee engaged in RTD.

Table 7: Business expenditure in RTD

	Scotland	**% of GDP**		
	£m	*Scotland*	*UK*	*EU-25*
1999	269	0.53	1.25	1.13
2000	400	0.53	1.21	n.a.
2001	512	0.65	1.27	1.17
2002	640	0.77	1.25	1.17
2003	521	0.58	1.23	1.17

Source: EUROSTAT.

Furthermore, according to the Scottish Executive (2005), what business RTD exists in Scotland is concentrated.

- By sector: Almost two-thirds of expenditure is in three sectors: pharmaceuticals, precision instruments, and communication equipment/electronic components. Recent growth has been driven largely by the pharmaceutical (especially biotechnology) sector.

- By ownership: Overseas inward investors undertake 63% of Scottish enterprises' RTD, comparing with only 29% by indigenous Scottish enterprises.

- By size of firm: Small enterprises undertake a larger share (17%) of Scottish RTD than in the UK (10%). However, this is a higher share of a much smaller total. Consequently, SME RTD expenditure per capita is lower than the UK average.

RTD is also concentrated in particular parts of the country, largely based around the main academic research centres and foreign business clusters. Eastern Scotland is the main location with Edinburgh and West Lothian between them accounting for almost 50% of expenditure, although there are significant concentrations in Glasgow and Dundee as well.

Expenditure on RTD is only one input to the innovation process. Innovation also requires expenditure on, for example, the acquisition of knowledge, design, equipment, training and marketing. Table 8 shows expenditure per employee on RTD and total innovation in Scotland and elsewhere in the UK.

Table 8: Expenditure per employee on RTD and innovation (£)

	RTD	**Other innovation expenditure**	**RTD as % of innovation**
Scotland	877	1,191	42
UK	1,542	1,665	48

Source: Michie et al. (2005) The Community Innovation Survey, Table 4.1, p. 32, Report for the Scottish Executive.

Main Barriers and Constraints to Research and Innovation

The low level of RTD and innovation reflects *inter alia*:

- Scotland's industrial structure with medium/high-tech manufacturing and high-tech services being under-represented (relative to both UK and EU averages).

- The limited presence of two of the UK's most RTD-intensive industries in Scotland's economy (ie. aerospace and automotive sectors).

Scottish and UK companies tend to cite the same constraints on RTD and innovation. The most frequently quoted factors, both by innovators and non-innovators, are the cost and risk of investing in innovation, combined with the cost and availability of finance. Given that much innovation is financed from retained earnings, the cost and availability of finance is influenced by both past company performance (ie. profitability) and problems of raising external finance.

Innovation requires expenditure (ie. investment) ahead of the generation of income arising from successful innovation. As such, it creates risk via its initial negative impact on cash flow. The payback period, especially from investment in RTD, can be long term. Furthermore, not all innovation is successful (eg. new products). Consequently, there is no one-to-one or automatic cause-and-effect relationship between investment in innovative activity and company success (or even survival). Innovation is a risky business, even if sometimes required to survive. The risks are most severe for small companies while small, young companies are also more dependent, almost by definition, on raising external finance for innovation (ie. they have fewer retained earnings).

A larger proportion of innovators (particularly in indigenous and in small enterprises) quote financial constraints than non-innovators. This is because many of the non-innovators see little need and few opportunities to innovate or calculate that the cost will outweigh the benefits in terms of additional revenue. Not surprisingly, they do not perceive finance as a barrier (with the exception of retained earnings). The majority of non-innovators say they are highly unlikely to invest substantially in RTD and innovation.

Nevertheless, there is a substantial minority of 'potential innovators'. For these, access to finance is a constraint. For those already involved in innovation, access to finance constrains the level of investment in RTD and innovation. These constraints are most severe for small and young enterprises (DTZ Pieda, 2004).

These issues apply across Scotland, although there are spatial variations in the pattern of RTD/innovation – as noted, the key centres for RTD/innovation tend to be concentrated in the major metropole areas, where the major universities and the bulk of large companies undertaking significant RTD are based. Statistics do not allow a detailed analysis of differences within the region. In any case, while the enterprise needs of RTD/innovation will vary within the region, the issues identified in this section remain consistent across

the bulk of the region and consequently, support should be devised within a pan-regional framework.

In this context, it is important to remember that innovation is not simply the direct application of technological ideas in the creation/improvement of products, but includes wider, systematic improvements in enterprise services and business processes. This wider definition takes account of the differences in the scale and nature of innovation in different industries – for example, innovation in 'high-tech' industries tends to be more closely linked to technological developments, whereas in 'lower-tech' industries, innovation can take the form of enterprise-specific, incremental changes in production processes.

For all innovation though, there are two common sets of issues for enterprises:

- access to key sources of new ideas, whether new technological developments or new approaches to other business processes; and

- internal enterprise capacity, skills and willingness to embed innovation throughout all the firm's activities.

Addressing both issues is essential in improving innovation growth across the region.

Key messages

- Similarly, the region's <u>productivity performance</u> is also comparatively limited, but with significant variations at sub-regional level.

- The region has a <u>low new firm formation rate</u>, despite the presence of a significant number of 'would-be' entrepreneurs.

- One of the key issues for new firm formation and survival is <u>access to finance</u>, but the market failure is concentrated in selected parts of the market rather than widespread.

- The region has an improving performance in <u>e-commerce</u> among its enterprises, but it continues to lag key comparator countries in the EU and North America.

- <u>Resource and energy efficiency improvements</u> in the business processes of the region's enterprises could contribute significantly to overall improved cost efficiency and contribute to reducing carbon emissions.

- Overall, the region has low rates of <u>RTD spend</u> relative to the economy. It is particularly low for businesses, where expenditure per employee is significantly below UK averages. Much of the existing business RTD spend has been made by large, foreign-owned firms, with low shares of spending in indigenous SMEs.

- Lowlands & Uplands Scotland has a <u>strong university research sector</u> with strong opportunities for commercialisation and spin-outs, though much of it is concentrated in the metropole areas of the region.

- Industrial <u>research strengths</u> are notable in some technologies and sectors in the region, such as chemicals, life sciences, micro- and opto-electronics and renewable energy.

2.3   Sub-Regional Challenges

Economic performance across Scotland is mixed. The challenges facing the economy are not simply systemic, but reflect the operation of local circumstances, often working in tandem to produce pockets of severe economic and social deprivation. If the LUPS region is to make its full contribution to the Lisbon targets, then all parts of the region must be able to make strong contributions. Indeed, the Community Strategic Guidelines make clear the importance of urban communities being able to make full contributions to the Lisbon growth and jobs goals and encourage the Structural Funds to give particular attention to the urban dimension.

While economic performance varies sub-regionally, one of the key distinctions between different parts of the region lie in the different challenges facing urban and rural parts of the region. Economic activity in the region tends to be centred on the main metropoles and Glasgow, Edinburgh and the region's cities are increasingly acting as growth poles for larger city-regions. However, for some urban areas, intense concentrations of poverty and worklessness have led to communities that lack the capacity to reverse economic decline and social exclusion. Similarly, the more peripheral, rural parts of the region, while facing different development challenges in under-employment, low earnings, distance from markets and dependence on primary industries, also have local economies that can be locked in cycles of economic decline. Although these areas often experience the same challenges facing the region as a whole, the issues distinct to them need to be examined.

Urban challenges

For several urban communities within the region, a series of debilitating factors have worked to make a 'vicious cycle' that has led to entrenched deprivation, low rates of economic activity and high rates of worklessness. Regeneration of such communities represent the main urban challenge for the Programme. Within that challenge, there are a number of issues working in combination to create these vicious cycles: concentrations of social exclusion, as measured by high levels of worklessness low levels of educational attainment, poor health and other indicators of poverty. In such concentrations, indigenous economic activity can struggle to grow and access to 'external' sources of economic activity (particularly enterprises attracted to the area) becomes increasingly more limited.

Community regeneration embraces a number of different policy interventions that address such concentrations of deprivation by focusing on the multiple reinforcing factors causing the problems, including initiatives on housing, health and education. Structural Funds are limited by scale and focus on the more directly economic policy areas. Consequently, this section outlines the evidence on and barriers affecting local variations in economic and social

disparities, particularly among disadvantaged communities (in effect, analysing the problems) as well as SME activity in disadvantaged communities (in effect, analysing the ability of communities to address these problems).

Urban Deprivation

Statistics to compare community disadvantage across European regions are not readily available. The analysis here is primarily confined to the Scottish Index of Multiple Deprivation (SIMD), which is a combination of six stand-alone indicators: current income; employment; education, skills and training; health; housing; and access to local services.

Not surprisingly, given the nature of the measures, urban areas are more likely to display the worst concentrations of social exclusion and poverty as defined here. Other measures can capture problems which are more endemic to rural areas. For example, the access to services indicator measures drive times to key services and is a proxy for rural disadvantage, including variations in access to local services, such as General Practitioners, primary school and supermarkets, across Scotland. However, as a measure of *urban* deprivation, it remains the most robust measure of social exclusion.

Table 9 gives an overview of the concentrations in Scotland using the SIMD at NUTS 3 level for the region's Local Authority areas. Concentrations are the areas where the different processes measured by the indicators combine to create particularly persistent areas of economic and social poverty – so, for example, poor educational performance, bad housing, low levels of health and limited access to key services (such as childcare and transport) can result in high rates of worklessness and manifested in relatively large numbers of claimants of state benefits. Because the factors tend to work together, areas that 'score' highly on several if not all indicators are likely to be those most resistant to initiatives to raise economic activity, whether in terms of the creation of wealth within the area itself or the ability of individuals/organisations within the communities to access neighbouring areas of opportunity.

The table concentrates on the worst concentrations of deprivation as measured at the 15% level, examining the incidence in terms of shares of data-zones relative to Scotland as a whole and relative to the Local Authority in question. From the table, deprivation has been concentrated in some parts of the region. Glasgow City shows a particularly high concentration – whether measured in national or local terms – and there are similar above-average concentrations in surrounding areas such as Inverclyde, North and East Ayrshire, North and South Lanarkshire, Renfrewshire and West Dunbartonshire. In the eastern part of the region, Clackmannanshire and Dundee City have relatively high concentrations as well as the City of Edinburgh, despite its relative overall prosperity.

Table 9: Concentrations of Scotland's 15% most-deprived data zones by LUPS Local Authority area (2006)

Local Authority	% of total Scottish data-zones	% of total Local Authority data-zones
Aberdeen City	2.8	10.1
Aberdeenshire	0.6	2.0
Angus	0.8	5.6
Argyll & Bute (whole area)	1.0	8.2
City of Edinburgh	6.5	11.5
Clackmannanshire	1.5	23.4
Dumfries & Galloway	1.1	5.7
Dundee City	5.4	29.6
East Ayrshire	2.9	18.2
East Dunbartonshire	0.3	2.4
East Lothian	0.1	0.8
East Renfrewshire	0.3	2.5
Falkirk	1.9	9.6
Fife	4.8	10.4
Glasgow City	33.8	47.6
Inverclyde	4.3	38.2
Midlothian	0.5	4.5
Moray (whole area)	0.0	0.0
North Ayrshire (whole area)	3.4	18.4
North Lanarkshire	8.6	20.1
Perth & Kinross	0.9	5.1
Renfrewshire	3.7	16.8
Scottish Borders	0.3	2.3
South Ayrshire	1.3	13.6
South Lanarkshire	5.7	22.1
Stirling	0.7	7.3
West Dunbartonshire	3.4	28.0
West Lothian	1.4	13.3
Scotland	**100.0**	**15.0**

Source: Scottish Index of Multiple Deprivation.

Concentrations of disadvantaged households take hold for different reasons in different places, but there are three main explanations put forward by the Social Exclusion Unit:

- <u>Changes in the nature and location of jobs</u>
    - A key local employer or industry closes down.
    - Lack of accessible jobs.
    - The informal economy can provide income opportunities which make formal work less attractive, especially when combined with benefits.

- Residential sorting
    - The housing market 'groups' the most disadvantaged people together.
    - Residents with sufficient financial resources can choose to move out of poorer neighbourhoods.
    - Housing policy can unintentionally exacerbate residential sorting.
    - Over half of all people moving into Scotland's 10% most deprived data zones were previously living in the 10% most deprived.

- Area effects. Residents' chances of finding work can be reduced simply because of where they live.
    - *Place effects* – these include location, poor infrastructure, lack of transport, competition for limited number of job or training opportunities, and variation in the quality and quantity of local services – these can combine to making such areas unattractive to businesses moving to these communities as well as stifling indigenous enterprise development.
    - *People effects* – these relate to the damaging effect of living with many other jobless people – for example, residents receive little information about jobs or encounter area-based discrimination by some employers.

In turn, these explanations can lead to a:

- skills mismatch – an imbalance between the characteristics of potential workers and the attributes required by local employers; and

- spatial mismatch – a geographical mismatch between residences and potential workplaces.

The Social Exclusion Unit, in reviewing UK and international studies, argued that it matters if jobless people are concentrated in the same areas.

- Living in these areas can damage a person's life chances – especially those of children and young people.
    - Individuals living in deprived areas are significantly more likely to be out of work than similar people living elsewhere.
    - Children's educational attainment is closely linked to the level of neighbourhood poverty. For example, only 46% of pupils living in Scotland's 15% most deprived data zones attained expected standards in writing at the end of primary school. The Scottish average is 61%.

- Residents have lower expectations of finding a job and a lower probability of actually starting a business.

- A significant number of children are in danger of growing up in families and neighbourhoods with little contact with the world of work and a lack of positive role models.

In addressing these barriers and constraints, research undertaken by the CEEDR (ODPM, 2003) on the evidence for successful enterprise-led

regeneration in deprived areas looked at the contributions of different types of enterprises. Economic growth for these areas is dependent on a combination of indigenous enterprise development, the attraction of outside businesses to the areas to act as significant local employers and the ability of residents to access good employment opportunities outside of the region. The latter activity is more appropriate to interventions through the ESF Programme for the region. However, with respect to the first two activities, the benefits can be summarised as follows.

- Enterprises provide employment opportunities to local residents. Their earnings can then be spent in the local economy which increases demand.

- Enterprises can boost the local economy by purchasing their requirements for materials, components and services locally.

Rural challenges

As will be seen in the next chapter, the Community Strategic Guidelines emphasise the importance of a territorial dimension in the 2007-13 Structural Funds programmes. This is as important for rural areas as for urban communities. The challenges of rural development involve a complex balance of addressing the specific challenges of peripherality and economic sustainability in rural areas and making sustainable economic use of its key assets, such as the environmental landscape, alternative energy sources and the competitive advantages within traditional rural activities.

Rural areas have been characterised by a number of distinctive economic and demographic features (Scottish Executive, 2000):

- population levels declining relative to Scotland's population growth, particularly when forecast over the programming period (although there are some rural areas where it is growing, such as the Scottish Borders);

- a population ageing at a greater rate than Scotland as a whole;

- key deficiencies in infrastructure, particularly road and rail transport (exacerbating peripherality in many areas) and higher and further education (contributing to out-migration of young people) – for example, although there have been improvements in recent years in higher and further education provision in areas such as the South of Scotland through the investments in the Crichton campus, the absence of a strong college network and local university presence continues to weaken the area's skills and research base;

- a reduced workforce, driven by the out-migration of young people from rural areas;

- an over-reliance on certain key sectors characterised by low and sometimes stagnant productivity levels, such as agriculture;

- an economy dominated by small enterprises, particularly relative to urban areas; and

- median earnings that are lower than the Scottish average.

These are discussed in more detail below.

Geographical Distribution of Rurality

Table 10: Rurality in different LUPS Local Authority areas (2005)

Local Authority	% of population in accessible/remote rural areas	% of population in accessible/remote small towns
Aberdeen City	2.9	4.1
Aberdeenshire	53.4	19.9
Angus	26.5	12.1
Argyll & Bute (whole area)	52.0	29.9
City of Edinburgh	1.4	2.8
Clackmannanshire	15.0	31.3
Dumfries & Galloway	22.6	49.0
Dundee City	0.5	0.0
East Ayrshire	27.6	35.9
East Dunbartonshire	7.1	6.8
East Lothian	27.8	47.7
East Renfrewshire	4.4	9.3
Falkirk	9.4	4.6
Fife	17.9	16.4
Glasgow City	0.2	0.0
Inverclyde	7.6	4.8
Midlothian	18.8	15.0
Moray (whole area)	42.6	32.5
North Ayrshire (whole area)	12.1	17.3
North Lanarkshire	7.4	10.9
Perth & Kinross	45.9	20.5
Renfrewshire	5.4	9.5
Scottish Borders	48.3	24.8
South Ayrshire	21.8	10.3
South Lanarkshire	12.2	9.5
Stirling	38.4	9.2
West Dunbartonshire	1.4	0.0
West Lothian	11.6	17.6
Scotland	**18.4**	**12.8**

Source: Scottish Executive Urban-Rural Classification 2005-06.

Rurality can be defined in terms of settlement size and access. The Executive's core definition of rural is based on the six-fold Urban/Rural classification. Within this system, a strong measure of rurality is the two classifications 'remote rural' and 'accessible rural', as jointly defined as settlements of less than 3,000 people and within 30 minutes driving of

settlements of 10,000 or more. At the same time, there are many parts of the region are 'semi-rural', as defined by the categories 'remote' and 'accessible small towns': ie. settlements of between 3,000 and 10,000 people and within 30 minutes drive of a settlement of 10,000 or more. In many cases, these small towns are the local growth poles for a wider rural hinterland.

Table 10 sets out the geographical distribution of rurality in terms of 'rural' and 'small town' groupings with the six-fold classification. Examining the 'rural' category, rurality is distributed throughout the region, with the following Local Authorities having significantly above-average shares of their population in these areas: Aberdeenshire; Argyll & Bute; Dumfries & Galloway; Moray; Perth & Kinross; Scottish Borders; and Stirling.

Rural Economic Activity

Economic activity in rural areas is characterised by a combination of overall low productivity, high rates of employment (but also high rates of part-time and under-employment) and relatively low earnings. With respect to productivity, as Table 2 above showed, rural Local Authority areas had gross value added per capita figures that were significantly lower than the Scottish average (apart from Aberdeenshire, where the impact of Aberdeen City and the oil-gas industry may be concealing more directly rural features).

Despite the low productivity, rural areas appear to have strong employment performance. Table 11 summarises the comparative performance of rural areas in relation to employment, unemployment and inactivity rates, based on the six-fold urban-rural classification.

- Employment rates in rural areas are significantly above the Scottish average (and have improved in recent years).

- Conversely, unemployment and inactivity rates are well below the Scottish average.

Table 11: Employment, unemployment and inactivity rates (%) of working-age population

	Employed	Unemployed	Inactive
Large urban areas	70.9	7.6	23.3
Other urban areas	73.0	7.2	21.3
Accessible small towns	73.6	8.1	19.9
Remote small towns	78.5	4.0	18.3
Accessible rural	78.2	4.4	18.2
Remote rural	78.4	5.9	16.7
Scotland	73.4	6.8	21.2

Source: Scottish Executive (2003).

However, it is likely that the averages for rural areas disguise significant inequalities in economic activity with the high employment rates of high income, long-distance commuters possibly cancelling out lower economic

activity rates for low skilled, low income people more dependent on local job opportunities. This polarisation can also have serious consequences for house prices and potentially for local labour supply. At the same time, rural areas can significantly differ from each other in terms of their main sources of income – for example, the rural hinterland surrounding major urban metropoles such as Edinburgh tend to have a more significant role as commuting zones for city workers than more isolated rural areas.

Rural areas are strongly characterised by self-employment, part-time employment and under-employment.

- <u>Self-employment</u> is much more prevalent in rural areas (Scottish Executive, 2003). This reflects the importance of micro/small enterprises in sectors such as agriculture and tourism and is often associated with low average wages. It does not represent a greater entrepreneurialism in rural areas, but an apparent lack of alternatives (Yellowbook, 2003). Moreover, evidence of the importance of smaller employers in the rural economy shows that 24% of employees in rural Scotland continue to work in workplaces with less than ten employees, compared to just 16% of employees in the rest of Scotland (Futureskills Scotland, 2005). In contrast, 27% of employees in the rest of Scotland work in workplaces with 250 or more employees, compared to just 11% of employees in rural Scotland.

- <u>Part-time employment</u> is much more common in remote rural areas than in Scotland as a whole. This reflects the thinner economic base in more sparsely populated, remote communities and the difficulties in sustaining full-time employment.

- <u>Under-employment</u> is a particular problem in rural areas. It can take a variety of forms, including taking on a job for which a lower qualification is required, or working for less time than one would like to. A measure of under-employment that captures the latter is the amount of people in work that would like to work more hours for the same pay. According the Annual Population Survey, when individuals were asked if they would want to work longer hours for the same pay, the Local Authorities with the highest share of respondents were those most characterised as 'rural' using the six-fold classification. This lends support to the idea that there is more under-employment in rural areas.

Seasonality of employment can also add to under-employment. Futureskills Scotland (2005) found that 28% of workplaces in rural Scotland had a workforce fluctuating seasonally, compared to 23% in the rest of Scotland. Temporary contracting was also much more common in rural areas.

Rural areas are also characterised by lower earnings, arising from this combination of self-employment, under-employment and concentrations of employment in lower-earning sectors such as agriculture and tourism. For example, in 2006, Dumfries & Galloway had median earnings 9% below the Scottish average and the Scottish Borders 18%.

It is also worth drawing attention to the importance of tourism, which is a particularly significant employer in many rural areas, with employment in hotels and restaurants – often strongly linked with wider changes in the tourist industry – representing a higher proportion of total employment in rural areas, compared to Scotland as a whole. Other evidence of the contribution of tourism to the rural economy comes from the Scottish Recreation Survey (Scottish Natural Heritage, 2005). This found that just under two-thirds of the Scottish adult population had made at least one visit to the outdoors for leisure or recreation purposes in the last 12 months – equivalent to 189 million visits. As the average spend was £22 per trip, they estimate that the total value to the rural economy was £4.2 billion.

Barriers and Constraints to the Rural Economy

One of the key features of the rural economy is the concentration of employment and economic activity in primary industries. Futureskills Scotland (2005) found that:

- employees in rural Scotland were more likely to work in agriculture, forestry and fishing, energy, water and construction, hotels and restaurants, and health and social work than those in the rest of Scotland, and show a strong representation in other sectors such as renewables, food and drink, textiles and tourism; and

- rural Scotland was significantly under-represented in financial intermediation and real estate, and is slightly under-represented in transport, storage and communications; public administration and education; and other services.

These statistics suggest that rural Scotland is more heavily dependent on traditional primary sector-based industries and the public sector for employment opportunities. In the case of agriculture and fishing, rural economies are often still dependent on employment in declining sectors, making it important that opportunities to diversify the industrial base of these economies are pursued. As noted above, some of the sectors have been identified as potential growth sectors by Scottish Enterprise, particularly food and drink, forestry, textiles and tourism.

Whilst there are many barriers faced by both rural and urban areas, rural areas face some additional barriers and the ways in which the barriers affect residents and the extent to which they do so are often more strongly felt in rural locations. SMEs located within rural locations face a number of critical issues (Smallbone et al., 2002):

- small local markets and distance to key urban centres with higher costs associated with accessing markets for businesses;

- relatively poor transport services and infrastructure, particularly with respect to road and rail connections in many rural areas (as seen in higher average transport costs for individuals in rural areas);

- few chances to do business with and communicate with local firms due to the small number of local companies in actual numbers rather than densities;

- distance from sources of key centres for industrial RTD and innovation, particularly with respect to higher and further education, which are clustered in the metropole parts of the region;

- shortage of industrial property for enterprises in some rural areas;

- skills shortages caused by restricted local labour markets and the absence of higher and further education institutions in many rural areas (though this has begun to change with, for example, the development of the Crichton campus in Dumfries);

- a shortage of accessible training schemes/courses; and

- remote location teamed with a lack of affordable housing and higher/further education opportunities, contributing to out-migration of young people.

The issue of access to services is particularly acute for rural areas. According to the SIMD, nearly 20% of people in remote rural Scotland are more that 15 minutes drive away from their doctor. Similarly, access to petrol stations is a particular problem in remote rural areas, especially given the dependence on personal transport because of more limited public transport options.

Key messages

- Concentrations of economic and social deprivation have led to <u>urban communities</u> experiencing 'vicious cycles' of economic decline. In the Lowlands & Uplands Scotland area, some urban communities show particularly low levels of economic activity, health and educational attainment among other measures.

- Within an ERDF context, regeneration of such communities would require activity focusing on <u>enterprise-led growth</u>, improving the conditions of these communities for enterprise growth, their attractiveness to external businesses as well as the ability for residents to access employment opportunities in neighbouring growth areas.

- Rurality characterises much of the region. <u>Rural areas</u> have distinctive economic challenges, including lower productivity and earnings, high dependency on primary (and, in some cases, declining) economic activities and high levels of part-time and under-employment.

- <u>Enterprises in rural areas</u> face key development bottlenecks related to access to key markets, distance from important sources of skills and research and innovation.

- Rural areas have <u>critical infrastructure deficiencies</u>, most prominently relating to transport and higher and further education.

2.5   Summary of Key Challenges

As has been stated, this socio-economic analysis has not set out to be a comprehensive analysis of the strengths and weaknesses of the region's economy. Instead, it has sought to identify the issues that are most pertinent to intervention by the ERDF, as defined within the Community Strategic Guidelines and the Structural Funds regulations. In this final section, on the basis of the statistical evidence presented above, a summary of the key issues to be addressed in the Programme is presented: first, an analysis of the main strengths, weaknesses, opportunities and threats for the region's economy; and second, a more detailed identification of the key challenges for the Programme.

SWOT analysis

Regional Strengths

- Lowlands & Uplands Scotland has had a relatively strong economic and employment performance in recent years, characterised by relatively <u>low unemployment rates</u>, although this conceals some significant weaknesses.

- The region has a <u>strong research base</u>, disproportionate to the region's size, as seen from the fact that its higher and further education sector protects more intellectual property than institutions elsewhere in the UK.

- <u>Infrastructure</u> has enjoyed strong investment in past decades, not least through support from previous Structural Funds programmes. This is particularly seen in near-100% broadband coverage.

- The region has <u>strong sectoral strengths</u>, not least in traditional and renewables energies and life sciences, sectors characterised by strong links between the enterprise base and the key sources of research and innovation.

Regional Weaknesses

- <u>Economic growth</u> and gross value added (as a measure of productivity) in the region continues to lag behind UK averages. Indeed, productivity relative UK averages has declined in recent years.

- <u>New firm formation</u> and entrepreneurship rates are low across the region relative to EU and UK averages.

- Despite the strong research base, the indigenous enterprise sector has not made full <u>use of the region's research capabilities</u> and RTD expenditure and innovation rates remain relatively low.

- Within the LUPS region, there are substantial <u>variations in economic growth and employment performance</u>, particularly among different communities, with some urban and rural areas lagging significantly.

- In some <u>urban communities</u>, combinations of poor economic conditions and high levels of worklessness have produced significant concentrations of social and economic deprivation.

- <u>Part-time and under-employment and low earnings levels</u> characterise rural areas and act as a drag on the economic development of the region as a whole.

- In rural areas, enterprises also experience distinctive problems, particularly in relation to <u>access to key markets, distance from important sources of skills and research and innovation</u>.

Regional Opportunities

- The number of <u>would-be entrepreneurs</u> in the economy provides a good base for improving new firm formation rates if provided appropriate support.

- <u>E-business</u> use among enterprises continues to show relatively good performance compared to the rest of the UK, but there are opportunities to improve take-up relative to EU and North American performance.

- Greater embedding of <u>resource and energy efficiency</u> practices in enterprises – particularly new firms – could improve cost competitiveness and contribute to wider climate change goals.

- The region's <u>strong university research sector</u> gives good opportunities for commercialisation and spin-outs which can be used to strengthen the overall innovation system underpinning the regional economy.

- There are a number of <u>technological sectors</u> where the region has considerable scope to develop, such as digital media, life sciences and renewable technologies.

Regional Threats

- The weaknesses in entrepreneurship and <u>new firm formation</u> could weaken the region's enterprise base, potentially exacerbating the gap between the strong research base in the higher and further education sector and the commercial applications of technological developments.

- Continuing decline in the <u>worst-off urban communities</u> may result in self-reinforcing 'vicious cycles' of economic and social deprivation that could prove increasingly resistant to policy intervention.

- The <u>out-migration of young people</u>, which could reduce the capacity of rural areas to reverse economic decline.

- <u>Long-term population decline</u>, skills shortages and problems in accessing key sources of industrial research and innovation in part derive from deficiencies in key services in rural areas, such as higher/further education and transport.

- Many rural areas continue to be <u>over-dependent on primary and traditional economic activities</u> which are often characterised by low earnings and productivity levels and vulnerable to longer-term shifts in competitive advantage.

Key programme challenges

The SWOT analysis – and the key messages highlighted in the foregoing sections – suggest that there are a number of key strategic challenges for the Programme.

1   **Increasing the regional benefits of a strong higher and further education sector**: while the region has a strong record in university research, the industrial research does not flow well into the region's enterprise community and consequently, has a limited impact on enterprise innovation – scope for encouraging more indigenous commercialisation is clear.

2   **Improving RTD and innovation across the region:** the research and innovation system in the region lacks a number of critical linkages that prevent it from operating as a strong source of regional competitiveness – measures to improve RTD and innovation collaboration, particularly where linked to other areas of enterprise development support, are required.

3   **Increasing the low numbers of people becoming entrepreneurs**: the issue for the region as a whole is not simply the number of new enterprises surviving, although that should remain an important target of policy – it is the low level of entrepreneurs in the first place, dissuaded by a range of barriers, particularly for those at 'pre-start' level.

4   **Addressing the development bottlenecks for new and growing businesses**: one of the market failures in the LUPS region is the absence of sufficient, accessible finance for enterprises seeking finance for start-up and growth, particularly related to the commercialisation of new technologies or key innovations – but while this is a key bottleneck, there are significant challenges for enterprises with respect to the continuing need to improve e-business performance and environmental and resource efficiency within business processes, especially for new firms.

5   **Improving the indigenous enterprise development of the most disadvantaged urban communities**: within the region, the most deprived urban communities require intense, targeted forms of support to break a cycle of economic disadvantage and encourage indigenous enterprise growth.

6   **Improving the ability of disadvantaged urban communities to access economic growth in the areas of opportunity**: the most deprived communities must not only have their internal sources of competitiveness improved, but be able to access nearby growth-pole areas, allowing individuals to gain employment opportunities.

7   **Increasing the diversification of the rural economy into new activities while supporting sustainable competitiveness of traditional industries**: the rural areas of the LUPS region share a common dependency on traditional industries that have experienced slumps in markets and are harmed by low levels of productivity.

8   **Improving key support services to underpin the sustainability of rural economic development**: the sustainability of rural economies is partly dependent on their ability to provide key services to individuals and enterprises, particularly with respect to research/innovation, training and access to markets.
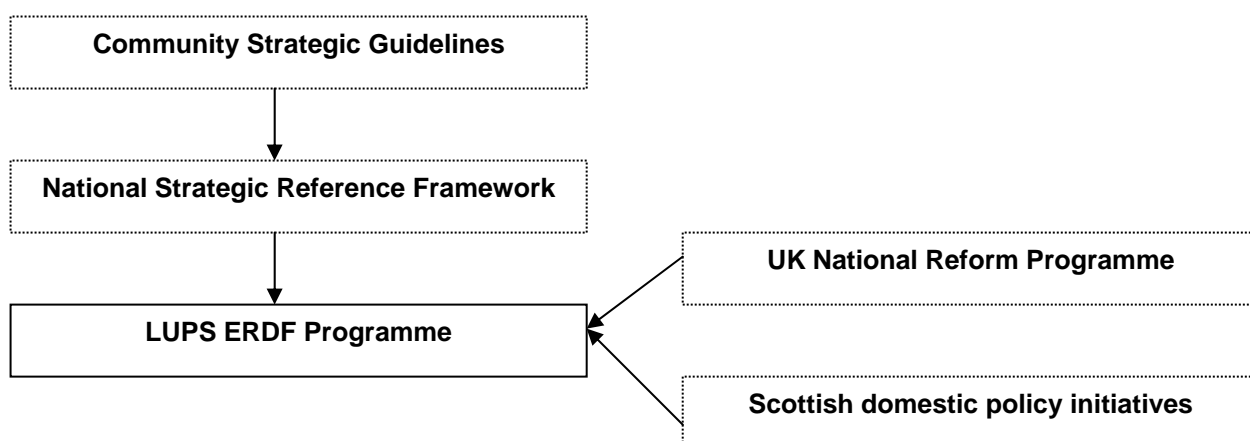
3   POLICY BACKGROUND

3.1   Policy Context

To be fully effective, the ERDF Programme must not only address the challenges set out in the analysis of the socio-economic background section, but link these to a range of policy actions in order to maximise the value added of the Structural Funds. These links must be established at different levels to ensure funding not only complements but builds on existing policy. Specifically, the ERDF Programme should fit within and alongside:

- the <u>Community Strategic Guidelines</u>, which set the indicative framework for the Cohesion Policy in support of the EU's growth and jobs commitments;

- the UK's <u>National Strategic Reference Framework</u>, as specified in Article 25 of the General Regulation, in which the chapter on Scottish Structural Funds goals provides the overall framework within which the ERDF Programme must fit;

- the UK's <u>National Reform Programme</u>, detailing how the UK as a whole is addressing the challenges and targets developed as part of the wider Lisbon Agenda, to which the Structural Funds are intended to contribute; and, lastly,

- the array of <u>domestic policy initiatives</u>.

Figure 1 illustrates how these different policy tiers should combine in the Programme.

<u>Figure 1: Hierarchy of strategic objectives</u>

The following section presents the key policy context for the challenges identified in the socio-economic background with these different tiers of policy guidelines and actions to ensure consistency of approach – at the levels of the EU, the UK and Scotland. It will form the basis of the priority structure set out

in Chapter 4. Reflecting the themes covered in the socio-economic analysis above, the policy areas to be considered are:

- enterprise, RTD and innovation challenges: mapping onto key challenges 1-4;

- urban challenges: mapping onto challenges 5-6; and

- rural challenges: mapping onto challenges 7-8.

In addition, there are three cross-cutting strategic themes which will inform all aspects of the Programme – equal opportunities, environmental sustainability and social inclusion. These are treated in Chapter 8.

Enterprise, RTD and innovation challenges

EU Level

Article 23 of the Structural Fund Regulations provides for the Council to establish Community Strategic Guidelines to provide an indicative framework for Structural and Cohesion Fund programmes. Based on the Commission's 2005 Communication, three main Guidelines for future spending have been identified:

- improving the attractiveness of Member States, regions and cities by improving accessibility, ensuring adequate quality and level of services, and preserving their environmental potential;

- encouraging innovation, entrepreneurship and the growth of the knowledge economy by research and innovation capacities, including new information and communication technologies; and

- creating more and better jobs by attracting more people into employment, entrepreneurial activity, improving the adaptability of workers and enterprises and increasing investment in human capital.

Within the Community Strategic Guidelines, there are several Guidelines where the challenges identified in the socio-economic analysis feature strongly.

- Facilitate innovation and promote entrepreneurship. The Guideline notes that there is a widespread need to encourage entrepreneurs to set up enterprises as well as to provide a support environment for their start-up and growth.
  - Programme challenge 1: Improving the capacity of the region's research centres to contribute to the wider research and innovation environment of the regional economy maps neatly onto the Guideline.
  - Programme challenge 3: The aim of improving the entrepreneurship rate is recognised explicitly in this challenge.
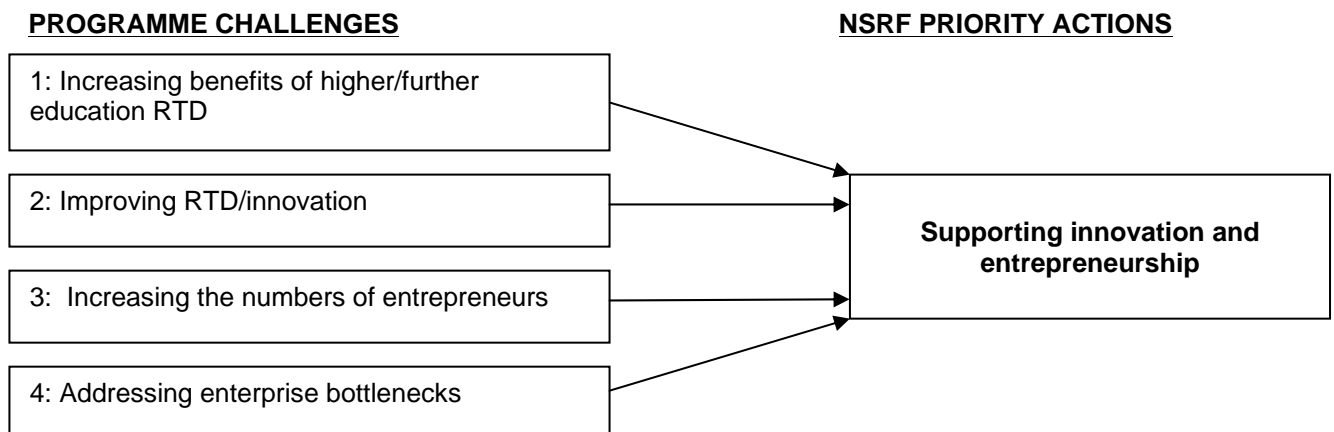
- - Programme challenge 4: Focusing support on key industries and clusters would enable the challenges of RTD and innovation set out in the Guideline to be addressed more effectively with limited resources.

- Improve access to finance. One aspect of the support environment for growing enterprises is the financial resources available to growing enterprises. The Guideline acknowledges that Cohesion Policy can contribute to regional economic growth by improving access to private equity and venture capital.
  - - Programme challenge 3: As the socio-economic background showed, access to finance is one of the key issues faced by entrepreneurs in the region.
  - - Programme challenge 4: Access to finance is explicitly recognised in this challenge as one of the developmental bottlenecks for the region.

- Increase and improve investment in RTD. The Guideline outlines the importance of strengthening co-operation amongst enterprises and research centres, supporting RTD undertaken by SMEs and developing the overall RTD capacity of the region.
  - - Programme challenge 1: As noted above, by addressing the critical weaknesses in the region's RTD and innovation system, the Guideline has been recognised as one of the priority areas for the Programme to address.
  - - Programme challenge 2: Improvements in regional RTD cannot be easily achieved across the economy as a whole with limited ERDF support – consequently, concentrating on particular industries and clusters where improvements can have significant spillover effects would be a more effective use of resources.

- Facilitate innovation and promote entrepreneurship. An environment that encourages the replenishing of the enterprise base with new firms and provides support for those enterprises with strong growth potential is a key source of regional competitiveness. Indeed, the Guideline notes that "*[The co-financing of investments in innovation] should be the main priority in the regions covered under the Regional competitiveness and employment objective*".
  - - Programme challenge 1.
  - - Programme challenge 2: Key challenges 1 and 2 have explicit links to this Guideline.
  - - Programme challenge 3: The commercialisation of the region's research capacity would be greatly facilitated by a strong support environment for entrepreneurs.
  - - Programme challenge 4: Finance is one of the major barriers to the emergence and survival of businesses taking advantage of the commercial outputs of the region's research centres.

The UK National Strategic Reference Framework (as required by the General Structural Fund Regulation, Article 25) provides a reference instrument for drawing up Programmes to ensure that Structural Funds spending is consistent both with the Community Strategic Guidelines and the Member State's National Reform Programme for delivering the Lisbon Agenda. In the UK NSRF, there is a dedicated chapter to Scotland.

Overall, the UK Framework sets out the Government's central economic objective to raise the rate of sustainable growth and achieve rising prosperity and a better quality of life, with economic and employment opportunities for all. In Scotland, the primary aim is to contribute to the sustainable economic growth of the region through improvements in productivity while addressing social inclusion and environmental sustainability needs. The European Social Fund will contribute to these strategies to increase employment and raise skill levels.

The Scottish chapter sets out the challenges and sets of priority actions for the ERDF Programme under the Competitiveness Objective. Low firm formation rates and deficiencies in the knowledge and innovation system are recognised in the NSRF as the key needs for Scotland as a whole. Figure 2 shows the links between the NSRF priority actions for the Competitiveness Programme and the challenges identified in the socio-economic background.

Figure 2: Programme challenges and the National Strategic Reference Framework: enterprise, RTD and innovation

PROGRAMME CHALLENGES   **NSRF PRIORITY ACTIONS**

1: Increasing benefits of higher/further education RTD

2: Improving RTD/innovation

3: Increasing the numbers of entrepreneurs

4: Addressing enterprise bottlenecks

Supporting innovation and entrepreneurship

UK and Scottish Levels

As part of the goal of promoting productivity growth, the UK's National Reform Programme emphasises the need to improve entrepreneurship and access to finance, particularly for businesses. With respect to RTD and innovation, the importance of addressing the challenge is reinforced in the UK's National Reform Programme. The UK Government's overall approach to encouraging national economic growth is based on improving productivity performance through an integrated series of policy measures. One of the key drivers of

productivity is the capacity to generate and make full economic use of science and innovation. In pursuit of this goal, the National Reform Programme highlights the need to encourage greater private and public investment in RTD – particularly in the enterprise sector – as well as investing in a research base that is responsive to the economy, not least in sustainable industries such as renewable energy. It has set the goal of increasing UK public and private investment in RTD to 2.5% of GDP by 2014. In addition, the NRP has an aspiration of achieving an 80% employment rate.

The UK approach is echoed in Scotland. The goal of improving RTD and innovation performance and improving new firm formation rates in Scotland is central to the Scottish Executive's key strategies supporting economic development. The <u>Framework for Economic Development in Scotland</u> (FEDS), refreshed in 2004, sets the overall strategy for developing the Scottish economy. Its vision is:

> *to raise the quality of life of the Scottish people through increasing the economic opportunities for all on a socially and environmentally sustainable basis.*

To achieve this, FEDS has four principal outcomes:

- <u>economic growth</u>: with growth accelerated and sustained through greater competitiveness in the global economy;

- <u>regional development</u>: with economic growth a pre-requisite for all regions to enjoy the same economic opportunities, and with regional development itself contributing to national economic prosperity;

- <u>closing the opportunity gap</u>: with economic growth a pre-requisite for all in society to enjoy enhanced economic opportunities, and with social development in turn contributing to national economic prosperity; and

- <u>sustainable development</u>: in economic, social and environmental terms.

Central to these four outcomes is a long-term strategy to improve the productivity of the public and enterprise sector in the Scottish economy. As in the wider UK strategy, one of the key factors in this is the generation and full economic use of knowledge – FEDS acknowledges that Scotland needs to adapt to knowledge-intensive global markets rather than the labour-intensive markets in which it has successfully competed in the past.

Scottish Executive policy for developing the enterprise sector has been set out in <u>Smart Successful Scotland</u>, which was also refreshed in 2004. The strategy not only lays out the goals of the Enterprise Networks in Scotland but acts as a framework for co-ordinating enterprise development policy more widely. It has a vision consisting of three outcomes:

- growing businesses: a fast learning, high earning Scotland;

- global connections; and

- learning and skills.

As part of the first outcome, the challenge of increased commercialisation of research and innovation is explicitly defined with a need to increased levels of research and development spending in Scottish companies, more effective links between universities and enterprises and increasing the number of ideas being registered for patents in Scotland.

Under the heading of Growing Businesses, the strategy points to a manifold challenge for Scottish entrepreneurship, recognising that: the Scottish enterprise birth rate is persistently below the UK average; and that the shares of new enterprises in Scotland owned by women as well as started by disadvantaged groups are low. The strategy also points to the gaps in the Scottish capital market for financing for Scottish companies with high growth potential.

Social enterprises are also important in this regard. The Scottish Social Enterprise Strategy sets out the social economy as a key area is creating employment and development opportunities for those furthest from employment through helping to make social firms more sustainable and competitive. Priorities for supporting the sector in the strategy complement the focus on the social economy within the ESF Programme.

Economic development has been placed in a wider sustainable development framework at EU, UK and Scottish levels. Consequently, it is important to recognise a significant environmental sustainability dimension, in terms of how environmental concerns are linked with enterprise development. The Scottish Green Jobs Strategy outlines how Scotland should seize the business opportunities and advantages arising from sustainable development with a view to creating a vibrant, low-carbon economy with Scotland a centre for green enterprise. This would be achieved through a combination of support for the economic opportunities arising from a commitment to environment sustainability – such as renewables technologies and economic efficiencies arising from waste-recycling – as well as more general information-raising and skills improvements in mainstreaming environmental issues into economic activity.

Another key strategy that will shape the policy context for the Programme is A Science Strategy for Scotland, published in 2001. Among its objectives, the strategy recognises the importance of maintaining a strong science base fully connected to UK and international activity and funding sources as well as increasing the effective exploitation of scientific research to strengthen Scottish businesses. Both have been identified as major challenges for the region. At the time that the Programme was being developed, a new version of the science strategy was under preparation.

Urban challenges

<u>EU Level</u>

Regeneration can be defined as the sustainable economic, physical, social and environmental transformation of areas with particular disadvantage. In a Lisbon perspective, it is essential that regeneration is pursued so that all areas can contribute to the jobs and economic growth agenda. The <u>Community Strategic Guidelines</u> recognise the distinctiveness of these challenges. The need to address urban regeneration acts as cross-cutting themes across all the Guidelines. It is explicitly noted that within the Structural Funds, "*actions supported [should] include measures to promote entrepreneurship, local employment and community development*". The Guidelines also point to the importance of contributing to plans for urban regeneration within the designated areas. This is recognised in the two key challenges associated with urban regeneration:

- <u>Programme challenge 5</u>: supporting enterprise development – including entrepreneurship and local employment growth – in the most disadvantaged urban communities; and

- <u>Programme challenge 6</u>: improving the ability of the most disadvantaged urban communities to link to areas of enterprise and job opportunity to support local employment growth.

This is further underlined by the <u>National Strategic Reference Framework</u> which points to community economic development as an important element of the Structural Funds strategy in Scotland, not least as part of the urban dimension to regional development as a whole, particularly through the priority action for 'promoting community regeneration'.

<u>UK and Scottish Levels</u>

In the <u>National Reform Programme</u>, the need to target areas of particular deprivation is acknowledged with a commitment to an integrated policy approach to addressing the problems of the most disadvantaged areas. The NRP makes special reference to Closing the Opportunity Gap, the Scottish Executive strategy aiming to prevent individuals and families from falling into and to provide routes out of poverty (discussed below). Taking forward the third of the outcomes in FEDS, the strategy sets a relevant targets to tackle poverty and disadvantage.

<u>Closing the Opportunity Gap</u> is the Scottish Executive strategy aiming to prevent individuals and families from falling into and to provide routes out of poverty. It sets two relevant targets to tackle poverty and disadvantage:

- to promote community regeneration of the most deprived neighbourhoods, through improvements in employability, education, health, access to local services and quality of the local environment; and

- to improve service delivery in rural areas so that agreed improvements to accessibility and quality are achieved for key services in remote and disadvantaged communities.

In 2004, this was translated into a set of six objectives with a particular focus on areas of particular deprivation:

1. to increase the chances of sustained employment for vulnerable and disadvantaged groups – in order to lift them permanently out of poverty;

2. to improve the confidence and skills of the most disadvantaged children and young people – in order to provide them with the greatest chance of avoiding poverty when they leave school;

3. to reduce the vulnerability of low income families to financial exclusion and multiple debts – in order to prevent them becoming over-indebted and/or to lift them out of poverty;

4. to regenerate the most disadvantaged neighbourhoods – in order that people living there can take advantage of job opportunities and improve their quality of life;

5. to increase the rate of improvement of the health status of people living in the most deprived communities – in order to improve their quality of life, including their employability prospects; and

6. to improve access to high quality services for the most disadvantaged groups and individuals in rural communities – in order to improve their quality of life and enhance their access to opportunity.

The ERDF Programme embodies – directly as well as indirectly – these Closing the Opportunity Gap objectives. The strongest links are through the fourth of these objectives and Programme challenges 5 and 6.

In 2006, Closing the Opportunity Gap was supplemented by the Scottish Executive's People and Place: Regeneration Policy Statement, which states that regeneration is central to achieving the main goal of sustainable economic development. The Regeneration Policy Statement integrates public, private, voluntary and community sector activities to sustainable regeneration. It defines the regeneration challenge for Scotland:

> *Regeneration is a crucial part of growing the economy and improving the fabric of Scotland… Our aim is to turn disadvantaged neighbourhoods into places where people are proud to live. To turn places that have been left behind into places connected with the opportunities around them. To create areas of choice and areas of connection, rather than inward-looking places excluded from the wider successful Scotland around them. To build mixed and vibrant communities that sustain themselves.*

The Regeneration Policy Statement recognises that this can only be achieved through an integrated policy approach that goes beyond investment in the physical infrastructure of these areas: *the economic, social, physical and environmental aspects of regeneration requires an integrated approach which*

'joins up' planning and delivery across these aspects, so that change is mutually reinforcing. At the same time, it must be an approach based on partnership, as no single organisation can deliver all of these outcomes.

Again, the analysis underlying the Regeneration Policy Statement fits neatly with challenges 5 and 6 outlined above.

One key instrument to take forward this and other strategies are the Community Planning Partnerships (CPPs). The CPPs, one for each Local Authority area, set out how the relevant partners at local level intend to combine their activities to achieve regeneration outcomes. The CPPs consist of partnerships of the major partners involved in local regeneration including the Local Authority, voluntary sector organisations, local Health Boards and other relevant bodies. Another important delivery mechanism in this context is the Urban Regeneration Companies, which have been charged with taking forward local regeneration initiatives in some of the deprived parts of the region.

There are also strong policy links to the National Planning Framework for Scotland, particularly with respect to urban regeneration requiring an integrated policy approach and the importance of making full sustainable use of environmental and cultural assets.

Rural challenges

EU Level

The Community Strategic Guidelines recognise the distinctiveness of rural development challenges: as the document notes, "*cohesion policy can also play a key role in support of the economic regeneration of rural areas*". It specifies the importance of Structural Funds support for services of general economic interest that can improve conditions in rural area, an integrated approach to supporting tourism and the development of development poles in rural areas, particularly around economic clusters based on local assets. This is reflected in two of the Programme challenges identified in the socio-economic background:

- Programme challenge 7: central to rural competitiveness in the LUPS region is the dual approach of strengthening traditional activities, supporting their adjustment to new global competitive conditions, and encouraging the development of new growth sectors and activities; and

- Programme challenge 8: improving some of the underlying sources of competitiveness to the rural economy – notably the provision of some critical services – would facilitate wider economic regeneration of the region's rural areas.

Similarly, the National Strategic Reference Framework specifically draws attention to the special needs of the region's rural areas and the importance of addressing them in the ERDF programme, fitting with the third priority area of action, 'Supporting rural development'.

UK and Scottish Levels

A focus on the rural development challenges set out above is also consistent with the UK National Reform Programme approach to addressing the specific productivity challenges of different regions. In addition, it is essential that ERDF funding in support of rural development is fully complementary with the Scottish Rural Development Programme. This is discussed in detail in Section 6.3.

From a Scottish strategic perspective, Rural Scotland: A New Approach sets out four key objectives for the development of rural areas: developing a strong and diverse rural economy; harnessing traditional strengths with an appetite for change in order to provide opportunity to young people; building a rural Scotland where everyone can enjoy a decent quality of life; developing a rural Scotland where people enjoy public services that are accessible, high-quality and with the greatest choice; and maintaining a rural Scotland where the natural and cultural heritage flourishes in all its diversity.

The Scottish Sustainable Development Strategy establishes five main priorities for sustainable development: sustainable consumption and production; climate change and energy; natural resource protection and environmental enhancement; sustainable communities; and learning to live differently (as discussed in more detail below). The Securing a Renewable Future paper sets out Scotland's approach to meeting its renewable energy commitments, particularly a target of 40% of its electricity needs from renewable sources by 2020. For rural areas, the National Transport Strategy sets out Scotland's plans through three strategic outcomes: improving journey times and connectivity; reducing emissions; and improving access and safety. Both strategies suggest a number of areas where complementary support from Structural Funds can have a more strategic impact.

3.2   Lessons from 2000-06 Programming

Structural Funds programming in Scotland has always built on the experience of 2000-06 programmes, maintaining the good practice while adapting to new circumstances. In developing the ERDF Programme for the LUPS region for 2007-13, the lessons of the 2000-06 use of European Regional Development Fund in Scotland were examined from a number of different perspectives. This section summarises the key studies drawing on those lessons:

- the mid-term evaluation updates of the Scottish Objective 2 programmes for 2000-06;

- the 2005 report of an internal Value Added Group on how to increase the value added of future Structural Funds programmes; and

- the 2006 Hall Aitken report on options for delivering Structural Funds programmes.

Mid-term evaluation updates

For the 2000-06 programming period, mid-term evaluation updates were conducted on the three Objective 2 programmes: the Western Scotland, the East of Scotland and the South of Scotland. While the reports are very specific in their analysis, several of their conclusions and recommendations have informed the development of the ERDF Programme for the LUPS region in the new period.

With respect to mid-term evaluation update for the <u>Western Scotland</u> programme, the evaluation had a wide-ranging number of recommendations, but those with strong relevance to the current programmes are noted here. First, the evaluation pointed to Programme successes in mainstreaming Structural Funds projects into standard national projects that have progressively relied less on Structural Funds interventions. It also recognised where Structural Funds could make significant future contributions, including working with the new Community Planning Partnerships to maximise the mutual benefit of domestic and EU funding streams. Similarly, the report pointed to the value of supporting projects that address national policy goals in a local context. Both of these conclusions are reflected in the approach to using Community Planning Partnerships under Priority 3 of the new Programmes, as set out in the Chapter 4 priority description and the Implementing Provisions chapter.

Second, the evaluation concluded that the urban targeting approach of the community regeneration aspects of the West of Scotland programme remained a useful tool for delivering the Funds and focusing them on the areas where their impact would be greatest. It notes that the identification of a number of priority areas for urban regeneration support could provide substantial value added for the limited resources available to the Programme. Again, under the Urban Regeneration priority of the new programme, the recognition that funding should be targeted on a limited number of areas to achieve maximum impact has been developed with the new Programme.

For the <u>East of Scotland</u>, the mid-term evaluation update drew attention to a number of areas. In risk capital the Programme was seen as having had notable successes in a range of complementary and very successful risk capital products, ranging from the large Scottish Co-Investment Fund (with its novel and innovative co-investment model) to the relatively small Genomia fund (supporting proof of concept and early proto-enterprises). The role of start-up and development loan/equity financing is set out in Priority 2 for the new Programme, having been informed by the experience of Structural Funds support for venture capital initiatives in the 2000-06 programme across the three Objective 2 programmes.

The East of Scotland update also noted the role of spatial targeting in reconciling the balance between need and opportunity. This was reinforced by the overlay of focusing support on key strategic growth sectors such as bio-technology and life sciences. This balance between spatial and sectoral

targeting has influenced the targeting of funding in the new Programme's priorities, not least with respect to the national focus of Priorities 1 and 2, the urban focus of Priority 3 and the rural focus of Priority 4.

Lastly, the East of Scotland update underlined the continued commitment to deliver the combined economic social and environmental benefits of a genuinely integrated approach to sustainable regional development and regeneration as being at the forefront of the Programme's approach to sustainable development. The new Programme embraces this approach and builds on the extensive range of practical guidance and support mechanisms for equal opportunities and environmental sustainability.

Lastly, the mid-term evaluation update of the <u>South of Scotland</u> Programme made several important points:

- the need to focus on competitiveness, with greater attention paid to rural competitiveness and supporting ambition (which underpins the approach taken in the new Programme to Priority 4);

- greater access to risk funding for priority sectors as well as increases in generic capital support (the former is set out in Priority 1, but given the reductions in funding, significant increases in generic capital support for enterprises through the Structural Funds has not been possible);

- more emphasis on exit strategies for community regeneration and the delivery of those strategies (which will be built into the annual review of Priority 2 projects supported through the partnership delivery channels); and

- flexibility to ensure the changing needs of the regional economies can be addressed (a feature reflected in the spatial targeting of the new Programme's priority structure).

These points were reinforced by the Hall Aitken (2006) study on the impact of Structural Funds done for the programme's labour market intelligence service.

Value Added Group: 'Adding Value, Keeping Value'

As part of the preparations by the Scottish Executive for developing Structural Funds programmes for the 2007-13 period, a short-life internal working group was set up in 2005 to draw lessons on the value added of the Structural Funds from the 2000-06 Scottish programmes. The specific objectives of the Group were the following:

- to identify the types of projects that have provided the highest added value in the 2000-06 programmes;

- to consider the characteristics of those projects which have made them particularly successful;

- to define added value in the context of Structural Funds programmes; and

- to assess how best to encourage development of such projects within the regulations governing future Structural Funds.

The Group was drawn from the European Structural Funds Division and the Programme Management Executives for the 2000-06 programmes. It concluded the following.

- In future, a greater premium should be placed on qualitative value added in project selection. This was not to suggest that value added should not have a strong quantitative dimension, but that qualitative value added should be a priority. In practice, this meant that Structural Funds could usefully support pilot, innovative projects.
  - *The importance of an innovative approach to projects is reinforced in the priority descriptions in Chapter 4.*

- Consideration should be given to providing a greater time limit on project funding in future. If the focus is on supporting qualitative projects, Structural Funds should have the role as a major lever for the early stages of a project's development. 'Repeat' projects or longer-term continuations should be discouraged unless there are strong operational reasons for doing so. As a result, project awards would be for a minimum of two years, though with annually-set targets and reviews.
  - *This conclusion will be reflected in the new guidance to be issued to applicants and in the priority descriptions in Chapter 4.*

- Partnership has been a critical factor in supporting value added, particularly when applied in particular ways. Partnership at a local/regional level in project development is important, often acting as 'brokers' for development activity (a role that has been supported through Structural Funds support). Where projects and activities have been developed through a networked, inter-agency approach, project quality appears to have been driven up.
  - *Chapter 7 sets out the role of partnership in delivering parts of the Programme, especially Community Planning Partnerships.*

- The continuing promotion of major shared policy goals should continue, particularly the horizontal themes. The Structural Funds have played a pivotal role in promoting equal opportunities and sustainable development as wider policy goals and should continue to do so.
  - *This is reflected on the continuing emphasis on the mainstreaming of these three horizontal themes, as set out in more detail in Chapter 8.*

Value added has also been apparent where funding has been coordinated through a series of activities targeting a common goal. Whether the coordination is of different types of funds (ERDF, ESF and other sources of EU funding) or different types of projects (through project clusters), their impact is strongest when geared towards a specific development goal. In Structural Funds, these goals have been most readily achieved when defined in terms of local geography (especially through community economic development) or niche sectors (particularly through targeted enterprise development activities). The focused approach is reflected in the targeted nature of the priorities described in Chapter 4.

Hall Aitken: 'Making Every Euro Count'

As part of the preparations for developing the 2007-13 programmes, the Scottish Executive commissioned a report of Hall Aitken Consultants in 2006 with several objectives:

- to identify a series of delivery options for single-stream funding of Structural Funds and other domestic policy resources, based on 2000-06 practice elsewhere in the EU;

- to draw out comparative lessons with a view to setting out options for Scottish delivery; and

- to set out options for Scotland.

On this basis, the report concluded that any approach should achieve as many of the following criteria as possible:

- minimise the administrative costs of operating projects;

- direct funds to where they will make the most difference in terms of economic need, opportunity and delivery capacity and quality;

- build on existing structures, partnerships and systems where possible and be developed with the support of stakeholders;

- shift the focus of effort from project selection to effective delivery and monitoring;

- integrate Structural Funds actions more closely with related domestic policy actions;

- retain sufficient flexibility to respond to changes in need and opportunity during the programme lifetime and ensure that projects address both issues;

- promote the horizontal themes; and

- spread learning and good practice.

The delivery mechanisms for the programmes – set out in detail in Chapter 7 – were developed with these conclusions in mind. They have also been designed to make use of the following range of elements, set out by Hall Aitken as mechanisms that could be used in delivering the programmes:

- single-stream funding: this principle lies behind the use of Intermediate Delivery Bodies, as set out in Chapter 7;

- area and local outcome agreements: the partnership-based approach to delivery for parts of the Programme set out in Chapter 7 reflects this mechanism;

- competition between single-stream funding bodies: again, as Chapter 7 details, competition is anticipated between partnerships for the delivery of parts of the Programme;

- <u>a more negotiated decision process</u>: the projects to be carried out by the Intermediate Delivery Bodies will be negotiated with the Managing Authority and the Programme Monitoring Committee; and

- <u>thematic partnerships</u>: in line with the second and third bullet points, the partnerships will be expected to show thematic complementarity in the supported activity.

4   STRATEGY AND PRIORITIES

4.1   Programme Vision

The strategy for the ERDF Competitiveness Programme proceeds from the identification of key challenges within the socio-economic analysis (in Chapter 2), the need for actions to fit with EU, UK and Scottish policy frameworks and the experience of previous programming (in Chapter 3). The socio-economic analysis described how the region has clear strengths and opportunities on which it can build – particularly with respect to its research and innovation, environmental and human capital resources – while recognising a range of significant weaknesses and challenges – deriving from low productivity, new firm formation rates, the commercial application of research and innovation and the specific challenges for economic development in urban areas of high deprivation and rural areas facing low economic growth. Eight challenges have been identified:

1   Increasing the regional benefits of a strong higher and further education sector.

2   Improving RTD and innovation across the region.

3   Increasing the low numbers of people becoming entrepreneurs.

4   Addressing the development bottlenecks for new and growing businesses.

5   Improving the indigenous enterprise development of the most disadvantaged urban communities.

6   Improving the ability of disadvantaged urban communities to access economic growth in the areas of opportunity.

7   Increasing the diversification of the rural economy into new activities while supporting sustainable competitiveness of traditional industries.

8   Improving key support services to underpin the sustainability of rural economic development.

Structural Funds in the Competitiveness Programme are limited. The EU resources in the ERDF Programme are €375.958 million for 2007-13, resulting in a total programme value of €970.89 million. In light of current developments in the EU, the funding may be the last substantial funding of this scale for the region, consequently, it is essential that the Programme aims to deliver lasting legacies to the region that will extend beyond the programming period, focusing on the key market failures in the competitiveness of the region and the sub-regional areas within it. The Programme can do this by making real contributions to tackle both the region-wide challenges of research and innovation and enterprise development as well as the localised challenges of urban and rural areas within the LUPS region.

In summary, the Programme will make its principal contributions and added value through:

- acting as a lever to encourage domestic resources to address the key development challenges outlined in the socio-economic analysis through its role as a match-funder;

- investing in the key research and innovation sources in the regional economy and encouraging their greater use by enterprises;

- promoting a more pro-active approach to research and innovation among all businesses;

- increasing the level of new firm formation;

- improving the conditions for indigenous economic growth in the most-deprived urban areas; and

- helping rural economies to diversify by developing their competitive advantages and enabling rural businesses to make full use of these advantages.

The overall vision of the ERDF Programme for the Lowlands & Uplands Scotland area is:

> **To encourage the growth of the region's economy within a sustainable development framework and thereby enable all parts of the region to contribute to achieving the Lisbon Agenda goals**

There are three important parts to this strategic goal.

- First, the overall goal of the Programme is to address regional economic growth with a view to enhancing the region's ability to contribute to Lisbon goals. Some of these goals have already been met in Scotland as a whole, particularly its employment rate, but there remain substantial areas in which EU funding can make important contributions to the region's underlying competitiveness.

- Second, the Programme acts within a sustainable development context – that is to say, taking full account of the need to balance conservation of the region's environmental assets with both economic growth and the importance of distributing the benefits of that growth to all individuals and parts of the region.

- Lastly, the Programme recognises that these are goals that are not only met at regional level, but for the constituent areas of the region. Economic performance varies substantially across the region, often for different reasons and consequently the Programme should recognise the need for different sets of actions in different areas.

Given the limited resources, the strategy for the Programme will be more effective if acting in tandem with the overarching objectives of Scottish economic policy. As set out in the previous chapter, FEDS provides clear direction for the role and priorities of the Scottish Executive: targeting those market failures in the economy where interventions will raise productivity and lead to a medium-to-long term economic growth whose benefits are enjoyed

by all and within the context of sustainable development. As Section 3.1 stressed, Structural Funds are intended to extend and build on the work of key Scottish policies within the context of the Lisbon Growth and Jobs Agenda. As a result, the Programme is unable to support all activities that can contribute to this goal, so must concentrate on those areas of market failure where additionality and added value can be clearly demonstrated. It also acts within a wider sustainable development context as set out in the Scottish Sustainable Development Strategy, in which the Programme aims both to minimise any damaging environmental consequences of supported activities as well as support measures that will increase environmental sustainability, again where such measures are directly linked to the Lisbon Agenda.

The ERDF Programme also works with the ESF Programme for the Competitiveness Objective in Scotland. Chapter 6 sets out how the two programmes can complement each other effectively.

The following Chapter contains: an outline of the Programme Objectives; and detailed priority descriptions, setting out the rationale, eligible activities, targeting and indicators for each priority. The Chapter also includes a description of the use of technical assistance as a separate priority and the categorisation of assistance for the purpose of Lisbon 'earmarking'.

4.2   Programme Objectives

The strategic vision of the ERDF Programme operates through four sets of Objectives, addressing market failures in the following areas:

1.   **Research and Innovation**

2.   **Enterprise Growth**

3.   **Urban Regeneration**

4.   **Rural Development**

These Objectives have different spatial dimensions. The research and innovation and enterprise growth Objectives have a region-wide focus and concentrate on the key areas of economic competitiveness that are systemic to the whole economy. The latter two Objectives address the spatially-distinctive and localised needs of different parts of the region: 'urban regeneration' recognises the distinctive problems arising from severe urban deprivation, while the 'rural development' objective acknowledges the special needs of the region's most peripheral areas.

<u>Objective 1</u>: Improving enterprise research and innovation

At the heart of the Lisbon strategy for improving the EU's growth and jobs performance is a need to increase growth and improve productivity by strengthening the sources of enterprise growth. Central among those sources is RTD and innovation, that is, the capacity for individual enterprises to renew the competitiveness of their products and services through continual technological, skills and business process renewal. The Community Strategic Guidelines give strong emphasis to the role of supporting RTD and innovation,

particularly through the Competitiveness Objective. Chapter 3 demonstrates that this is also a high priority within UK and Scottish economic development.

RTD and innovation can be defined broadly. In economic development terms, policy has tended to focus both on what individual enterprises can do – in terms of their ability to generate, access and develop new ideas and skills – as well as on how regions as a whole can act as a self-sustaining innovation systems that will constantly refresh the economy's sources of competitiveness through, for example, increased knowledge transfer between the science base and industry.

The socio-economic analysis identified a range of issues relating to the RTD/innovation capacity of the region. The region lags behind both UK and EU averages for RTD spend by enterprises. Overall, the Objective recognises that while there are a number of elements underpinning the region's economic competitiveness, sustainable growth will only be possible if the region has a strong innovation system linked to a enterprise base with the skills, resources and capacity to make full use of RTD and innovation. Chapter 2 also draws attention to the strengths that the region has in some technological and industrial research areas – such as the life sciences and renewables – and the opportunities available to the region that targeted investment could make in reinforcing those strengths and linking them with the wider economy.

As a result, the Objective has been set as follows:

> **to improve the competitiveness of the Lowlands & Uplands Scotland enterprise base through increased innovation and a fuller use of its RTD base**

Structural Funds Value Added

As shown in Chapter 3, the importance of RTD and innovation in Scottish policy is strong and the resources supporting it – particularly through Scottish Enterprise and the higher/further education sector – substantially dwarf the Programme's funding. But the Programme has key areas where added value can be important in this area, acting as a catalyst for supporting significant projects underpinning RTD in the region's key sectors and by giving a strong focus to RTD and innovation issues, shaping policy priorities more widely.

Structural Funds policy will contribute to developing competitiveness by deepening the self-renewing value of the main sources of RTD and innovation in the economy, intensifying and broadening the links between this research capacity and the enterprise base and improving the ability of the enterprise community in Scotland to make maximum use of this research. The funding can have particular added value by investing in the emerging sectoral research strengths of the Scottish economy, improving the commercialisation of research in higher and further education and the enterprise base and enhancing the capacity and willingness of regional enterprises to make use of and develop innovation.

The Programme would also aim to encourage value added by encouraging more pilot, innovative approaches to tackling these enterprise development issues. In the 2000-06 period, the EU-funded Innovative Actions Initiative provided funding for cross-Scotland projects that funded pilot projects examining more systemic innovation issues. The Programme will include within its scope explicit support for projects that will address these issues on a cross-Scotland basis through co-ordinated bids with the ERDF Programme for the Convergence Objective in the Highlands & Islands area. The Intermediate Delivery Body described in the Implementing Provisions chapter will also be encouraged to take forward such ideas.

Objective 2: Supporting enterprise growth and entrepreneurship

The region's enterprise base is hampered by limited replenishment through new enterprises and the capacity of existing enterprises to develop into high-growth businesses. Both issues have similar bottlenecks lying at their heart, particularly with respect to the provision of business finance. The region lacks a sufficiently strong, self-sustaining market for business finance, both for start-ups and for enterprises wanting to expand their operations. This is particularly important within the emerging key sectors at the regional level, such as the life sciences and renewables, as well as sectors that have a strong importance to parts of the region.

The Lisbon Strategy calls for "more emphasis on actions that stimulate greater productivity, employment growth and a more dynamic economy". The High Level Group that reported in November 2004 identified the need to increase the availability of risk capital on the grounds that the limited availability of capital is an obstacle to the establishment and development of businesses. Availability of risk capital to innovative SMEs is therefore central to achievement of the Lisbon aim of innovative growth-oriented businesses creating a more dynamic knowledge-based economy.

In the past, ERDF has been fundamental to expanding the venture capital market in Scotland. It has increased the amount of capital available for investment in SMEs, and has helped companies and investors appreciate this means of driving the expansion of innovative companies. Both in the 1994-99 Programmes and the 2000-06 Programmes, ERDF has supported investment funds that have enabled the expansion of innovative small businesses which by their nature carry significant risks. High-risk equity provision in Scotland has undoubtedly developed faster and more effectively as a result of ERDF involvement in these funds. ERDF has been an effective lever for greater involvement by the private sector. It has built awareness of the need for investor-readiness schemes and encouraged the development of Business Angel syndicates and their interest in investing in innovative SMEs. European funding has steered this process positively, encouraging investment eight or ten years ago in the then less favoured area of biotechnology and life sciences, and now in the emerging field of nanotechnology. As the socio-economic analysis underlined, there remains a need in the regional economy for these continuing interventions.

Enterprise growth is not simply a matter of making more resources available to enterprises. Finance needs to be complemented by targeted business support and advice, especially for entrepreneurs and new enterprises. This should not only include business advice, but other issues set out in the socio-economic analysis. In keeping with the sustainable development principles underlying the Programme, there should be support for specific activities designed to improve resource efficiency in enterprises and the commercial use of key environmental technologies. It also should include support for enterprises to make greater use of e-technologies and develop their e-commerce capabilities.

As a result, the Objective has been set as follows:

> **to improve enterprise formation and growth rates by enhancing the enterprise support environment, particularly with regards to access to finance, entrepreneurship, e-commerce and resource efficiency**

Structural Funds Value Added

As with Priority 1, Scottish and Lisbon policy goals are strongly complementary – consequently, there is widespread support for enterprise growth and competitiveness in the region. Much of this takes the form of generic business development support. The Structural Funds should not support such basic provision for the region. The added value of the Funds lies in encouraging support for entrepreneurs and new enterprises at an early stage, as the existing business advice network has good coverage of other enterprises, as well as encouraging entrepreneurs into the advice network in the first place. Moreover, in tackling specific issues such as resource/energy efficiency and e-business, the Funds would be highlighting issues where the region continues to have lagging performance.

Above all, the Funds would have a major catalytic impact in the areas of access to finance. This would build on the experience of the Scottish Co-Investment Fund and other ERDF-supported schemes in past programmes and take full account of the market failures identified in the socio-economic analysis. The Funds would help to support an integrated, comprehensive approach to addressing finance gap issues for the region's enterprises, potentially in the context of a major project, as set out in one of the annexes to this Operational Programme.

Objective 3: Promoting urban regeneration

Urban regeneration is an important contributor to achieving Lisbon goals. Regional competitiveness cannot be achieved simply by single-minded investment in the high-growth areas of a region, but in ensuring that all parts of the region can contribute to economic growth and minimising regional disparities. As seen in the socio-economic analysis, for some urban communities within the region, there are severe constraints on the capacity of these communities to take full advantage of their economic assets, leading to a debilitating systemic cycle of community decline and economic deprivation.

As the economic problems faced by these areas are made up of different problems, there is a need for coordinated, targeted policies, driven locally within a national framework of commitment to addressing regeneration – a point reinforced in the strategies described in Chapter 3.

These problems are concentrated in particular urban areas, where the combination of economic and social deprivation can undermine the wider ability of the region to contribute to Lisbon Agenda goals. Consequently, this Objective will focus on supporting sustainable urban development with a view to improving the contribution of disadvantaged urban areas to wider regional growth. Despite sustained employment growth and historically high employment rates, a small number of Local Authority areas still have significant concentrations of deprivation. There needs to be a significant investment in creating sustainable urban regeneration in the poorest communities within these localities. Investment needs to cover a range of areas that are not the proper area of Structural Funds activity.

As a result, the Objective has been set as follows:

> **to increase the contributions of the most disadvantaged urban communities to Lisbon goals by supporting their regeneration.**

Structural Funds Value Added

Chapter 3 noted a range of domestic strategies recognising the problems of social inclusion in parts of the region and the detrimental impact that this can have on local economic development. Resources for tackling these issues are provided across the region, but the Programme can have a particularly added-value effect by targeting its limited resources on particular areas. Specifically, the ERDF can be most effective in adding value to other initiatives through the following:

- addressing aspects of the physical environment that can make disadvantaged communities unattractive to external enterprises;

- enabling individuals to develop their own enterprises (including social enterprises) and economic activities with more customised and localised support than more general region-wide entrepreneurship initiatives;

- encouraging innovative interventions linking areas of economic opportunity with the regeneration needs of these communities; and

- working closely in tandem with related initiatives under the European Social Fund (an issue described in more detail in Section 6.1).

Moreover, the role foreseen for the Community Planning Partnerships described in Chapter 6 shows the value of the Funds in encouraging partnership working at local level and an integrated action-plan approach to tackling social exclusion issues.

<u>Objective 4</u>: Enhancing rural development

The diversity of local economic circumstances in Lowlands & Uplands Scotland suggests that different parts of the region will be helping Scotland contribute to Lisbon goals in different ways. While there are issues that affect the region as a whole – such as the RTD and innovation challenges set out under Priority 1 – rural areas have distinctive economic issues that need specific action. The Community Strategic Guidelines recognise that there is a wide variation in the economic situation of the rural areas, and distinguishes between those with good links to urban centres and those more remote rural areas which have to contend with a highly dispersed and ageing population, poor technical and social infrastructures, inadequate services. The Guidelines emphasise one of the determining features of cohesion policy as its capacity to adapt to the particular needs and characteristics of specific geographical challenges and opportunities, and member states and regions are advised to "*pay particular attention to those specific needs in order to prevent uneven regional development from hampering growth potential.*"

There has been some concern within rural areas of Europe that a strong RTD or high technology focus on future Competitiveness programmes would place rural areas on the periphery of the growth and jobs agenda. However, it is clear that the EU considers a strong territorial dimension to both Convergence and Competitiveness interventions as important key aspects and not simply considered as an optional extra. For Europe to achieve maximum competitiveness, each region of Europe must maximize its contribution. This priority is designed to achieve this within the context of rural areas in the LUPS region.

As a result, the Objective has been set as follows:

> **to maximise the contribution of rural areas to achieving Lisbon goals with a view to developing sustainable economic growth.**

<u>Structural Funds Value Added</u>

Domestic policy in recent years has been often concentrated on the needs of areas within the region's Central Belt and more urban areas. While this has not been to the exclusion of rural areas, the Funds can enhance the profile of rural development issues and demonstrate the value of integrating different policy initiatives through the joint working with the Scottish Rural Development Programme outlined in Chapter 6. It can also bring significant value in supporting local economic strategies, such as the South of Scotland Competitiveness Strategy, enhancing a local partnership approach to economic development.
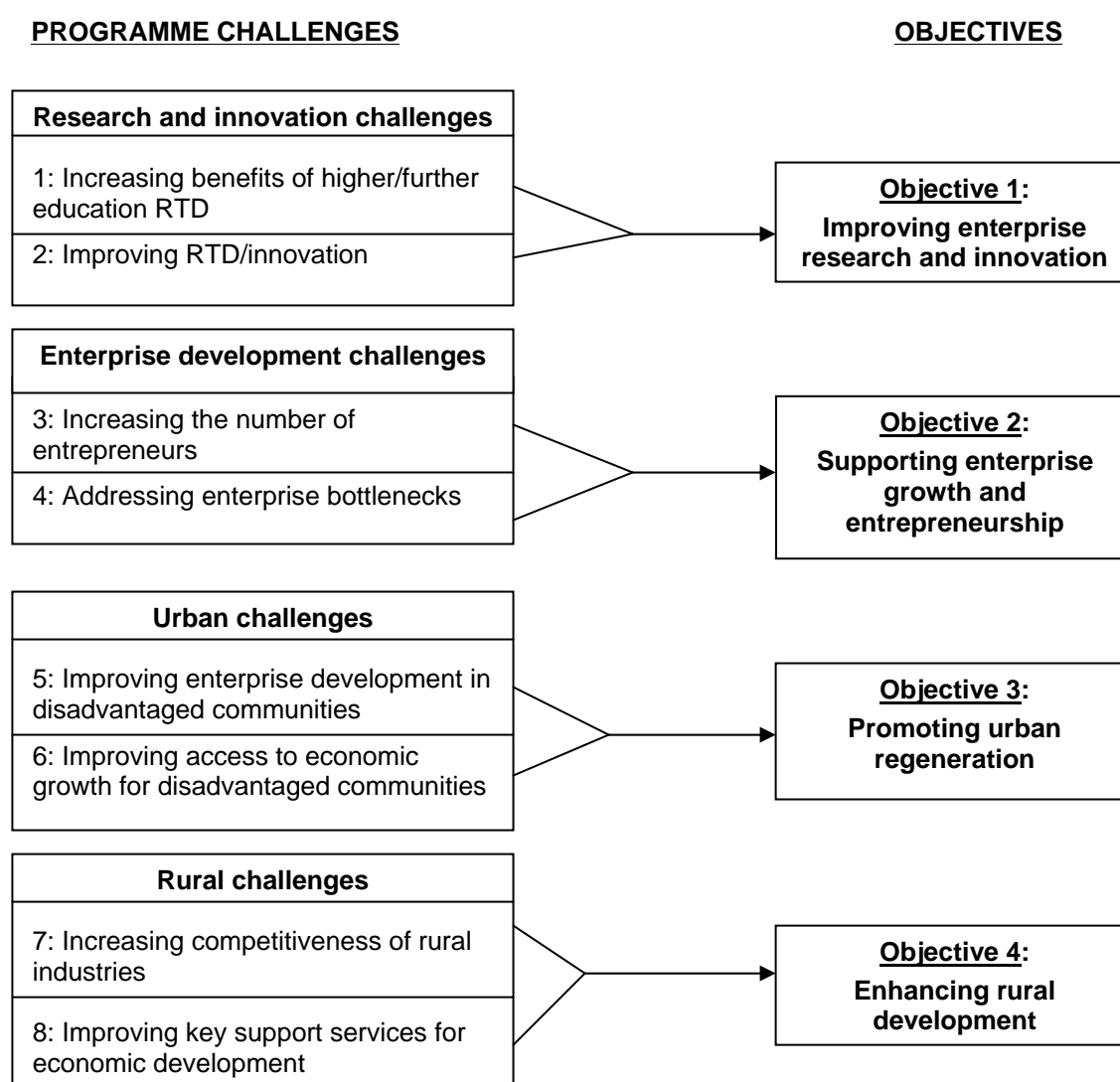
In recognising the distinctiveness of the problems facing the most rural areas scattered across the region, there is a strategic need to address the underlying problems of these local economies. Consequently, Structural Funds can bring clear added value to activities such as:

- the challenges facing their traditional industries;

- the need to encourage wider economic diversification into new sources of sustainable economic activity; and

- the longer-term issues of reversing population decline by improving the research and skills and other types of infrastructure in these areas.

The Objectives have been derived from the key Programme challenges set out in the socio-economic analysis, as Figure 3 displays. Each of these Objectives is addressed in the Programme by a single priority, as described in the following sections.

Relationship between Programme challenges and Objectives

Figure 3: Relationship of Programme challenges and Programme Objectives

PROGRAMME CHALLENGES   **OBJECTIVES**

Research and innovation challenges
1: Increasing benefits of higher/further education RTD
2: Improving RTD/innovation

Objective 1:
Improving enterprise research and innovation

Enterprise development challenges
3: Increasing the number of entrepreneurs
4: Addressing enterprise bottlenecks

Objective 2:
Supporting enterprise growth and entrepreneurship

Urban challenges
5: Improving enterprise development in disadvantaged communities
6: Improving access to economic growth for disadvantaged communities

Objective 3:
Promoting urban regeneration

Rural challenges
7: Increasing competitiveness of rural industries
8: Improving key support services for economic development

Objective 4:
Enhancing rural development

60

As noted, these Objectives operate at different spatial levels: the first two address issues of the regional economy as a whole, while the latter two recognise that parts of the region have distinctive problems that could affect the economic health of the overall region. Moreover, the Objectives do not work in isolation – each not only makes its contribution to the overall vision for the Programme but does so by complementing and reinforcing the other Objectives.

- <u>Objective 1</u> addresses the overarching source, circulation and exploitation of the competitive ideas and technologies that will underpin any long-term improvement to the competitiveness of the regional economy.

- <u>Objective 2</u> should enable the enterprise base to take full advantage of the ideas and technologies encouraged under Objective 1 (as shown by **1** in Figure 4 below). Support for business finance would make key resources available for developing new products, services and processes. Support for entrepreneurship would help to strengthen the enterprise base that will take advantage of these ideas and technologies. Support for energy and resource efficiency would ensure that enterprise development takes full account of the region's sustainable development goals.

- Objectives 3 and 4 ensure that the support in the first two Objectives are not concentrated in the growth areas of the regional economy, but that the benefits are distributed more widely (as shown by **2** in Figure 4 below). The two Objectives would reduce regional disparities by addressing particular development bottlenecks. <u>Objective 3</u> enhances the ability of urban areas where deprivation is specially concentrated to provide good growth conditions for the enterprises brought forward under Objectives 1 and 2, both in terms of enterprises indigenous to these areas and the encouragement of investment by enterprises from outside these areas.

<u>Figure 4: Relationship between the Programme vision and its Objectives</u>

Programme vision: To encourage the growth of the region's economy within a sustainable development framework and thereby enable all parts of the region to contribute to achieving the Lisbon Agenda goals

Region-wide Objectives   *Sub-regional Objectives*

Objective 1: *Research and innovation*   **Objective 2**: *Enterprise growth*   **Objective 3**: *Urban regeneration*   **Objective 4**: *Rural development*

1

2   **2**

- **Objective 4** targets the enterprise growth conditions of rural areas facing acute development challenges. In this Objective, support would be available to enterprises and groups of enterprises wanting to improve the competitiveness of their sector or diversify, but not activities are RTD/innovation-related, which would be supported under Priority 1. The focus would be on improvements in marketing strategies and potential (including exports) and the introduction of improvements to supply and production processes.

The following sections set out the descriptions for each of the individual priorities. Eligible activity is set out under each as well as geographical targeting for Priorities 3 and 4. In addition, a common eligibility criteria will be applied across the Programme with respect to project size. A <u>minimum project threshold</u> of an annual average of £200,000 in total eligible project costs will be put in place. The threshold has been introduced to:

- support the development of most strategic, legacy projects for the Programme with more significant impacts;

- encourage smaller, complementary projects to come together into more strategic partnerships;

- minimise the financial and audit risk of funding small projects; and

- promote linkages between small, pilot actions and activities to mainstream and disseminate their results.

The threshold has been set to take account of the nature of the eligible activities in the Programme and the financial and audit experience of the 2000-06 Programmes.

4.3 Priority 1: Research and Innovation

Rationale and aim

The priority given to RTD and innovation is clear in the Structural Funds, as the Community Strategic Guidelines identify research capacity and innovation as key drivers of regional competitiveness. Cohesion policy can make a number of important contributions to developing competitiveness by improving the main sources of RTD and innovation in the regional economy, the links between this research capacity and the enterprise base, and the ability of the enterprise community in Scotland to make maximum use of this capacity. These different elements should be self-reinforcing within a wider enterprise support framework.

First, <u>a strong research base</u> is a key source of sustainable economic growth. The socio-economic analysis identified a number of issues in the Lowlands & Uplands Scotland region that restrict the ability of the research base to support enterprise growth. The first is its overall size – relative to EU averages, Scottish private sector RTD investment rates have remained low, suggesting that the enterprise base needs to expand its contribution if long-term economic growth is to be improved. The second is the composition of the

existing base with a heavy dependence on research conducted by higher education establishments, research centres and foreign-owned large companies with limited linkages to the wider, indigenous economy. Although there are a number of sectors where the region's research excellence offers good opportunities for developing wider competitiveness – including life sciences, digital and electronics technologies, and renewables – there is scope for increasing the contributions research can make to the overall economy. However, as Chapter 3 noted, the support through Structural Funds needs to complement the funding for research in the 7th Framework Programme – consequently this priority needs to target the commercial application of research rather than 'blue-sky' activity.

Second, it is not simply a question of the size and activity of the research base, but <u>the links between that research base to an enterprise community</u> that will translate research into improving products, services and processes in enterprises. These links can take two forms: either direct contributions by the research base to enterprises through spin-out companies (particularly from the higher, further and research sector) or indirectly through cooperative research and development partnerships. In both cases, the socio-economic analysis noted that the region needs to improve.

Third, it is important that <u>the industrial community has the capacity to take full advantage of its links with the research base</u> by having the resources, knowledge and systems for developing sustainable innovation. The socio-economic analysis drew attention to the continuing constraints on innovation in individual Scottish enterprises, notably the cost and availability of investment finance and key technical skills and personnel. This is particularly true of small and medium-sized companies, which can face significant barriers in accessing these resources.

Lastly, the <u>willingness and demand among enterprises for research and innovation</u> should be strengthened. In this context, research and innovation does not simply mean technological RTD, but the development of new products, services and processes with a view to improving the competitiveness of enterprises.

These issues are long-term challenges facing the Lowlands & Uplands Scotland economy whose resolution will extend beyond the Structural Funds programming period. The challenges are central to Scotland's principal strategies in support of economic and enterprise development, the Framework for Economic Development in Scotland and Smart Successful Scotland. It is important that Structural Funds complements the work of these strategies and the longer-term work to improve the sources of Scottish economic competitiveness by making additional sustainable, targeted contributions in these four areas. However, Structural Funds can also act as a catalyst to domestic policy, encouraging a greater focus on the sources of competitiveness that lie at the heart of the region's ability to contribute to achieving the Lisbon Agenda.

Consequently, this priority will address the range of challenges that prevent

the region from taking full economic advantage of its potential research and innovation resources. These will be set against a wider background of an enterprise sector with a number of key development constraints, which differ between rural areas and those closer to centres of higher and further education. The priority implements Objective 1 of the Programme:

> **to improve the competitiveness of the Lowlands & Uplands Scotland enterprise base through increased innovation and a fuller use of its RTD base**

Eligible activities

In the socio-economic analysis, it was recognised that there are already active steps to improve links between industry and the main sources of research in the region, commercialisation of university research, high-tech new starts and non-local collaborative research. As noted, the Programme can make value-added contributions to the following:

- support for individual enterprises, such as funding for commercialisation of RTD; and

- support for collaboration, such as links between enterprises and higher and further education (not just with respect to technological development but in contributing to wider product, service and process innovation) and collaborative projects that can have a wider impact on Scottish sectors and industries.

Over the programming period, €92.11 million of EU funding has been allocated to the priority, or 25% of the Programme. It is important that the limited EU resources are targeted on a selected set of activities in order to maximise impact.

Structural Funds were used substantially during previous programmes to enhance support provided by partner organisations. Actions now envisaged seek to build on the progress of recent years, address change and changing circumstances and direct the limited resources available at businesses in key sectors and increased value added – ie. those which have the greatest propensity to contribute to external and internal cohesion through GDP growth and have a strong RTD basis in the economy. As set out in the socio-economic analysis, these sectors currently include the following: aerospace; chemicals; digital media; electronics; energy; life sciences; and micro- and opto-electronics. Renewable energy will be given particular emphasis in the priority. Over the lifetime of the programme, new sectors may emerge, so the Programme will retain the flexibility of shifting resources to develop business growth and RTD/innovation capacity in these emerging sectors should they become apparent.

The Programme should concentrate funding on high-growth enterprise activities in this area and the key bottlenecks identified in the socio-economic analysis. Eligible activities would include the following.

Support for individual enterprises

- Technology transfer programmes for individual enterprises

- Support to enterprises and individuals for converting research ideas into potential products, services and process improvements

- Scoping studies and prototype development for individual enterprises

- Projects aiming to increase demand in individual enterprises for research and innovation and adapt business processes that encourage more internal innovation practices

- Investments in individual enterprise capacity to develop full product development and market research

Support for research collaboration

- Creation of collaborative research projects that address RTD bottleneck gaps in particular technologies and sectors

- Pilot projects that test out new approaches to encouraging innovation with mainstreaming activity

- Projects that encourage enterprises with limited experience in working with research partners to develop collaboration

- Promotion of new sustainable RTD and supply networks, particularly for local SMEs, that transfer key research and innovation knowledge

The priority does not have spatial targeting, but aims to improve the competitiveness of the region as a whole. While there is likely to be support on activities surrounding higher and further education institutions and research centres, it is important that enterprises in all parts of the region are in a position to benefit from the support.

Much of the activity under this priority will be delivered by Scottish Enterprise as an Intermediate Delivery Body, as described in more detail in the Implementing Provisions chapter below.

There is the flexibility facility, which can allow up to 10% of the funding in this priority to be used for related ESF-type activity. We envisage using this to support limited training activities associated with the development of new research and learning facilities, research and technology development in key sectors (such as the training of key research staff). The flexibility could be applied in cases where the supported activity would not warrant a full-scale application to the ESF Programme as the support to be provided would be limited.

Indicators and targets

As shown in the table below, the selected indicators reflect the priority's focus on two sub-groups of activities. For activities to support <u>individual enterprises</u>:

- for output indicator, the number of individual enterprises supported; and

- for result indicators, the number of new products and services resulting from support.

For activities to support the <u>research networks and collaboration</u>, the following output and result indicators have been set:

- for output indicators, the number of supported networks/collaboration; and

- for result indicators, the number of new products and services resulting from support and increase in turnover of supported enterprises.

For the <u>priority as a whole</u>, there are several indicators to be assessed:

- the number of renewable energy projects supported (as an indicator of the Programme's cross-cutting environmental sustainability theme);

- number of gross jobs created;

- number of gross jobs safeguarded;

- the number of net new jobs created; and

- and the change in the level of expenditure by supported businesses on research and innovation.

Targets have been set with reference to previous programme experience. The data for the majority of these indicators will be collected from individual participant data on a quarterly basis, as described in more detail in Chapter 9. However, there are a number of indicators which will be measured through a specially-commissioned data-gathering exercise. These include changes in research/innovation expenditure by enterprises and the number of net new jobs created, which will be assessed through a specifically-commissioned evaluation to be conducted in the latter half of the programming period – this would allow for a suitable period of time for the results of actions to become manifest.

Guidance on definitions of indicators will be provided by the Managing Authority to all potential applicants in advance of programming rounds. In particular, these will define the type of projects set out in the output indicators.

Baselines for the priority are set in Chapter 9, which also discusses in more detail how the data will be used for evaluation and reporting purposes.

Indicator	Type	Target
Support for individual enterprises		
Number of enterprises supported	Output	2,500
Number of new products and services developed by supported enterprises	Result	1,600
Increase in turnover by supported enterprises (£mn)	Result	150
Support for research collaboration		
Number of research networks and collaborations supported	Output	600
Number of new products and services developed by supported networks	Result	1,600
Priority as a whole		
Number of renewable energy projects supported	Output	150
Number of gross jobs created	Result	6,100
Number of gross jobs safeguarded	Result	3,100
Number of net new jobs created	Impact	
Increase in research/innovation expenditure by supported enterprises	Impact	

4.4   Priority 2: Enterprise Growth

Rationale and aim

A thriving research and innovation system in a region can only add to regional competitiveness if it is linked to an active and replenishing supply of new enterprises – and consequently, entrepreneurs willing to set up new enterprises – that are able to sustain the enterprise community's capacity to develop innovative new products and services. As seen in the socio-economic analysis, Lowlands & Uplands Scotland has experienced persistently low new firm formation rates. The roots of the problem are varied, including the lack of sufficient access to resources for enterprise formation and growth and the overall supply of entrepreneurs in the economy. A co-ordinated set of initiatives is required to tackle the problem, involving improvements in the provision of risk capital in Scotland, a strong support environment for new and developing enterprises and measures to assist the cultural shift in the region towards greater entrepreneurialism.

To achieve this, the priority will address the Programme's second Objective:

> **to improve enterprise formation and growth rates by enhancing the enterprise support environment, particularly with regards to access to finance, entrepreneurship, e-commerce and resource efficiency**

There are three areas where the Programme can make a significant difference: access to finance; support for entrepreneurs; and business processes.

Access to Finance

Development finance has been a key market failure for new and existing enterprises seeking to grow. In past programmes, ERDF-supported funds helped the development of new and ground-breaking businesses in Scotland. The 2000-06 programmes have shown the way to the emergence of sustainable funds, whose returns – both capital and revenue – can be retained within the fund for reinvestment in new companies. Some ERDF-supported venture capital funds have also added value by enhancing the provision of finance with the provision of advice and mentoring services, and sometimes the offer of a non-executive director to help steer the company through a period of rapid growth. The provision of risk capital has shown itself to be a sustainable financial instrument for supporting the creation and growth of the SME base in Scotland and thereby for building and maintaining the regional economy.   With the associated business mentoring and non-executive director role of the investor, increased growth and higher business survival rates are delivered in a more sustainable way than with direct grant aid. Innovation, RTD and modernisation are key needs of the Scottish economy. Availability of risk capital as part of an effective investment market available for all stages of a company's growth is a way of meeting these needs and forms a key component of a sustainable Scottish economy.

Support should be available to target clearly-identified market failures and a clear economic rationale in each case. It would target development funding for enterprises seeking to expand, particularly for small firms growing into sustainable medium-sized enterprises. There is scope for providing a range of different enterprise finance instruments, addressing gaps at different stages in enterprise formation and development across the region.

Support for Start-Ups

For entrepreneurs and new firms, Programme resources could be most effective by supporting more pre-start events to stimulate action, provide the necessary skills, role models and informal networks; and by mobilising 'successful' entrepreneurs to provide more informal enterprise advice to complement the existing public sector system. The Programme can also usefully support promotional events in different parts of the region, targeted campaigns to address fears and lack of knowledge and initiatives to improve the networks between potential entrepreneurs and key sources of support, advice and finance. Special attention should be given to groups which may face particular barriers to developing new enterprises, particularly women entrepreneurs, those from ethnic groups, individuals with disabilities and those experiencing multiple difficulties that have kept them out of the labour market.

<u>Enterprise Business Processes</u>

Two other areas where the Programme can make significant contributions with limited funding are in addressing specific issues about the use of existing technologies to improve business processes.

First, <u>e-business</u> can continue to be improved throughout the region, taking advantage of the infrastructure investments in recent years in broadband. Such support can take the form of familiarising enterprises with the potential of the technologies, investing in their capacity to incorporate e-commerce into their businesses and addressing particular bottlenecks in their e-commerce potential.

Second, in keeping with the region's sustainable development aspirations and in line with the recommendations of the Strategic Environmental Assessment included in the Annex, the Programme should also support activities that contribute to an increased embedding of environmental sustainability within those activities directly contributing to the Lisbon Growth and Jobs Agenda. Encouraging <u>greater resource and energy efficiency</u> will improve the competitiveness of enterprises as well as meet the sustainable development aspiration of the Programme. Consequently, EU funding can provide added value through supporting activities that provide greater application of renewables technologies within business processes and initiatives that will improve the environmental sustainability of enterprises by tackling their resource efficiency.

Eligible activities

€122.186 million of EU funding has been allocated to the priority, or 33% of the Programme. Under this priority, three groups of eligible activities will be funded.

<u>Access to finance</u>

- Investor readiness programmes

- Support for risk capital funding for the region as a whole, where such schemes can demonstrate market gaps and build on the experience of past schemes

- Investment funding for early stage and start-up of new enterprises

- Targeted services for sign-posting enterprises to potential funding sources

- Initiatives that raise the capacity, skills and readiness of enterprises to assess their funding needs, manage new funding and general investor readiness

Entrepreneurship support

- Addressing gaps in pre- and post-start up provision of advice

- Promotional events for would-be entrepreneurs, particularly in more remote or deprived parts of the region, in parallel with (but distinct from) the activity set out in Priorities 3 and 4 below

- Projects that promote start-ups from groups with relatively low rates of entrepreneurship, such as ethnic minorities and women

- Projects that encourage the greater conversion of would-be entrepreneurs to start-ups

Business processes

- Projects that encourage the take-up of e-business among enterprises

- Support for the development of e-commerce strategies by enterprises

- Development and implementation of environmental and carbon-use/footprinting audits by enterprises

- Introduction of more environmentally-sustainable production systems and business processes

- Small-scale adaptation of businesses to renewable energy technologies

In addition, there is the flexibility facility, which can allow up to 10% of the funding in this priority to be used for related ESF-type activity. The use of this should be in supporting small-scale training activities associated with the entrepreneurship, e-commerce and business/resource efficiency. The flexibility could be applied in cases where the supported activity would not warrant a full-scale application to the ESF Programme as the support to be provided would be limited.

Indicators and targets

As shown in the table below, the selected indicators reflect the priority's focus on two sub-groups of activities. For activities to support access to finance:

- for output indicator, the number of enterprises receiving any form of financial support; and

- for result indicator, the increase in turnover in those enterprises.

For activities to support entrepreneurship, the following output and result indicators have been set:

- for output indicator, the number of individuals and new firms receiving advice or business consultancy; and

- for the result indicator, the number of new enterprises that result.

For activities to support business processes, the following output and result indicators have been set:

- in support for development of e-commerce skills, the output indicator is the number of enterprises supported to develop their e-commerce capacity and the result indicators are the number of e-commerce strategies and plans introduced; and

- in support for resource and energy efficiency in businesses, the output indicator is the number of enterprises supported in energy and resource efficiency projects and the result indicator is the number of environmental audits and energy/resource efficiency business processes/systems introduced as a result.

Indicator	Type	Target
Access to finance		
Number of enterprises receiving financial support	Output	250
Increase in turnover in supported enterprises (£mn)	Result	140
Entrepreneurship support		
Number of individuals/enterprises receiving advice/consultancy	Output	11,600
Number of new business starts	Result	5,500
Business processes		
Number of enterprises receiving support for e-commerce	Output	5,700
Number of enterprises receiving support for energy-saving and resource-efficiency	Output	5,700
Number of e-commerce strategies developed	Result	4,100
Number of enterprises implementing environmental audits and energy-saving/resource-efficiency systems	Result	4,100
Priority as a whole		
Number of gross jobs created	Result	13,600
Number of gross jobs safeguarded	Result	7,800
Number of net new jobs created	Impact	
Gross value added in supported enterprises	Impact	

For the priority as a whole, there are several indicators to be assessed:

- number of gross jobs created;

- number of gross jobs safeguarded;

- the number of net new jobs created; and

- gross value added in supported enterprises.

Targets have been set with reference to previous programme experience. The data for the majority of these indicators will be collected from individual participant data on a quarterly basis, as described in more detail in Chapter 9. However, there are a number of indicators which will be measured through a

specially-commissioned data-gathering exercise. These include changes in turnover and gross value added in supported enterprises and the number of net new jobs created. These will be assessed through a specifically-commissioned evaluation to be conducted in the latter half of the programming period – this would allow for a suitable period of time for the results of actions to become manifest.

Guidance on definitions of indicators will be provided by the Managing Authority to all potential applicants in advance of programming rounds. In particular, these will define the type of projects set out in the output indicators.

Baselines for the priority are set in Chapter 9, which also discusses in more detail how the data will be used for evaluation and reporting purposes.

4.5   Priority 3: Urban Regeneration

Rationale and aim

The European Council of Lisbon in March 2000 recognised that the extent of poverty and social exclusion in certain areas was a major constraint on the EU achieving its competitiveness aims. Moreover, building a more inclusive EU is considered an essential element in achieving the Union's ten-year strategic goals of sustained economic growth, more and better jobs, and greater social cohesion. Growing the economy in a sustainable way is also the Scottish Executive's main priority. However, in common with other areas of Europe, Lowlands & Uplands Scotland has a number of urban communities which are not included in many of the benefits of economic growth. Efforts to bring about lasting regeneration in such communities are a high priority for Scottish Ministers. Failure to tackle these problems is not only contrary to a commitment to social justice but also represents a failure to make best use of all of the economic resources at our disposal in order to drive growth.

In addressing sustainable urban development, the Executive's regeneration policies have been founded on the principle that it is only by promoting and encouraging economic growth that the regeneration challenges of the most deprived communities can be tackled. This view is consistent with the European Council's vision of "*growth and employment making for social cohesion*". It is, however, recognised that a key barrier to securing sustainable urban development in certain parts of the region is the high level of social and economic exclusion experienced by people living in the most deprived communities. The high levels of worklessness and the low level of economic activity are in themselves a major barrier to Scotland contributing fully to the realisation of the Lisbon growth and employment targets. In effect, social exclusion acts as a brake on Scottish ambitions to grow the economy in line with the Lisbon Agenda.

As described in Chapter 3, the Scottish Executive Regeneration Policy Statement, People and Place, puts '*capturing the unrealised potential of people and places*' at the heart of the Executive's approach to regeneration as the most effective means of securing deep and lasting regeneration

outcomes. By concentrating actions in this priority on sustainable development in the urban areas of greatest need the best use is being made of the limited funding available to make the greatest impacts on exclusion and poverty and help provide additional fuel for a drive to contribute to the Lisbon Agenda. Consequently, the priority will address Objective 3 in the Programme:

to increase the contributions of the most disadvantaged urban communities to Lisbon goals by supporting their regeneration

The Programme will work in tandem with Priority 1 of the region's ESF Programme, which tackles the parallel challenges of worklessness and social inclusion in deprived urban areas. Section 6.1 sets out how these two priorities will be co-ordinated.

As it is clear that regeneration initiatives that are imposed on disadvantaged areas are not only rarely successful but also reinforce the sense of exclusion within that community it will be a key criteria for successful sponsors to be able to demonstrate that ERDF projects in this Programme are delivered with the support and active involvement of the local community and an appropriate range of partners. As a result, the priority will place emphasis on supporting projects that integrate together a range of activities to support urban regeneration.

The priority's objective will be delivered through two inter-linked sets of activities, discussed in turn below:

- <u>to links urban areas of need with areas of opportunity</u>, by ensuring that people living in those communities can take advantage of the employment and training opportunities offered and complementing the social inclusion activity under the region's ESF programme; and

- <u>to improve the potential of urban areas to develop</u>, particularly by encouraging enterprise start-ups and sustain SME activity.

<u>Linking Urban Areas of Need with Areas of Opportunity</u>

It will be important to invest in the social and economic infrastructure required to allow people living in disadvantaged communities to take advantage of training and employment opportunities elsewhere. Priority 1 in the ESF Programme for the LUPS region will tackle exclusion of the 'hardest-to-reach' groups from the labour market. However experience suggests that ESF interventions are most effective when they form part of a long-term and integrated regeneration plan and the actions under this heading should complement the ESF actions.

EU funding can make key contributions in this area by supporting developments that encourage and empower individuals to gain access to such opportunities. This can include support for training and ICT facilities, the provision of safe and transport hubs and childcare for disadvantaged groups in parallel with ESF training support.

<u>Improving the Potential Capacity of Urban Areas to Develop</u>

In order to encourage the development of enterprise formation and development within most disadvantaged communities and sustain SMEs, additional specialised enterprise support will be funded. This will partly require improvements to the physical environment of some communities, though investments will only be limited to small-scale infrastructure in such cases, such as affordable workspace for community and private enterprises. It will be distinguished from Priority 1 by focusing on the conditions and facilities supporting enterprise development in these areas rather than direct support to the enterprises themselves.

A key aspect of this would be support for social enterprises as a means of combining support for employment growth and services to tackle social deprivation in the most disadvantaged areas. This is particularly true given that the aims and ethos of social enterprises is to intervene in these markets to create jobs and wealth. The goal should not only be to encourage such activity but to ensure that it is placed on a long-term sustainable footing.

Developing enterprises in urban communities should take place within a sustainable development frameworks. Consequently, support should be available to encourage communities to contribute to sustainable development goals through the application of renewable energy technologies for community energy needs, such as small-scale renewable energy production for local use, and the 'greening' of community regeneration construction projects.

Geographical targeting

Resources are finite and it is not possible to regenerate everywhere at the same level of engagement at the same time. The Community Strategic Guidelines and the level of funding available through this priority place restrictions on our ability to make impacts across the full spectrum of regeneration activity – physical, economic, social and cultural. In order to secure the deepest impact possible and to ensure that the ERDF funding available through this priority complements the substantial investment of domestic funding, effective targeting is essential if the value of interventions are to be maximised and a lasting legacy left after the end of the programming period.

The Scottish Regeneration Policy Statement has a specific aim to '*maximise the impact of reduced European funding streams by targeting resources on areas of greatest need*'. ERDF funds allocated to regeneration-type actions can make a more significant impact in Scotland if they are concentrated on supporting activity in the most deprived parts of the region. Consequently, funding will be targeted on selected urban areas of the region rather than be made available to all communities, linked to local plans of regeneration.

By concentrating actions in this priority on particular urban areas, the best use is being made of the limited funding available to make the greatest impacts on exclusion and poverty and help provide additional fuel for a drive to contribute

to both the Lisbon Agenda. Although the targeted areas are likely to change through the programming period, the principles for their selection should remain constant. Support will be limited to those Local Authority areas that are:

- areas prioritised in key Scottish strategies, specifically Workforce Plus, the NEET Strategy and the Regeneration Policy Statement; and

- in addition, to reflect any changes in relative deprivation within the period covered by these strategies, other Local Authority areas with the ten highest shares of their population in the 15% most deprived data-zones, as measured by the Scottish Index of Multiple Deprivation, will be considered eligible.

At present, these areas would account for approximately 60% of the region's population, but it is anticipated that the list of eligible areas will change through the Programme, reflecting changes in the indicators and the relevant policy focus. Consequently, the areas will be identified by the Managing Authority in advance of each project selection round using the methodology above.

Projects will be supported which address the challenge of these areas, although activity can be located elsewhere in the Local Authority area. Moreover, where projects covered beneficiary groups that overlap with similarly deprived data-zones in bordering Local Authorities, up to 10% of the project award could be in the neighbouring data-zones.

Individual projects will be eligible for support through the priority, though the emphasis will be on projects that integrate several of the eligible activities. In addition, a share of funding will be set aside to support projects that are part of integrated packages of support put forward by Community Planning Partnerships. This may include a range of small projects, linked together into a common aim of improving the sustainability of communities within the list of eligible areas. The approach is described in more detail in section 6.1 with respect to bringing together ERDF and ESF funding to support integrated action plans. The 10% geographical flexibility described above would not apply to the funding for Community Planning Partnerships.

Eligible activities

€101.509 million of EU funding has been allocated to the priority, or 27% of the Programme, to support the following activities, preferably integrated together into more co-ordinated projects.

Linking urban areas of need with areas of opportunity

- Support for locally-based job brokerage schemes that aim to match disadvantaged individuals with employment opportunities

- Supporting safe transport hubs to link areas of need with those of opportunity

- Support for investment in increased local access to ICT facilities within communities with the intention of improving skills of local people seeking to re-enter the labour market and increasing access to web-based public services

Improving the potential capacity of urban areas to develop

- Support for refurbishment and enhancement of locally-based training/learning and e-skills centres

- Support for refurbishment of existing facilities and workspace to make them suitable for new or established SMEs (especially those that employ 'green design' principles)

- Support for small-scale conversion and adaptation to industrial sites and business centres/facilities that offer employment or training opportunities to people living in targeted areas (especially those that employ 'green design' principles)

- Support for small-scale energy production from renewable energy technologies in response to local energy needs

In addition, there is the flexibility facility, which can allow up to 10% of the funding in this priority to be used for related ESF-type activity. This is anticipated to assist projects with limited training activity required in providing support/advice to enterprises in these communities (eg. in e-commerce and e-skill centres). The flexibility could be applied in cases where the supported activity would not warrant a full-scale application to the ESF Programme as the support to be provided would be limited.

Indicators and targets

As shown in the table below, the selected indicators reflect the priority's focus on two sub-groups of activities. For activities to support <u>linking urban areas of opportunity with areas of need</u>:

- for output indicators, the numbers of job brokerage initiatives, ICT facilities and local transport hub projects supported in the target areas; and

- for result indicators, increases in the numbers of individuals gaining employment as a result of the supported job brokerage initiatives and ICT facilities (as measured at least six months after the support has been completed) and improvements in journey times resulting from the transport hub investments.

For activities to support <u>developing the capacity of urban areas</u>, the following output and result indicators have been set:

- for output indicators, the number of local facilities supported (specifically e-learning, childcare and other community centres), the area of business space created or modified for use by local enterprises and the number of renewable energy projects supported; and

- for the result indicators, the number of enterprises supported, increases in the numbers of those gaining employment through the supported facilities and increases in the share of renewables in local energy usage.

Indicator	Type	Target
Linking urban areas of opportunity with areas of need		
Number of job brokerage initiatives supported	Output	210
Number of ICT facilities supported	Output	350
Number of transport hub projects supported	Output	25
Increase in the number of individuals gaining employment through supported job brokerage schemes	Result	
Increase in the number of individuals gaining employment through supported ICT facilities	Result	
Time saved per journey (journey time *x* freight/passenger volume)	Result	
Improving the potential capacity of urban areas to develop		
Number of e-learning/childcare and other community facilities supported	Output	350
Area of business space created or modified (m^2)	Output	7,500
Number of renewable energy projects supported	Output	180
Number of enterprises supported	Result	1,100
Increase in the number of individuals gaining employment through supported e-learning/childcare/community facilities	Result	
Increase in share of energy for renewable resources in supported areas	Result	
Priority as a whole		
Number of gross jobs created	Result	4,500
Number of gross jobs safeguarded	Result	3,600
Number of net jobs created	Impact	

For the priority as a whole, there are several indicators to be assessed:

- number of gross jobs created;
- number of gross jobs safeguarded; and
- the number of net new jobs created.

Targets have been set with reference to previous programme experience. The data for the majority of these indicators will be collected from individual participant data on a quarterly basis, as described in more detail in Chapter 9. However, there are a number of indicators which will be measured through

specially-commissioned data-gathering exercises. These include increase in employment resulting from support to job brokerage initiatives and facilities, changes in journey times and changes in the share of local energy usage accounted for by renewables and the number of net new jobs created. These will be assessed through specifically-commissioned evaluations to be conducted in the latter half of the programming period – this would allow for a suitable period of time for the results of actions to become manifest.

Guidance on definitions of indicators will be provided by the Managing Authority to all potential applicants in advance of programming rounds. In particular, these will define the type of projects set out in the output indicators and other key definitional issues such as how to count employment gains resulting from support to facilities.

Baselines for the priority are set in Chapter 9, which also discusses in more detail how the data will be used for evaluation and reporting purposes.

4.6   Priority 4: Rural Development

Rationale and aim

The benefits of growth need to be available to people in all parts of Scotland. At present, as the socio-economic analysis underlined, peripheral rural areas do not share equally in the opportunities for growth. GDP and average wage levels in remote and rural parts of Scotland are strikingly lower than those in cities. There is a real danger that current trends such as the focus on metropolitan regions will work to reinforce these differences by permitting a dual pattern of development to emerge. Under such a pattern of development, innovation and growth would centre on city-based development poles, and people beyond the travel-to-work areas for the cities would not share in the prosperity thus created. The economic role of rural areas could diminish to the provision of residential and retirement services unless appropriate alternative models of development are supported. Priority 4 in this Programme is designed to meet that need.

At the same time, it is important that the Structural Funds complement other sources of EU funding for rural areas to maximise the potential for a coordinated, comprehensive approach to rural development. As Chapter 6 sets out, the strategic complementarity of the Structural Funds with the Scotland Rural Development Programme and the Scottish plan for the European Fisheries Fund has been an important design principle in the ERDF programme. A separate priority which can address related but distinct areas of rural development to the other two funds will help ensure such coordination is embedded in the structure of Structural Funds spending.

In Lowlands & Uplands Scotland, rural areas are not concentrated in any one part of the region. Although the Scottish Borders and Dumfries & Galloway constitute a large, contiguous rural area, there are other significant rural areas in North-East and parts of Central Scotland. Despite the scattered nature of rural areas across the Lowlands & Uplands Scotland region, the National

Planning Framework for Scotland recognises that some rural areas of Scotland share key similarities. These include "*low population densities, sparse settlement patterns and valuable natural heritage and cultural resources*". The Framework suggests that the future for rural Scotland lies in economic diversification and environmental stewardship. It also recognises that "*higher education has a key role to play in developing the knowledge economy in rural areas*" and concludes that "*across rural Scotland the aim should be to develop a diverse, modern economy with an international perspective based on environmental and cultural resources and adding value through long term planning, careful resource management and attention to good design.*"

Reflecting this, and the intention of developing a priority that can balance the need for rural areas to establish their internal sources of competitiveness as well as link to urban growth poles in the region, the priority implements Objective 4 of the Programme:

> **to maximise the contribution of rural areas to achieving Lisbon goals with a view to developing sustainable economic growth**

To achieve this aim, and recognising the limited resources of the programme, the priority will contribute to two broad sets of activity. In this, the Programme will be complementing both national strategies, such as the Scottish Rural Development Programme as well as major local strategies. The key themes supported by the priority are:

- to assist the strengthening and renewal of rural industries; and

- to support the development of key shared services in the region to underpin economic and community sustainability.

Strengthening Rural Industries and Diversification

In addressing the role of rural areas in regional competitiveness, there can be a tendency in economic development policy to suggest that rural areas are merely passive recipients of urban-centred development. In this context, there are two parallel, but distinct, avenues for supporting the development of rural areas where the challenges of peripherality and a limited economic base are most acute. The first is to strengthen the competitiveness of traditional, largely primary-based industries, such as food and drink, forestry, textiles as well as tourism, particularly where those industries have strong cross-over into other activities (eg. 'food and drink' tourism). The Scottish Rural Development Programme will focus on the primary growing and processing at the source of these industries, but this priority will contribute to wider business and commercial development of key natural resources. Section 6.2 sets out the relationship between these funding streams in more detail.

A related strand of intervention will focus on diversification strategies. Eco-friendly energy generation and software development are among more recent developments in rural areas, and innovative sources of growth such as these should be supported by the Programme where they build on the strengths of the area without compromising the features that make it special. In supporting

the development of emerging industries based on these new technologies, the priority will need to consider the importance of fostering local supply chains that would embed as many stages of the sector in the local economy as possible.

Support for more general RTD and innovation, new firm formation and access to capital will continue to be the responsibility of Priorities 1 and 2. Priority 4 will focus on other activities that will underpin the competitiveness of these sectors, particularly with regard to marketing and export development, new production strategies, business advice on market and product diversification and other business process to develop competitive niches in key local sectors such as tourism, forestry and food and drink.

Some of the activity described here will be delivered for Dumfries & Galloway and the Scottish Borders areas by the South of Scotland Alliance partnership as an Intermediate Delivery Body, as detailed in the Implementing Provisions chapter below.

<u>Supporting Development of Key Shared Services to Underpin Rural Sustainability</u>

Deficiencies in shared services are one of the key factors behind the lagging development of many rural areas. In order for rural areas to maximise fully their contributions to the Lisbon Agenda, fundamental weaknesses in the sources of their competitiveness need to be addressed, particularly in their basic service provision. These services can cover a variety of areas – their specific nature will vary between localities and where they form a key bottleneck to economic development, the Programme will focus resources on them.

Across rural areas as a whole, these services can relate to the fragility of local communities as drivers of their local economies and can include the provision of ICT and training facilities, both of which can be important for sustaining a local enterprise base. Given the limits on infrastructure investment in the region, the focus would not be on supporting capital developments, apart from some small-scale actions, but in encouraging greater use of existing infrastructure, enabling enterprises and communities to identify their service needs and develop strategies for tackling these and piloting new approaches to addressing these issues (in keeping with the programme's focus on innovative actions). In this context, there are two services worth highlighting because of their importance to the sustainability of the rural economy: higher and further education; and accessibility.

- Higher and further education. Scottish small towns and rural areas have traditionally shown a high regard for educational values, and achieved high levels of educational success. Also traditionally, graduates from such areas have moved elsewhere on qualifying, often returning only later in life. A major economic challenge for peripheral areas is how to retain or replace the expertise so generated. In the Highlands & Islands, this challenge is being addressed with the development of the University of the Highlands & Islands, an innovative, 'distributed' university that is intended to act as a research and skills anchor for the region. There is scope for using support in Priority 4 to improve the higher and further educational resources of rural areas. An important development in recent years has been the expansion of further education access to market towns and the establishment of a higher education presence in rural centres. ERDF funding has a vital part to play in encouraging higher and further education bodies to engage with SMEs in rural areas and assist the development of innovative enterprises through initiatives to reach out to rural enterprises and communities.

- Accessibility. Access and public transport are critical issues for rural areas. Accessibility issues were identified in the socio-economic analysis as a major restraint on the ability of rural enterprises to develop markets as well as on the attractiveness of rural areas to enterprise investment from outside. The scope of the Programme for addressing the problems of rural transport is limited given resources and EU eligibility criteria. However, the Programme can ensure that transport development in rural areas will contribute to sustainable development through support for projects that pilot new vehicles and fuels and transport schemes for reducing emissions and public transport fleet conversion.

Geographical targeting

The funding should not be available across all areas that can potentially demonstrate rurality. It is important that the limited funding in this priority is not thinly spread but can make effective contributions to the most peripheral, disadvantaged rural parts of the region. Consequently, eligibility will be determined on the basis of 'remote rural' and 'accessible rural' areas, as defined in the Scottish Executive's six-fold urban-rural classification: these are defined as settlements with less than 3,000 people and within 30 minutes driving of settlements of 10,000 or more. With limited resources, the Programme will need to concentrate on those Local Authority areas where rurality is particularly pronounced. Consequently, eligibility would be for those Local Authorities with more than 35% of their population in 'remote' or 'accessible' rural areas.

At present, these areas would account for approximately 17% of the region's population. The areas will be identified by the Managing Authority in advance of each project selection round using the methodology above.

Projects which address the challenge of these areas will be supported, although activity can be located elsewhere in the Local Authority area, as long as the impact in the target area can be demonstrated. Moreover, where projects cover activities in remote and accessible rural areas in adjacent Local Authorities, up to 10% of the project award could be in the neighbouring area even if it is not one of the eligible Local Authorities.

Eligible activities

€51.13 million of EU funding has been allocated to the priority, or 14% of the Programme. It can be used in support of the following activities under each of the themes identified above.

Rural diversification

- Support for sector-wide marketing initiatives to promote diversification in traditional industries in the region, particularly through identification of new market opportunities (including niche and exporting strategies)

- Support for enterprises and groups of enterprises in developing new sources of supply and production processes

Key shared services

- Support for refurbishment and enhancement of business centre and childcare facilities and training/learning centres

- Small-scale support for ICT investments enabling distance learning and higher and further education outreach in remote communities

- Small-scale business site development (especially those that employ 'green design' principles)

- Development of educational access strategies for rural areas

- Start-up support for the development and initial implementation of community transport initiatives

- Piloting of emission-reducing and clean-energy vehicles and transport systems

In addition, there is the flexibility facility, which can allow up to 10% of the funding in this priority to be used for related ESF-type activity. This would be expected to be used in supporting small-scale training activities associated with the sector-wide initiatives above, the development of community facilities (eg. ICT/business centres) and emission-reducing transport initiatives. The flexibility could be applied in cases where the supported activity would not warrant a full-scale application to the ESF Programme as the support to be provided would be limited.

Indicators and targets

As shown in the table below, the selected indicators reflect the priority's focus on two sub-groups of activities. For activities to support <u>rural diversification</u>:

- for output indicators, the number of enterprises supported; and

- for result indicators, the numbers of new marketing initiatives and enterprises introducing significant improvements to production and supply processes.

For activities to support <u>key shared services for rural areas</u>, the output indicators reflect the range of activities supported

- the number of community facilities supported, including e-learning and childcare facilities;

- the area of business space modified/created for enterprises;

- the number of educational access strategies and projects supported; and

- the number of local transport initiatives supported.

The results indicators would be:

- the number of enterprises benefiting from the supported community facilities;

- occupancy rates of the modified/created business space;

- the number of enterprises benefiting from the new educational access strategies; and

- improvements to journey times.

For the <u>priority as a whole</u>, there are several indicators to be assessed:

- number of gross jobs created;

- number of gross jobs safeguarded;

- the number of net new jobs created;

- increase in turnover; and

- increase in gross value added.

Targets have been set with reference to previous programme experience. The data for the majority of these indicators will be collected from individual participant data on a quarterly basis, as described in more detail in Chapter 9. However, there are a number of indicators which will be measured through a specially-commissioned data-gathering exercise. These include changes in turnover and gross value added, the number of enterprises accessing higher/further education research and training resources, time savings as a result of the local transport initiatives, occupancy rates after two years and the number of net new jobs created. These will be assessed through specifically-commissioned evaluations to be conducted in the latter half of the

programming period – this would allow for a suitable period of time for the results of actions to become manifest.

Guidance on definitions of indicators will be provided by the Managing Authority to all potential applicants in advance of programming rounds. In particular, these will define the type of projects set out in the output indicators and definitional issues such as 'enterprises benefiting from supported facilities'.

Baselines for the priority are set in Chapter 9, which also discusses in more detail how the data will be used for evaluation and reporting purposes.

Indicator	Type	Target
Rural diversification		
Number of enterprises supported	Output	1,400
Number of new marketing initiatives	Result	910
Number of enterprises introducing new supply and production processes	Result	910
Key shared services		
Number of e-learning/childcare and other community facilities supported	Output	40
Area of business space created or modified (m^2)	Output	2,400
Number of educational access projects supported	Output	20
Number of local transport projects supported	Output	20
Number of enterprises benefiting from supported facilities	Result	900
Occupancy rates of business space after 2 years	Result	
Number of enterprises accessing higher and further education research/training resources	Result	
Time saved per journey (journey time *x* freight/passenger volume)	Result	
Priority as a whole		
Number of gross jobs created	Result	1,400
Number of gross jobs safeguarded	Result	1,300
Number of net new jobs created	Impact	
Increase in turnover in supported enterprises	Impact	
Increase in gross value added in supported enterprises	Impact	

4.7   Priority 5: Technical Assistance

Technical assistance support will be provided to assist the management and administration of the programme. This will include activities in support of the various selection, appraisal, management and committee groups, the monitoring of financial and performance progress, Programme publicity and

communication, and facilitating the exchange of best practice. Technical assistance will be used to support the work of the Intermediate Administration Bodies, which are described in Chapter 7.

Eligible activities

€9.023 million of EU funding has been allocated to the priority, or 2% of the Programme to support the following eligible activities:

- Servicing Programme groups and committees

- Communicating decisions and policy to partners

- Implementation of a common monitoring and evaluation framework and provision of regular monitoring reports

- Provision of advice to applicants

- Publicity and awareness-raising of the Programme among all beneficiaries and applicants in line with the activities set out in the publicity section in Chapter 7

- Annual reporting on the Programme

- Development of ICT systems to assist the application, monitoring and financial control of the Programme

- Evaluation studies in line with the strategy set out in Chapter 9

4.7   Categories of Assistance

As set out in Article 9 of the General Regulation, Programmes under the Competitiveness Objective must meet an target of 75% for expenditure on activities contributing directly to the objectives of the Integrated Guidelines for Growth and Jobs (2005-08). The relevant categories of assistance are listed in Annex IV of the General Regulation.

While the 75% target will be met, the ERDF Programme for Lowlands & Uplands Scotland has set itself an ambition of achieving 78% of expenditure. A table with a breakdown by category of the programmed use of the Funds is attached in the Annex, though this will be indicative only.

5   FINANCIAL ALLOCATIONS

The financial allocations for each year of the programme are shown in the table below. €375.958 million of Community funding will contribute to a Programme of €970.89 million in total, resulting in a target Programme intervention rate of 39% (as calculated on the basis of total funding).

Table 12: Year by source of funding for the Programme (in €)

Year	Community Funding (a)	National Public Funding (b)	National Private Funding (c)	Total Funding (d) = (a)+(b)+(c)	Co-financing Rate (e) = (a)/(d)
2007	50,570,825	63,590,003	16,435,518	130,596,346	39%
2008	51,582,242	64,861,803	16,764,229	133,208,274	39%
2009	52,613,886	66,159,039	17,099,513	135,872,438	39%
2010	53,666,164	67,482,220	17,441,503	138,589,887	39%
2011	54,739,487	68,831,864	17,790,333	141,361,684	39%
2012	55,834,277	70,208,502	18,146,140	144,188,919	39%
2013	56,950,963	71,612,672	18,509,063	147,072,698	39%
2007-13 total	375,957,844	472,746,103	122,186,299	970,890,246	39%

For the four key priorities of the Programme, resources have been relatively evenly distributed, as shown in Table 13. The rationale for the allocation between these priorities reflects several factors, but broadly, Priorities 1 and 2 have received the majority share of funding because of their focus on region-wide challenges directly related to the Lisbon Agenda while Priorities 3 and 4 jointly have less funding in recognition of their sub-regional focus.

- Priority 1 has received nearly a quarter of the funding, reflecting the importance of research and development within the Programme and the role of Scottish Enterprise as an IDB in delivering some of the priority's objectives (as set out in the Implementing Provisions chapter). It has a higher co-financing rate because of the higher risk of RTD and innovation projects and the greater need for Structural Funds to ensure that key projects will be forthcoming.

- Priority 2 has the highest share of funding because it covers a range of important, inter-related factors influencing enterprise development in the region. It also takes account of the scope for major activity in support of access to finance (as described in an annex) and in recognition of the region-wide eligibility of funding

- Priority 3 has a significant share of funding because of the number of significantly-deprived communities which can be eligible for the funding and in recognition of the need for a strong urban dimension to the Programme.

- Lastly, Priority 4 has the smallest share of funding because of the more limited number of areas and scope of activity covered by the priority.

Table 13: Priorities by source of funding (in €)

	Community Funding (a)	National Public Funding (b)	National Private Funding (c)	EIB Contributions	Other	Total Funding (d) = (a)+(b)+(c)	Co-financing Rate (e) = (a)/(d)
Priority Axis 1	92,109,671	112,578,487	0	0	0	204,688,158	45%
Priority Axis 2	122,186,299	122,186,299	122,186,299	0	0	366,558,897	33%
Priority Axis 3	101,508,618	152,262,925	0	0	0	253,771,543	40%
Priority Axis 4	51,130,268	76,695,402	0	0	0	127,825,670	40%
Priority Axis 5	9,022,988	9,022,990	0	0	0	18,045,978	50%
Total	375,957,844	472,746,103	122,186,299	0	0	970,890,246	39%

The intervention rates have been set to reflect previous ERDF experience and to ensure that the minimum required EU funding would be provided to match-fund projects.

6   CO-ORDINATION WITH OTHER FUNDS

Co-ordination of the Structural Funds with other relevant funding streams is a regulatory requirement, but it is given greater importance in the 2007-13 programming period. Compared to previous funding rounds, the scale of funding in Lowlands & Uplands Scotland is significantly reduced, making it more critical that the value of the 2007-13 Structural Funds are enhanced by ensuring they work closely with other sources of funding. Similarly, the scope of eligibility in the 2007-13 programming round is more targeted than in previous rounds, giving greater opportunities for Structural Funds to work in combination with other, similarly targeted policies.

In this context, there are several relevant funding streams. This chapter discusses how the ERDF Programme will work closely with:

- the European Social Fund;

- the European Territorial Co-operation Objective;

- EU support for agriculture and fisheries;

- EU research funding; and

- support through the European Investment Bank.

6.1   European Social Fund

As the other major funding stream within EU cohesion policy, it is essential that ERDF works closely with the European Social Fund, while recognising their distinctive objectives. In parallel with this ERDF programme, there will be a European Social Fund programme for the Regional Competitiveness and Employment Objective, covering the same eligible area. This is an important change from the 2000-06 programming period, where the ERDF programmes for Lowlands & Uplands Scotland (through Objective 2) did not cover all of the eligible territory for the principal ESF programme for the area (through Objective 3). In addition, there was an element of ESF in the Western Scotland Objective 2 programme – in the 2007-13 programming period, programmes will be mono-fund, avoiding some of the problems of potentially overlapping funding streams in the 2000-06 period.

The experience of the 2000-06 programming period in co-ordinating ERDF and ESF funding (as discussed in Chapter 3 above) has fed into developing the approach for the 2007-13 programming period. As the mid-term evaluations of the 2000-06 programmes attested, ERDF and ESF co-ordination was broadly successful but there have been lessons to be learnt. Foremost among these has been the need to build in greater complementarity at the start of the programme, not least with respect to setting up formal mechanisms to ensure that not only co-ordination takes places systematically, but that it is monitored and assessed on a regular basis.

The main co-ordination mechanism will be through a single Programme Monitoring Committee overseeing both the ESF and the ERDF programmes

for the whole LUPS area. The arrangements for the Programme Monitoring Committee (PMC) are discussed in detail in Chapter 7.

As part of this annual reporting, the use of the funding flexibility allowed in the 2007-13 programming period will also be reviewed. Under the Article, up to 10% of total ERDF Programme resources can be spent on ESF-related activities. This will enable projects to avoid unnecessary applications on projects where such activities are likely to be a small proportion of total project funding. At the start of the programming period, the Managing Authority will set out detailed guidelines on the types of activities that could be covered by the flexibility rule. The Managing Authority will monitor spending on 'ESF' activities and provide the information as part of the annual report on ERDF-ESF co-ordination. Details of how this flexibility mechanism may operate for the individual priorities is set out in Chapter 4 above.

As set out in section 4.5 above, one of the ERDF Programme priorities will be delivered jointly with one of the priorities in the ESF programme for the LUPS region. Joint awards of funding under Priority 1 (Progressing through Employment) of the ESF Programme and Priority 3 (Urban Regeneration) of the ERDF programme will be made to bidding projects. Priority 1 of the ESF Programme concentrates on supporting those outside the workforce to secure employment, particularly among the most disadvantaged groups, and has a clear strategic fit with the community economic development focus of Priority 3 in the ERDF programme. Both priorities will have the same geographical eligibility criteria which will be reviewed and changed at the same time during the course of the programming period. Projects will not be required, but will be encouraged to put forward action plans that will show how ERDF and ESF funding can be used in tandem within the same project. While applications need to be made separately to each Programme, appraisal and project selection between both programmes will be co-ordinated through advisory groups (as described in the Implementing Provisions chapter below). Applications will need to be specific in allocating distinct activities, expenditure and outcomes to each Fund. Projects will also be required to report on the co-ordination between both sets of Funds on an annual basis.

Use Community Planning Partnerships

For the first years of the period, the Programme will make limited use of the Community Planning Partnerships model for delivering some funding. As set out in Chapter 3 above, the Partnerships are local networks of key community regeneration and social inclusion actors which are charged with setting out their collective goals and spend on tackling regeneration/inclusion within Scottish-wide policy through Regeneration Outcome Agreements. They have been allocated Community Regeneration Fund support to take forward new activities within these Agreements. The partnership-based approach and the use of co-ordinated public funding offers clear opportunities to the Programme to extend the value added of the Funds. An example of such an integrated bid could include: funding the development of e-learning facilities under the ERDF Programme and the rolling-out of an e-skills learning project for target groups

under the ESF Programme as well as support for some of the local initiatives taken forward by the Urban Regeneration Companies.

A small number of Community Planning Partnerships will be selected to deliver funding under Priority 3 of the Programme in conjunction with ESF Priority 1 at the start of the programming period. A minority share of the allocation under the priorities will be available to support these Partnerships on a competitive basis and using the eligibility criteria of both priorities for selection (notably the geographical criteria). Selection will be on the basis of the eligibility criteria set out in the priority description above as well as the capacity of the Community Planning Partnerships to administer the Funds successfully. Detailed criteria – as well as further examples of integrated action plans – will be provided by the Managing Authority in advance of the bidding round.

The approach will encourage a more co-ordinated, area-based approach to addressing areas with the most severe social inclusion and employability challenges. It is distinct from the Intermediate Delivery Body mechanism, which is described in detail in the Implementing Provisions chapter. Awards will be made on a competitive basis for a share of the joint ERDF Priority 3-ESF Priority 1 allocation. Funding will be provided for two years to support eligible activities as set out in the priority descriptions – this will act as a pilot for the approach to funding delivery. At the end of the two-year period, the Partnerships will be evaluated for the effectiveness and value added in their use of the funding, after which, decisions would be taken on whether the funding initiative would be continued.

Funding would be delivered through specified accountable bodies to be used in activities set out in line with key local strategies. Activity would be set out in annual Structural Funds Outcome Agreements. The Agreements would identify the specific activities to be funded by the ERDF contribution, how the funding would be used in conjunction with the ESF contribution (and identifying clear ESF outcomes for the funding), make clear the additionality of activity and set financial and performance targets in line with the priority targets. The Agreements would be monitored regularly by the Managing Authority, which would report to the PMC on the performance of the selected Community Planning Partnerships on an annual basis.

Other Co-ordinated Activity

Less formally, Priority 2 of the Programme has also been designed to complement Priority 2 (Progressing through Employment) of the ESF Programme. The focus of Priority 2 on enterprise development needs of SMEs, new enterprises and entrepreneurs will complement ESF Priority 2's support of the skills needs of entrepreneurs and SME managers. In addition, support for developing the business use/access to higher/further education services under Priority 4 of the Programme will also complement the support for improving access to lifelong learning under ESF Priority 3. Where complementary activities fall into these priorities within the same project, co-ordinated joint applications will be invited to ensure that EU funding for

projects is as integrated and strategic as possible. Such activity will be distinct from the Community Planning Partnership and the Intermediate Delivery Body activity, as it will be taken forward on a case-by-case basis with individual projects that are in a position to deliver high value-added through activity linking together two different priorities.

Again, as set out above, while applications need to be made separately to each Programme, appraisal and project selection between both programmes will be co-ordinated through advisory groups (as described in the Implementing Provisions chapter below). Applications will need to be specific in allocating distinct activities, expenditure and outcomes to each Fund. Projects will also be required to report on the co-ordination between both sets of Funds on an annual basis.

6.2   Territorial Co-operation Objective

As well as the ERDF and ESF programmes under the Regional Competitiveness and Employment Objective, there are a number of programmes in the different strands of the Territorial Co-operation Objective which cover part of the LUPS area. Activity supported under these Co-operation programmes will be co-ordinated, where appropriate, with the ERDF programme.

In the transnational co-operation strand, there are two relevant programmes. The Northern Periphery programme (NPP) principally covers the Highlands & Islands but allows some eligibility in the LUPS area. The programme's partners include Denmark, Finland, Ireland and Sweden within the EU and Norway, Iceland, Faroes and Greenland outwith the EU. The programme's thematic priorities mesh with the eligible activities set out under all Priorities in the ERDF programme. Similarly, the area is eligible under the North Sea programme. The programme's priorities relate to all priorities.

The transnational programmes are continuations of programmes from the 2000-06 period and will build on their experience. Under the cross-border co-operation strand, the LUPS area will be eligible for support from a programme with partners in Northern Ireland and Ireland. Its themes had not been finalised at the time of the finalisation of the ERDF Operational Programme, but the eligible activities are likely to fit with Priorities 1 and 4 of the ERDF programme through support for best practice and joint development activity of RTD, innovation, entrepreneurial support, and economic development in rural areas.

To ensure full complementarity with the co-operation programmes, the following would take place:

- projects bidding for ERDF funding would be required to demonstrate knowledge and fit with any relevant funded projects under the NPP in their applications; and
- on an annual basis, the Programme Monitoring Committee would receive a report by the Managing Authority that would summarise

activities being supported under the NPP in order to refine the demarcation of eligible activities in the priorities and better inform its recommendations on projects to be supported.

As Managing Authority, the Executive will identify opportunities for projects that have received funding from one programme to have a later stage of their development funded under another programme, if appropriate – for example, a project developing RTD in a key sector through Priority 2 of the ERDF Programme could benefit in a successive development phase through best-practice/benchmarking work with international partners through one of the transnational programmes.

There is an option for inter-regional co-operation to be pursued as a strand of the ERDF programme. Given the limited funding and the greater effectiveness of keeping co-operation activities under a single banner, the option is not currently envisaged for the LUPS area in the 2007-13 programming period.

6.3   The European Agricultural Fund for Rural Development

Both the General and the ERDF Regulations specify that the Operational Programmes must set out how ERDF and the European Agricultural Fund for Rural Development (EAFRD) will complement each other. EAFRD in Scotland is governed by the Scottish Rural Development Programme, which covers the whole of Scotland. The Managing Authority for the Fund is the Scottish Executive through the Environment and Rural Affairs Department.

The ERDF Programme and the Scotland Rural Development Programme (SRDP) have been developed in parallel by the Scottish Executive with particular attention given to the areas where project eligibility could overlap. The consultations on the two sets of documents made explicit reference to each other with responses solicited on the relationship between the two.

The main area where demarcation is important is in Priorities 1 and 2 of the ERDF programme, particularly with the support for key sectors in a largely rural economy, and Axis 3 of the SRDP. Both programmes have some common areas of scope, as set out by their respective regulations in supporting business viability, more sustainable economic use of natural assets and addressing the community dimension to economic development. To ensure that there is no overlap in eligibility, but at the same time, that there is full complementarity in the activities supported, the lists of eligible activities of the programmes have been drawn up on a regional basis so that projects receiving funding through one stream in one phase of their development could receive follow-on support from the other stream in a new development phase. Demarcation will take place in terms of eligible activities as well as the target of support (eg. the SRDP will concentrate on micro businesses, especially those in the agricultural and forestry sectors, while ERDF will support larger enterprises based on other sectors). The table below sets out the eligible activity areas where demarcation is necessary.

At the same time, at local level, relevant projects will be expected to take explicit account of priority-setting by the local Rural Development Fora for Axis 3 of the Scottish Rural Development Programme at the time of application. Both Programmes will include representatives in cross membership of the different decision-making bodies.

Complementarity will be regularly also be reviewed through an annual meeting of the respective Managing Authorities. This will produce a report on joint implementation of the different Funds which will be presented on an annual basis to the Programme Monitoring Committee as part of annual reporting exercises. The PMC would then be able to refine eligibility criteria and project recommendations to take account of supported activity through the SRDP. As part of any mid-term evaluation, the strategic and operational fit between the programmes will be part of formal evaluation.

Table 14: Demarcation of SRDP and ERDF activity

Type of activity	SRDP eligible activities	ERDF eligible activities
Transport infrastructure	• Not directly supported	• No transport infrastructure
Tourism	• New or upgraded tourist accommodation • Small-scale tourist visitor infrastructure • Improvements to historical sites • Support as an additional benefit of other investment eg agri-environment or adding value to agriculture and forestry products	• No support for infrastructure development • Improving tourism business practices in targeted rural areas (eg. marketing) and products
Support for diversification of agriculture and forestry	• Support for the development of new agricultural and forestry products • Development and restructuring of agricultural and forestry businesses • Support for micro-enterprises in the rural economy	• Support for the innovation capacity of enterprises developing new products based on primary sectors • Support for businesses based on non-agricultural/forestry sectors • Support for firms larger than micro scale • No direct support for agricultural, forestry, fishing and aquaculture enterprises

<u>Renewable energy</u>	• Small-scale renewable energy facilities for enterprises and communities • Developing raw materials for renewable energy (eg. biomass)	• Support for small-scale renewable energy facilities in urban areas • Support for developing renewable energy research excellence and commercialisation opportunities • Support for new and high-growth enterprises developing renewable energy
<u>Support for biodiversity</u>	• Actions attributable to support and enhance biodiversity	• Support for enterprises developing new products from biodiversity • No direct support for biodiversity, but commitment to ensuring supported projects are 'biodiversity-proofed'
<u>Provision of local services</u>	• Direct support to rural community services	• Development of facilities for use in common by rural enterprises and community facilities with an economic development purpose • Support for plans and strategies to improve community services with an economic development dimension, but not direct support to the services themselves

6.4   The European Fisheries Fund

The regulatory requirements applying to the EAFRD apply similarly to the European Fisheries Fund (EFF). In Scotland, EFF strategic priorities are set out in [add] and the Managing Authority is also the Scottish Executive Environment and Rural Affairs Department. Demarcation issues are more limited in the case of the EFF, because of the limited geographical overlap with the ERDF programmes. The main parts of the LUPS area where EFF support is available is in the coastal zones of the region.

The main areas where complementarity is evident are set out in the following table.

Table 15: Demarcation of EFF and ERDF activity

Type of activity	EFF eligible activities	ERDF eligible activities
Transport infrastructure	• Limited support for port developments directly related to the fishing industry	• No transport infrastructure
Support for diversification of agriculture and forestry	• Support for the development of new fisheries and aquaculture products • Market research to support aquaculture and fisheries, especially for export and niche markets	• Support for the innovation capacity of enterprises developing new products based on primary sectors as well as for high-growth companies based dependent on these sectors • Support for firms larger than micro scale • No direct support for agricultural, forestry, fishing and aquaculture enterprises
Support for biodiversity	• Sustainable conservation of fish stocks and their ecosystems • Support inshore marine environment	• Support for enterprises developing new products from conservation • No direct support for conservation, but commitment to ensuring supported projects are 'biodiversity-proofed'
Provision of local services	• Support for Community groups in the preparation and implementation of the local development strategy	• Development of facilities for use in common by rural enterprises and community facilities with an economic development purpose

As with the EAFRD, the two Managing Authorities will meet on an annual basis to review strategic and operational co-ordination and report back to the Programme Monitoring Committee.

6.5 EU Research Programmes

The 7th Framework Programme for Research, Technology Development and Demonstration Activities has combined all research-related EU activity into a common framework addressing how research can contribute to achieving the Lisbon Agenda goals. The broad objectives of FP7 have been grouped into four categories: cooperation; ideas; people; and capacities. For each type of objective, there is a specific programme corresponding to the main areas of EU research policy though all are designed to work together to promote and encourage the creation of European poles of (scientific) excellence.

For the ERDF Programme, the key areas of complementarity lie in the co-operation area. FP7 will support calls for transnational research projects in a number of areas, some of which overlap with the research focus of the ERDF Programme, particularly:

• food and biotechnology, including food products, life sciences, biotechnology and biochemistry for sustainable non-food products and processes; and

- energy, including renewable electricity generation, smart energy networks, and energy efficiencies and savings.

The activities supported through the ERDF Programme have been defined to be demarcated from FP7 but to complement supported projects where appropriate. Support under Priority 1 will focus less on 'blue-sky' research than in the industrial application of technologies.

Similarly, the EU <u>Competitiveness and Innovation Framework Programme</u> also highlights areas identified in the socio-economic analysis for the region, such as competitiveness of enterprises, promotion of innovation and the promotion of energy efficiency. One of the key blocks of activities is the Entrepreneurship and Innovation Programme which fits with support under Priority 1 of the ERDF Programme.

Complementarity between the different funding streams will be reviewed with the following instruments:

- ERDF project applications would be required to show strategic fit and clear distinction from any relevant projects supported through FP and the CIP; and

- the Managing Authority will report annually to the Programme Monitoring Committee on project activity supported under the research streams to allow the PMC to make more informed decisions on eligibility criteria in the ERDF Programme and project recommendations.

6.6   The European Investment Bank

The General Regulation specifies the need for the Operational Programme to discuss how the cohesion-policy funding initiatives of the European Investment Bank will be co-ordinated with the use of Structural Funds. The principal funding streams to which this applies are the JEREMIE and JESSICA Initiatives. JEREMIE provides a mechanism for setting up revolving loan instruments for providing development capital to enterprises while JESSICA provides repayable and recyclable assistance to public-private partnerships for urban renewal and development.

In respect of JEREMIE, as part of Priority 2 of the ERDF programme, support for financing engineering instruments has been identified as a significant area for ERDF spending. As detailed in the priority description, eligible activity will include funding for venture capital schemes operating in the LUPS area, building on the experience of the Structural Funds-supported Scottish Co-investment Scheme of the 2000-06 programming period. The use of JEREMIE as a mechanism for delivering financial engineering instruments will be actively explored with the European Commission and the European Investment Bank.

In respect of JESSICA, the scope for using the Initiative to support the sustainable urban development aims of Priority 3 will be actively explored as well.

7   IMPLEMENTING PROVISIONS

7.1   Roles and Responsibilities

The following section sets out the roles and responsibilities for the management of the programme. It covers the identity and duties of the following:

- Managing Authority
- Certifying Authority
- Audit Authority
- Compliance Body
- Intermediate Delivery Bodies

<u>Managing Authority</u>

The Managing Authority of the Programme will be the Scottish Executive through the Enterprise & Lifelong Learning Department:

> Scottish Executive Enterprise & Lifelong Learning Department
> European Structural Funds Division
> Meridian Court
> 5 Cadogan Street
> Glasgow G2 6AT
> United Kingdom

In accordance with Article 60 of Regulation 1083/2006, the tasks of the Managing Authority will consist of the following:

- ensuring that operations are selected for funding in accordance with the criteria set out in the Operational Programme and with relevant Community and national rules;

- verifying that co-financed activities have been delivered and permissible expenditure defrayed in accordance with Community and national rules and that beneficiaries and other bodies maintain appropriate arrangements for accounting and maintenance of documents required for verification and audit;

- establishing and maintaining an effective monitoring system – including financial management, verification, audit and evaluation – and that beneficiaries can fulfil their monitoring obligations as well;

- providing the Certifying Authority with all appropriate information to allow it fulfil its obligations as set out below;

- guiding the work of the Monitoring Committee and providing it with appropriate monitoring information;

- ensuring the evaluations set out in Chapter 9 are made;

- overseeing the annual and final reports on implementation;

- ensuring compliance with the required publicity actions; and

- providing the Commission with information to allow it to appraise major projects as required.

Lastly, the Managing Authority will pay the beneficiaries on receipt of valid claims.

Intermediate Administration Body

In accordance with Article 59, the Scottish Executive has decided to delegate selected Managing Authority tasks to an Intermediate Administration Body (IAB). A single body will be responsible for managing and administering selected Managing Authority tasks in the ERDF Programme on behalf of the Scottish Executive for the whole of the Lowlands & Uplands Scotland region. The principal tasks will be:

- publicity: to implement the relevant publicity requirements of the EU regulations;

- project applications: to facilitate the process of publicising, overseeing the application process, registering new organisations and providing advice and support to prospective applicants and communicating decisions, key guidance and programme/policy changes to partners;

- project selection: to undertake technical checks on applications and facilitate the assessment of challenge-fund applications and recommendations of awards to the Programme Monitoring Committee;

- project monitoring: to carry out monitoring visits on all projects in fulfilment of Programme obligations;

- reporting: to monitor progress towards Programme financial targets and contribute to Programme requirements; and

- secretariat to the Programme Monitoring Committee.

The IAB will be accountable to the Managing Authority and act in accordance with the formal contractual agreement. ESEP Ltd has been awarded the contract to carry out these delegated functions will be reviewed by 31 December 2010:

> ESEP Ltd
> Suite 3
> Forth House
> Burnside Business Court
> North Road
> INVERKEITHING
> Fife, KY11 1NZ

Certifying Authority

The Certifying Authority of the Programme will be the Scottish Executive through the Enterprise & Lifelong Learning Department. Certification will be undertaken by a unit within the Department that is functionally independent from the Managing Authority. Its tasks, as set out in Article 61, will be to:

- draw up and submit certified statements of expenditure and payment applications to the Commission;

- certify that the statements of expenditure are accurate and verifiable, comply with relevant Community and national rules and have been incurred in accordance with the relevant Operational Programme criteria;

- ensure for the purposes of certification that the Managing Authority has provided adequate information on procedures and verifications carried out in relation to the expenditure detailed in the statements of expenditure;

- take account of all relevant audits for the purposes of certification; and

- maintain adequate records of expenditure declared to the Commission and of amounts recoverable or withdrawn following cancellation of a contribution for an operation.

The Executive will also make payments to individual projects and Intermediate Delivery Bodies and ensure all monies incorrectly paid are recovered.

Audit Authority

The Programme Audit Authority will be the Scottish Executive through the Finance & Central Services Department.

> Scottish Executive Finance & Central Services Department
> Audit & Accountancy Services Division
> Victoria Quay
> Edinburgh EH6 6QQ
> United Kingdom

As described in Article 62, the tasks of the Audit Authority will be to:

- ensure that audits are carried out to verify the effective functioning of the management and control system of the programme, including audits on a sample of operations to verify expenditure declared;

- submit to the Commission an audit strategy for the Programme within nine months of the programme's approval as well as an annual control report detailing the audits carried out during the previous year, their result and any shortcomings consequently found in the management and control of the programme;

- submit to the Commission an annual control report setting out audit findings in the previous year (to the period ending 30 June of the year concerned);

- issue an annual opinion on the basis of the controls and audits that have been carried out under the Audit Authority's responsibility as to whether the management and financial control systems function effectively and provide assurances to the Commission with respect to the statements of expenditure;

- where appropriate, produce for the Commission a declaration for partial closure assessing the legality and regularity of the expenditure concerned (where appropriate) and, at the latest by 31 March 2017, a closure declaration covered by the final statement of expenditure, which will be supported by a final control report; and

- ensure that audit work takes account of internationally accepted standards.

Compliance Body

Article 71 requires that an independent body is designated to give an opinion whether the management and control systems are in compliance with the Articles 58-62, based on a description of the systems to be provided to the Commission within twelve months of the programme's approval. The 'Article 71' body for the Programme will be the same as the Audit Authority: the Scottish Executive through the Finance & Central Services Department.

Intermediate Delivery Bodies

Within particular priorities, funding will be earmarked for the delivery of key strategic projects by particular organisations or groups, or Intermediate Delivery Bodies. Structural Funds will be supporting activity that is clearly additional to their existing activities and fully eligible with the scope of the Programme. This would be demonstrated through annual plans setting out planned expenditure, activity to be supported and financial and performance targets. Funding will be expected to support a handful of strategic projects of regional or sub-regional significance, selected using the IDB's internal selection procedures.

For the ERDF Programme, these bodies will be:

- Scottish Enterprise within Priority 1 (Research and Innovation)

- the South of Scotland Alliance within Priority 4 (Rural Development)

Scottish Enterprise will be commissioned to deliver a number of strategic projects of region-wide significance for a part of the ERDF programme. Operating through a network of Local Enterprise Companies and funded by the Scottish Executive, Scottish Enterprise is the chief national agency responsible for economic development in the LUPS region. It is the key agency in delivering Lisbon Agenda objectives in Scotland, particularly in Priority 1. Scottish Enterprise will match-fund Structural Funds for the support of a selection of projects 1 through an annually-reviewed outcome agreement. These activities are likely to include support for pre-commercialisation initiatives, investment in key research centres, programmes to increase links

between sources of research and innovation and enterprises and the development of business RTD networks. Strong consideration will also be given to the opportunity for joint activity within other bodies such as Highlands & Islands Enterprise on Scotland-wide pilot innovative projects through co-ordinated bids on funding with the Highlands & Islands ERDF Programme

The South of Scotland Alliance will be commissioned to implement strategic projects to improve the regional competitiveness of the South of Scotland under Priority 4. The Alliance is a partnership of the Local Authorities and Local Enterprise Companies for Dumfries & Galloway and the Scottish Borders and a number of other partners. For the purposes of Intermediate Delivery Body status, one of the Alliance partners would be identified as the accountable and reporting body for he funding. Their designation as an IDB reflects the sizable development challenges of the areas, its successful track record in making effective use of Structural Funds through the 2000-2006 Objective 2 Programme and its clearly-articulated regional aspirations in the published Competitiveness Strategy, which shows where Structural Funds can have a clearly additional and significant impact. Projects to be funded are likely to include region-wide projects aimed at diversification or renewal of locally-significant sectors and the development of key shared services (such as access to further and higher education).

The financial envelope for the IDBs would be set by Scottish Ministers on an annual basis. Ministers and the Programme Monitoring Committee would be responsible for approval of the outcome agreements setting annual activity within that financial envelope. Outcome agreements would be required to set out the EU value added of the projects and their contributions to Programme and priority goals.

The roles and responsibilities of the IDB would be broadly the same as those as for individual project beneficiaries. There would be a body designated to receive awards and to be responsible for the financial management, reporting and accounting of expenditure (such as the submission of quarterly claims). Financial spend and project performance would be reviewed on a quarterly basis by the Managing Authority and the Intermediate Administration Body. This review would form the basis for a formal annual review of the IDB annual plans by the Managing Authority and the Programme Monitoring Committee. Projects put forward by the IDB would require approval by the PMC. Where financial and project performance targets set out in the operating agreement were significantly and unreasonably under-achieved, the PMC would have the option of re-allocating the IDB funding to the competitive bidding pot of the priority.

In addition, a number of Community Planning Partnerships will operate in Priority 3 of the Programme, as set out in section 6.1 above. Their obligations will be the same as for other project sponsors and will be subject to the same financial and management controls by the IAB and the Managing Authority.

7.2   Financial Flows and Payments

The Certifying Authority will make all payment claims to the European Commission, derived from the declarations of expenditure submitted by beneficiaries. The Managing Authority will maintain systems to identify all Commission receipts as well as all beneficiary payments. Procedures to ensure that all relevant regulations are complied with and appropriate financial controls will be in place.

Financial flows will operate as follows:

1.   Final beneficiaries declare through interim claims expenditure defrayed to the Managing Authority. The financial check obligations set out above are made by the Intermediate Administration Body.

2.   The Managing Authority verifies claim expenditure and ensures that the financial management system contains correct information. The Intermediate Administration Bodies will be responsible for checking claims in the first instance before passing to the Managing Authority.

3.   The Managing Authority certifies and authorises payments to final beneficiaries and carries out any necessary recovery action.

4.   The Certifying Authority submits payment requests to the European Commission at Programme level.

5.   The Commission makes payments to the Managing Authority's dedicated account.

6.   When the Commission requests a refund, the Managing Authority will be responsible for the necessary payments.

Figure 5: Financial flows and payments
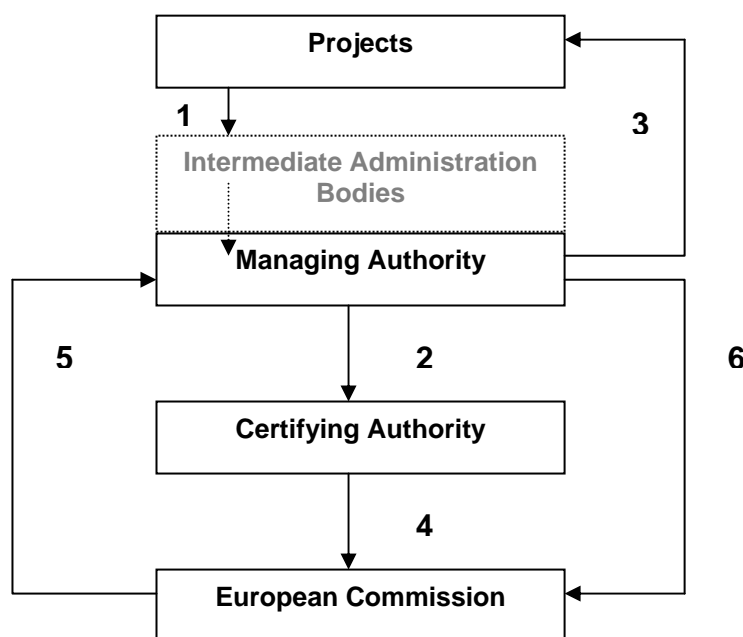
7.3   Partnership and Committee Structure

The Operational Programme will be implemented in partnership with the European Commission and with appropriate authorities and bodies in accordance with national rules and practice. At the consultation stage, the Programme was developed in partnership with key stakeholders such as relevant Government departments, social partners, equality commissions, the voluntary and community sector and others who have a positive contributory role to play. Partnership arrangements will continue as programme activity is prepared, implemented, monitored and evaluated. The Managing Authority will encourage the participation of social partners in Programme activities. It will also encourage participation and access of non-governmental organisations, particularly in projects that will promote social inclusion, gender equality and equal opportunities in the Programme.

At Programme level, partnership will be embodied in the Programme Monitoring Committee, which will be responsible for monitoring implementation of the programme. A single PMC is proposed to oversee both the ERDF and the ESF Programmes for the Lowlands & Uplands Scotland area, ensuring greater strategic overview in specific project decisions but also in the overall use of Structural Funds for the region. The ERDF and ESF Programmes have been drawn up to complement each other strategically so a single strategic oversight body is appropriate.

Reflecting the principle of partnership, the PMC's membership will be drawn from representatives reflecting the key sectoral interests in the programme, including the economic, environmental and social partners, along with the Scottish Executive. As the PMC will bring together both ESF and ERDF interests, membership will be evenly and adequately drawn to ensure full representation of those interests. In addition, the PMC will be selected to provide representation of the key sub-regions in the region and key local Structural Funds partner networks. The European Commission will be represented in an advisory capacity.

The Committee will set its rules of procedures with the Managing Authority within the institutional, legal and financial framework of the Member State. It is expected to meet at least twice a year and will be chaired by a senior Scottish Executive representative. The Intermediate Administration Body will provide the secretariat function for the PMC and its meetings, under the guidance of the Scottish Executive.

In accordance with Article 63, the PMC tasks will be to:

- adjust the Operational Programme, when appropriate;
- approve the indicative annual financing plan for each priority;
- set the criteria for selecting operations eligible for financing under each priority within six months of the Operational Programme approval to review the specific objectives of each priority at periodic intervals;
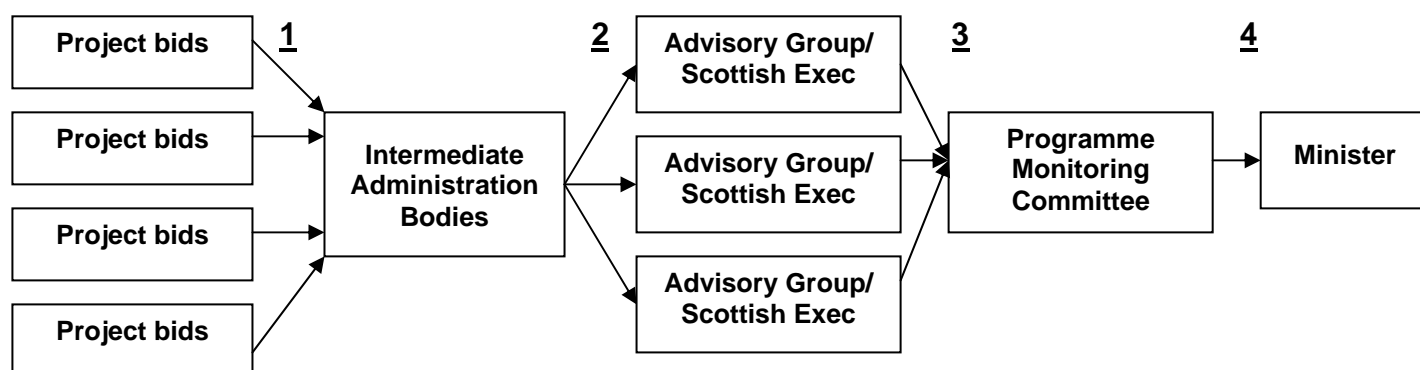
- consider the annual implementation reports to be submitted for the Programme before submission to the Commission as well as relevant parts of the annual control report and monitor progress towards achieving the targets set for the Programme, particularly at the mid-term point;

- approve adjustments to applicant guidance;

- monitor co-ordination of funding with European Regional Development Fund, European Agricultural Fund for Regional Development and the European Fisheries Fund in line with the arrangements set out in Chapter 6;

- make recommendations on the IDB outcome agreements as discussed above;

- consider the recommendations of advisory groups on other projects and set out a list of recommended awards for Scottish Ministers;

- propose adjustments to assistance to the Managing Authority with respect to the implementation of the programme; and

- set up appropriate supporting committees.

7.4   Award Decisions

The Programme is predicated on projects consistent with Programme objectives and contributing to Programme targets being identified for funding either through IDB arrangements or under direct competitive bidding into the priorities. Transparency and peer/partnership appraisal are important aspects of both – these have been traditionally used in Structural Funds appraisal and will continue to do so in the current period. Bids will be invited into each priority on an annual basis (as shown in Figure 6).

- Applications competing for funding will be exposed to technical/eligibility checks by the IAB (**1**).

- This is followed by peer and policy appraisal by the Scottish Executive and advisory groups (**2**). Each priority would be covered by a single advisory group, established by the Managing Authority though where joint appraisals may be required – as in the case of Priority 3 of the ERDF Programme and Priority 1 of the ESF Programme – joint sittings of the Groups and other mechanisms of co-ordination will be used. Membership of the advisory groups will reflect expert knowledge, key regional partners and Scottish Executive policy officials and would be chaired by the Managing Authority.

- Proposals/recommendations are then considered by the Programme Monitoring Committee or any sub-committees delegated to consider the recommendations by the PMC (**3**).

- Formal offers of grant are made on behalf of Scottish Ministers (**4**). Arrangements for deciding on IDB projects are discussed separately above.

Figure 6: Project appraisal and decisions

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┌─────────────┐
│ Project bids│─┐  1
└─────────────┘ │
                │
┌─────────────┐ │
│ Project bids│─┼──▶┌──────────────┐ 2   ┌──────────────┐ 3
└─────────────┘ │   │ Intermediate │────▶│Advisory Group/│
                │   │Administration│     │ Scottish Exec │
┌─────────────┐ │   │   Bodies     │────▶│Advisory Group/│──▶
│ Project bids│─┤   └──────────────┘     │ Scottish Exec │
└─────────────┘ │                        │Advisory Group/│
                │                        │ Scottish Exec │
┌─────────────┐ │
│ Project bids│─┘
└─────────────┘
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[Figure 6 flow diagram: Four "Project bids" boxes (1) feed into "Intermediate Administration Bodies" (2), which feeds into three "Advisory Group/Scottish Exec" boxes (3), which feed into "Programme Monitoring Committee" (4), which feeds into "Minister".]

7.5   Publicity

Article 69 of the General Regulation 1083/2006 stipulates that the Managing Authority is responsible for setting out communication and publicity actions to ensure the full visibility of the funds throughout the programming area. Publicity forms an integral part of the programming strategy and the Managing Authority will ensure that the benefits of the Funds are communicated to the wider public. The Managing Authority will be the chief body with responsibility for making sure publicity obligations are met.

Innovative publicity activities and campaigns using print, broadcast and creative media as appropriate will be employed by the Managing Authority to clearly promote and position the ERDF brand. These activities will be developed proactively and implemented in collaboration with the European Commission in Brussels, the Representation Office Edinburgh and Information relays and networks in the UK as appropriate, which will ensure the visibility and transparency of the Funds at a local, regional and national level.

Potential projects sponsors and final beneficiaries/recipients will be informed of funding opportunities and also the publicity requirements linked to receiving ERDF funding during the programming period. Responsibility for this will lie with the Intermediate Administration Body on behalf of the Managing Authority, as set out above.

Project sponsors will be required to respect the publicity elements of the general and implementing regulations especially with regards to signage – including billboards, plaques and promotional material. These requirements will be set out in detailed guidance to be made available to potential applicants and project sponsors alike.

In conformity with the provisions set out in section 2 of the Implementing Regulation provisions, the Managing Authority will present a communications plan to the Commission no later than four months after the formal adoption of the Programme.

The Communication plan will set out the:

- objectives of the plan and the target groups;

- activities in support of publicity and information including events, seminars and project launches, for potential applicants, partners and the wider public;

- bodies/persons responsible for the implementation of the plan;

- budget for implementing the plan; and

- evaluation frameworks for the plan.

The Managing Authority will report on progress in implementing the plan (including examples of publicity activities) to the Programme Monitoring Committee and also in the annual implementation report. The Communication plan will be easily accessible and will be published on the Managing Authority's website. The use of electronic media – through the Managing Authority's and the IAB's websites – will be the key channel of delivery for disseminating information about the Programme.

Funding for publicity and communications will be provided through the technical assistance budget for the programme.

7.6 Aid Schemes

The Programme will comply with Community law on state aids and the Managing Authority will notify relevant Programme activities under prevailing block exemption regulations.

7.7 Exchange of Computerised Information

The Commission has set up a new computer system to permit the secure exchange of data between the Commission and the Member State. The new system – SFC 2007 – will be used for the exclusive official exchange of all information about the Operational Programme, in accordance with the Commission's Implementing Regulation.

The Commission and the Member State will ensure compliance with relevant EU and national provisions on the protection of personal data. Information exchanged will be covered by professional confidentiality and protected in the same way as set out for similar information in national legislation. Information will not be used for any other purpose than that agreed between the Commission and the Member State, unless express consent is given by the Member State.

The system contains information of common interest to the Commission and the Member State. An agreement has been reached with the Commission on the core and categorisation data to be provided. The categories will not change during the Programme lifetime.

The Scottish Executive has also put in place appropriate computer systems for the collection, storage and security of information and documents relevant to the Programme.

Exchange of data and transactions will be signed electronically in accordance with the relevant EU Directive. The Commission will provide the arrangements for use of electronic signatures.

The Commission will regard a document as having been sent once it has been signed by the Member State in the system. The Commission acknowledges that the date of receipt by the Commission will be the date on which the Member State sends the documents.

In cases of *force majeure*, notably the malfunction of the computer system or the failure of a lasting connection, the Member State may forward information and documents to the Commission in hard copy.

9   CROSS-CUTTING THEMES

In the 2000-06 programming period, cross-cutting themes were defined to act as underpinning policy priorities and be applied across all programmes. These horizontal themes were embedded at all stages of programming, from project design and application, through project selection to implementation and, finally, to project monitoring and evaluation. As the Adding Value, Keeping Value report on lessons of earlier programmes made clear, this commitment to a series of overarching policy objectives running through the programmes should be maintained into the 2007-13 period.

For the 2007-13 programmes, the intention is to build on the work of the horizontal themes in 2000-06 programming and further mainstream them. The General Regulation of the 2007-13 Structural Funds makes clear the need to address the issue in Article 3.1 (and further set out in Article 17):

> *The action taken under the Funds shall incorporate, at national and regional level, the Community's priorities in favour of sustainable development by strengthening growth, competitiveness, employment and social inclusion and by protecting and improving the quality of the environment.*

As the Lowlands & Uplands Scotland ERDF Programme has been developed with a view to supporting sustainable development in Scotland, the horizontal themes to be supported in the 2007-13 period reflect the commitment to achieving that goal. Sustainable development consists of three key elements:

- the sustainable growth of the Scottish economy in a way that does not compromise the environmental resources of future generations;

- the inclusion of as much as Scottish society as possible in the achievement and benefits of that growth, through equal opportunities and social inclusions actions; and

- the conservation of Scotland's environmental assets in pursuing sustainable development.

As the Programme already has as its central aim to contribute towards the sustainable growth of the region's economy by balancing support for underlying sources of national as well as regional competitiveness, the economic growth strand of sustainable development is already recognised. To ensure that the other two elements are mainstreamed effectively in the programme, three horizontal themes have been identified:

- equal opportunities;

- environmental sustainability; and

- social inclusion.

While they will be subject to common processes in the programme, they are discussed in turn below.

8.1 Equal Opportunities

A Structural Funds commitment to equal opportunities is clearly set out in the General Regulation at Article 16:

> *The Member States and the Commission shall ensure that equality between men and women and the integration of the gender perspective is promoted during the various stages of implementation of the Funds. The Member States and the Commission shall take appropriate steps to prevent any discrimination based on sex, racial or ethnic origin, religion or belief, disability, age or sexual orientation during the various stages of implementation of the Funds and, in particular, in the access to them. In particular, accessibility for disabled persons shall be one of the criteria to be observed in defining operations co-financed by the Funds and to be taken into account during the various stages of implementation*

In Scotland, a wide view of equality has traditionally underpinned the design and operation of Structural Funds programmes, encompassing not just the integration of a gender perspective into all stages of programming, but ethnicity, disability, age and sexual orientation perspectives as well. All these perspectives have been applied to the design of the Programme and will permeate its delivery to ensure that no discrimination on any of these bases will take place. The 'mainstreaming' approach has been set out in the Scottish Executive's Equality Strategy – Working Together for Equality:

> *Mainstreaming equality is the systematic integration of an equality perspective into the everyday work of government, involving policy makers across all government departments, as well as equality specialists and external partners.*

The Equality Strategy will be fully integrated into the design of the Scottish Structural Funds programmes. This can be seen in the Strategy's Objectives and how they apply to the programme:

- to make sure that an equality perspective is integrated into the Executive's work and activity in policy and programme development, legislation and spending plans, service design and delivery: in the Structural Funds programme, this has been apparent in the use of specialist workshops and 'equality' proofing in the development of the programme;

- to follow policies and programmes that seek to address the inequalities and exclusion which result from discrimination: the programmes have a range of 'vertical' and 'horizontal' measures designed to tackle discrimination, as outlined below;

- to extend the ownership of and commitment to this strategy to all key public, private and voluntary sector bodies, equality specialists, academics and trade unions: the mainstreaming approach described below is intended to ensure that all Structural Funds partners build the equality perspective into their project design and delivery;

- to promote the inclusion of under-represented groups in policymaking, decision-making and public appointments: representation of the target equality groups are included in the key decision-making and advisory bodies of the Programme;

- to foster greater understanding of and respect for Scotland's different communities: the publicity, good practice and training actions envisaged under the Programme's approach to equal opportunities have been developed from this perspective; and

- to educate and raise awareness about discrimination and the need for it to be challenged: the profiling of equal opportunities as a key horizontal theme in the programmes shows this commitment to awareness-raising.

Scotland has a strong tradition in mainstreaming equal opportunities into Structural Funds programming and past experience has formed the basis for the approach set out for 2007-13 programmes. The experience was extensively examined in the mid-term evaluations of the 2000-06 programmes, which gave special attention to the horizontal themes. In the case of equal opportunities, the common theme in the evaluations was the strong embedding of a mainstreaming approach in the management and administration of Structural Funds, but limits to pushing partners to develop their existing approach to equality further in their projects. Responding to these comments, the programmes developed a common Equal Opportunities Good Practice Guide, Equality in Practice – Making It Work, which picked out the principles and practical examples of mainstreaming equal opportunities into project design and delivery. Similarly, the report of the Mainstreaming Equal Opportunities in the EU Structural Funds Conference held in Glasgow in 2003 has also shaped the approach taken for 2007-13.

The Equal Opportunities Impact Assessment took forward the equal opportunities dimension in programme development, as summarised in an annex. As a result, the aim of the 2007-13 Programmes for equal opportunities is to take forward the work that has been done by earlier programmes. The vision is:

> **to increase the opportunities within the Programme for all groups and to prioritise and adapt support for groups facing particular disadvantages to participation.**

The vision will be delivered through two objectives:

- **to adjust the scope of the Programme to support the particular needs of groups facing barriers to achieving sustainable employment and access to lifelong learning**; and

- **to improve the approach to mainstreaming equal opportunities in Scotland**.

These objectives are part of a twofold approach to equal opportunities. The first objective will be addressed through direct support for projects that explicitly aim to achieve equal opportunities goals. The approach is integrated

across all three priorities. This can be seen in examples of the types of activities in support of equal opportunities eligible under the different Priorities:

- Priority 1
  - Projects should take pro-active measures to ensure that skilled individuals from all equal opportunities have the opportunity to work on supported research and innovation projects.

- Priority 2
  - Support for enterprise start-ups will be monitored to ensure that key target groups are being sufficient represented. Where under-representation is notable, support will be available to projects to address any particular issues relating to publicity and take-up as well as deeper issues relating to entrepreneurship in certain groups.

- Priority 3
  - Where support is given for limited infrastructure developments, they will be required to demonstrate that the needs of disabled people were fully taken into account in building design.

- Priority 4
  - The rural dimension to disadvantage should be fully considered in project design – for example, the problems of peripherality exacerbate the problems faced by some disadvantaged groups in accessing some enterprise support projects.

The second objective of the Programme's vision for equal opportunities will be achieved through a wider mainstreaming of the horizontal theme into Programme processes. This would mean that explicit consideration of the issues would be required at every stage of Structural Funds-supported policy and project design: from the initial development of the project/scheme through application for Structural Funds support to actual project activity and finally, monitoring and evaluation. Structural Funds cannot affect a cultural change alone, but through mainstreaming, help to set up procedures that will inform policy-making and project design more generally.

The instruments for mainstreaming build on existing methods which have been tested and assessed under earlier programmes, not just in Scotland but elsewhere in the UK.

- Administration and management: The equal opportunities perspective outlined here will be applied throughout the different management and administration arrangements of the Programme. The Programme Monitoring Committee will aim to have a balanced representation in line with the equal opportunities vision set out above. Similar representation will be pursued for the roles and responsibilities set out in Chapter 7 above, in line with the equal opportunities policies set out for the Scottish Executive and the Intermediate Administration Body.

- Capacity. The experience of 2000-06 programmes has shown the importance of having equal opportunities champions and expertise in different parts of programme delivery. *Champions* will be designated for the different committees, particularly the Programme Monitoring Committee and advisory groups in the Programme, in many cases drawn from relevant Scottish organisations. However, the Programme's commitment to equal opportunities will not be concentrated in individuals, but be a dimension to all delivery activities. Consequently, short-term *expertise* will be used for training different parts of the delivery system to mainstream equal opportunities on a continuing basis through the Programme lifetime. There is also a need for expert advice to be available to projects in terms of meeting their equal opportunities obligations. This will be provided through the 'delivery body' and core guidance and good practice material.

- Selection: To encourage projects to take full account of equal opportunities, the principle will be embedded in the application and selection system for projects. All projects will be required to demonstrate a commitment to equal opportunities as a core programme criteria at each part in the application form, showing – where relevant – how the issue has been taken fully into account at all stages of project design, implementation and evaluation. A minimum level of commitment needs to be demonstrated for project selection. Where projects can demonstrate that they are exceeding regulatory norms in their approach to equal opportunities, they will be given a higher score.

- Monitoring: To assess the equal opportunities impact of the Programme, relevant indicators have been built into the project monitoring system. The issue will be reviewed annually for the Programme Monitoring Committee and independently assessed as part of thematic evaluation during the course of the Programme.

8.2   Environmental Sustainability

As defined by the World Commission on Environment and Development, sustainable development entails "*development that meets the needs of the present without compromising the ability of future generations to meet their own needs*" (WCED, 1987). Environmental sustainability is the component in a sustainable development approach governing how the environmental resources of a region are used. While usually referring to the treatment of the physical environment, environmental sustainability has wider implications beyond natural resource usage, involving cultural attitudes to environmental protection. Consequently, environmental sustainability has several elements that should be addressed in programming:

- ensuring that economic and social development is fully in line with the conservation of the surrounding environment and its biodiversity;

- making full economic and sustainable use of environmental assets so that conservation and economic development goals reinforce each other rather than work in opposition or require compromise; and

- raising awareness of the importance of environmental sustainability as a fundamental consideration in project /policy-making more widely.

This has been given higher profile in recent years with the EU's commitment to the principle through Gothenburg and in the UK, by the recently-published Stern Report.

Within Scotland, there is a strong tradition of environmental sustainability in domestic policy, both in terms of giving it due policy prominence as an areas in its own right as well as promoting it as a key influence on all policy-making. As the Scottish chapter of the National Strategic Reference Framework detailed, the Structural Funds programmes in Scotland for 2007-13 would reflect both goals by being fully informed by the key environmental sustainability statements of policy, particularly the Green Jobs Strategy, the Scottish Sustainable Development Strategy and the Scottish Biodiversity Strategy. The Green Jobs Strategy was discussed in Section 3.1 above; the other two strategies are discussed below.

The Scottish Sustainable Development Strategy, set out in 2005, shares with the UK the common aspiration:

> *to enable all people throughout the world to satisfy their basic needs and enjoy a better quality of life without compromising the quality of life of future generations*

The strategy has four sets of principles:

- <u>sustainable consumption and production</u>: achieving more with less by reducing the inefficient use of resources, considering the impact of products and materials across their whole lifecycle and encouraging people to take into account the social and environmental consequences of their purchasing choices;

- <u>climate change and energy use</u>: securing a profound change in the way in which energy is generated and used and reducing greenhouse gas emissions.

- <u>natural resource protection and environmental enhancement</u>: protecting natural resources by developing a better understanding of environmental limits and actively improving the quality of the environment; and

- <u>sustainable communities</u>: creating communities that embody the principles of sustainable development locally

These four principles have informed the development of the ERDF Programme. For example, <u>sustainable consumption</u> will be reflected in a commitment to funding and promoting greater 'greening' of enterprises and compelling projects to consider the consequences of their procuring choices. The active support of renewables would take forward the commitment to <u>climate change and energy use</u>. Natural and environment resource protection would be reinforced by supporting projects that give such objectives strong economic development grounding in making full sustainable economic use of

environmental assets. Lastly, <u>sustainable communities</u> are the clear goal of Priority 3, where the aim is to support urban regeneration within the framework of sustainable economic development.

The Scottish biodiversity strategy – 'It's in Your Hands' – was published in 2004. While Structural Funds are limited in their pro-active contributions to direct conservation work, the principles of the strategy underpin the Programme with respect to proofing all funded project activity so that there is a neutral, if not positive impact of Structural Funds support on biodiversity within the region. All projects will need to take account of the strategy in making applications and the issue has been given explicit consideration in the Strategic Environmental Assessment of the Programme (as set out in the annex).

There is also a strong tradition of environmental sustainability in Scottish Structural Funds programming. It has been a key horizontal theme in previous programmes, particularly in the 2000-06 period, where the approach to sustainable development was taken forward substantially. Structural Funds programming has developed a 'missionary' approach to environmental sustainability, viewing its embedding in wider policy-making as one of the legacy aims of the Programmes. To a large extent, this has been achieved through the development of an archive of good practice projects and processes, which have informed the development of the approach taken in the 2007-13 programme. For example:

- The Scottish Natural Heritage good practice guide, Linking Sustainable Development to Regional Development, has been an important source document in programme development.

- The approach was also an important focus in mid-term evaluations in the 2000-06 programming period. The evaluations noted the success in establishing a commitment to environmental sustainability across the different programmes, while acknowledging that there remained significant challenges to ensuring more than lip service at project level. Addressing these continuing challenges has been a UK-wide goal.

- Lastly, the 2007-13 programme has made use of UK research to tackle the issue, particularly Leaving a Legacy, a report of the Environmental Sustainability seminar for Structural Funds Programme practitioners in England.

The Strategic Environmental Assessment has made a number of recommendations that have informed the Programme on this theme (as set out in an annex). As a result, the environmental sustainability vision of the 2007-13 Programmes is as follows:

> **to ensure that Structural Funds programmes promote the sustainable use and conservation of Scottish environmental assets by enhancing the role of environmental sustainability in economic and social development policy-making**

This translates into two distinct objectives governing Programme activities:

- **to strengthen the mutual contributions of environmental sustainability and economic and social development in Structural Funds-supported activities**; and

- **to raise awareness of the role of environmental sustainability in project planning and policy development**.

As with equal opportunities above, the two objectives embody a twofold approach to horizontal themes. The first objective will be addressed through direct support for projects that explicitly aim to achieve environmental sustainability goals. While the scope for this may be more apparent in Priority 4 (rural development) in the ERDF Programme, the approach is integrated across all three priorities. This can be seen in the types of activities in support of environmental sustainability that would be eligible under the different Priorities:

- Priority 1
    - The sustainable commercial use of renewables technologies is supported under this priority with the aim of promoting the development of a thriving new energy sector that would bring together economic development and climate change goals.

- Priority 2
    - A specific objective of the priority is to encourage the 'greening' of enterprises through improved resource efficiency. Eligible activities include environmental and carbon-use audits, more environmentally-sustainable production systems and business processes and plans for energy and resource efficiency.
    - The potential for a cultural change in environmental sustainability is more likely to develop with new rather than existing enterprises, particularly where energy and resource efficiency processes are mainstreamed into their practices from the start. In supporting new firm start-ups, the priority will link enterprise development support – whether advice or financial – with requirements for adoption of baseline environmental processes.

- Priority 3
    - Community regeneration can be taken forward in the context of environmental sustainability through funding of small-scale infrastructure developments for enterprises that comply with sustainable development goals – for example, the application of environmental building standards and the use of derelict/brownfield sites for development.
    - Activities to raise environmental awareness in communities and enterprises can be directly supported through the Programme.
    - Support for small-scale renewables in local energy generation will contribute to the local dimension of the wider Scottish sustainable development agenda.

- <u>Priority 4</u>
  - The economy of rural areas depends more clearly on use of environmental assets. The priority will support key environmentally-based activities such as wildlife/wilderness tourism.
  - Potential new sources of economic activity will be funded, including renewables.
  - Support will be available for improving the environmental sustainability of transport in rural areas through investments in pilot fuels and vehicles projects.

The second objective of the Programme's vision of environmental sustainability will be achieved through a wider mainstreaming of the horizontal theme into Programme processes. Again, paralleling the approach under equal opportunities, this would mean that environmental sustainability issues would be built into policy and project design at each stage. For example, this would include compliance with minimum construction standards and consistency with the Scottish biodiversity strategy. Projects that exceed environmental regulatory standards will be given higher scores in project scoring. More detailed criteria will be developed in advance of the first round of programming.

As noted, the scope of eligible activity has been extended to provide positive support to some of the issues, as recommended by the Strategic Environmental Assessment. These include:

- Support for environmental audits and carbon-footprint approaches for enterprises (Priority 2)

- Support for resource and energy efficiency initiatives by enterprises (Priority 2)

- Support for 'green design' and higher-than-required construction standards for building projects in support of sustainable communities (Priorities 3 and 4)

Monitoring has been informed by the Strategic Environmental Assessment as well. The Programme will measure the following on an on-going basis:

- Number of energy-saving and resource-efficiency projects

- Number of renewable energy projects

In addition, as Chapter 9 sets out, the Programme will conduct a thematic evaluation of the environmental sustainability impact of the Programme at a suitable juncture during the course of programming, which will examine effects on carbon emissions and energy/resource efficiency.

The instruments for mainstreaming are the same as those for equal opportunities with the exception of the Strategic Environmental Assessment. They build on existing methods which have been tested and assessed under earlier programmes, not just in Scotland but elsewhere in the UK. Not only do the 2007-13 Structural Funds Regulations require a strategic environmental

assessment of Operational Programmes, but such assessments are a Scottish legislative requirement for new policy initiatives. For the ERDF Programme, the SEA has provided an environmental profile and baseline as well as an ex-ante commentary on the Programme's impact and handling of environmental sustainability (effectively 'proofing' the documents). The Programme has been developed through iterative feedback with the SEA.

8.3   Social Inclusion

The essential principle of the 'European Social Model' is to reconcile social inclusion, competitiveness and economic performance. Structural Funds can act as a catalyst to ensure a genuine interaction between social policies and economic policies. The Lisbon Strategy centred on growth and employment, was taken up by the European Council in a broader context so that it formed both a social agenda and a durable development strategy. It is that broader context which is reflected in the Scottish Structural Funds programmes.

Social inclusion is about reducing inequalities between the least advantaged communities and the rest of society by closing the opportunity gap and ensuring that support reaches those who need it most. It means actively promoting opportunities to participate, whether in work, in learning or in society more generally. Having this as a cross cutting theme will help ensure that communities are strengthened and regenerated, that young people get the best possible start in life and the opportunity to fulfil their potential, and that older members of these communities are able to contribute fully while also improving their skills, and their future financial security.

An essential part of the commitment to the Lisbon and Nice strategies was to secure greater social inclusion and to make a decisive impact on poverty. The UK's National Action Plan on Social Inclusion describes the current position in the UK and the action that the UK Government will take in the years 2006 to 2008 to tackle poverty and increase social inclusion. This plan reflects an in-depth engagement with a wide range of stakeholders, including people experiencing poverty, the voluntary and community sector, and devolved and local government.

> *Through work people can lift themselves and their children out of poverty by raising their income and expectations. That is why employment is at the heart of our approach to inclusion, while ensuring security and support for those who cannot work.*

Strong links must be made between the Closing the Opportunity Gap approach to social inclusion (as set out in Chapter 3) and Structural Funds policy and implementation in the new programme, so that the Structural Funds can be used to enhance Scotland's social inclusion agenda. Social inclusion cannot be a secondary aim, or a product of the state of the economy. It has a fundamental value in its own right that contributes to the durable development of an 'economic and social model', which combines a social objective and an economic objective forming an integrated strategy where the social policy is designed as an investment in the human capital and is therefore a productive factor.

Against this background, the vision of the 2007 – 2013 Programme for social inclusion is:

> **to ensure that economic growth and tackling exclusion go hand in hand to help people overcome multiple barriers to employment and realise their full potential.**

The vision will be delivered through two objectives:

• to focus on: the most important issues that will make the most difference to people's lives; the most disadvantaged individuals; the issues where progress has been slowest; and the issues where the Executive has the power to make a difference; and

• to improve the way in which services are provided to help people overcome multiple barriers to employment, education or training, and realise their potential.

The first challenge is obviously that of exclusion and unemployment or inactivity. Working to reduce the divide between those who benefit from globalisation and those who are excluded from it is key. The second is to focus on supporting people through the changes that globalisation will bring, develop new skills and make the most of their talents. However, it is also essential to improve access to the services and advice which can enable individuals to engage, and reduce the number of those who feel threatened by a growing risk of poverty. In this way the benefits of a growing economy can be carried over to our social institutions to create new safety measures as economic and social reforms move together.

This approach can be seen in the types of activities in support of social inclusion which are eligible under the different priorities in the programme:-

• Priority 1
  - Requiring additional help for individuals, such as young people, disabled people, ethnic minorities or migrant workers, facing particular barriers to developing research capacity in their enterprises.

• Priority 2
  - Ensuring that all groups can have equitable access to the financial engineering instruments supported under the Programme.

• Priority 3
  - Creating sustainable vibrant outward looking communities out of disadvantaged areas of urban deprivation by connecting the people living there with opportunities in neighbouring accessible areas.

• Priority 4
  - Supporting economic regeneration in rural areas to reduce the exclusion and isolation felt by these communities, and increase their prosperity.

An inclusive labour market supports social inclusion and a well functioning economy. This is a long-term approach, which requires a balance between the objectives of social inclusion and economic objectives. The reality that poverty and exclusion is not decreasing among all groups or communities, despite the efforts so far, points clearly to the fact that actions to close the opportunity gap need to be mainstreamed across all the new Structural Funds programmes and priorities.

9   EVALUATION, MONITORING AND REPORTING

9.1   Evaluation

In accordance with general provisions in Articles 47 and 48 of the General Regulation, the evaluations covered under this Operational Programme will aim to improve the quality, effectiveness and consistency of the assistance provided under the Programme.

Our approach to evaluation activity builds on the lessons learned from the Scottish European Structural Funds Evaluation Strategy of 2000-06 and the refreshed Strategy covering the years 2004-06. Evaluations will be carried out by experts or bodies, internal or external, functionally independent of the Scottish Certifying and Audit authorities and will be financed from Technical Assistance. The following sets out the expected evaluation activity to be covered in the lifetime of the 2007-13 Programme.

- Ex-ante evaluation. The evaluation cycle is required to start with an ex-ante evaluation of the programme, an iterative process ongoing in relation to this Operational Programme. This also includes a Strategic Environmental Assessment of the Programme as well.

- Ongoing strategic evaluation. In applying the lessons from the 2000-06 evaluation activities it is important to recognise the need to review how the programmes are performing at suitable points of the programme. The experiences of the 2000-06 Programme evaluations – the mid-term evaluation (2003) and the mid-term evaluation update (2005) – show the key is to measure programmes when they have been under actual operation for a time period which is not too early to report on results or, conversely, too late to affect any important change of direction to the programme. As such we will set up a Scottish Evaluation Group to make decisions on the optimum times, and key thematic areas of activity, to cover in a Scottish Evaluation Strategy for 2007-13. Such areas are likely to include the horizontal themes (equal opportunities, environmental sustainability and social inclusion) as well as the key thematic areas covered by the programme priorities. This strategy will now be refreshed on a yearly basis and consultation on content for corresponding years ahead will be taken with partners through Programme Monitoring Committees and in line with the European Commission evaluation planning. This revised approach will allow the Programmes to plan evaluation on a more flexible and need-driven basis.

- Ongoing operational evaluation. The delivery arrangements in Scotland have altered from the 2000-06 programme. Projects will now be delivered under two systems:

    - Competitive bidding – applications delivered through the newly-appointed Intermediate Administration Body (IAB).

    - Commissioned approach – a series of strategic projects, planned through a detailed strategy, by the designated Intermediate Delivery Bodies (IDBs).

We will be undertaking a review of the new arrangements in 2010, to take stock of this new operating environment, including specifically the publicity measures achieved by the new structures.

- <u>Ex-post evaluation</u> - it will be the Commission's responsibility to carry out an ex-post evaluation, in line with Article 49 of the General Regulation, to be completed by 31 December 2015.

The evaluations will take appropriate account of the equal opportunities, environmental sustainability and social inclusion objectives of the Programme outlined in Chapter 8.

9.2 Monitoring

Monitoring will be the joint responsibility of the Managing Authority, the Monitoring Committee, the IAB and IDBs, in accordance with Articles 63-66 of the General Regulation. These bodies will be responsible for setting up appropriate monitoring systems, defining indicators and disseminating knowledge of their use, ensuring that projects fully understand their reporting obligations, assuring themselves on the quality and coverage of the indicator data, and providing appropriate reporting on the basis of that data. Data will be stored in the Scottish Executive computer system established for collecting/reporting on Structural Funds by the Managing Authority.

In essence, project partners – including IDBs – will be responsible for reporting on the indicators set out under the priority descriptions in Chapter 4, as appropriate for their project, on a quarterly basis. These reports will be initially checked for consistency by the IAB and the information will be stored and analysed on a regular basis by the Managing Authority. Analysis of the information will feed into reports to the Programme Monitoring Committee – twice-yearly for regular project reporting (including the IDBs) but also on an annual basis for the annual implementation reports discussed below. The data will also be used as part of the thematic evaluations detailed in the previous section.

A quarter-year monitoring regime of projects will ensure the quality and effectiveness of implementation of projects through assessment of progress towards achievement of the indicators defined in the Programme (as discussed below). In drawing up indicators, account has been taken of the indicative methodology and practical guidance in the Commission Working Paper Indicators and Evaluation: A Practical Guide, including the main messages of that paper concerning:

- creating an evolutionary approach from existing indicators;
- concentrating on better focused and less complex set of activity measuring;
- making clear links to priorities within EC policies; and
- adopting a broader approach to the concept of core EU indicators.

Management information systems will provide core data on a regular, timely and consistent basis throughout the programming period, enabling the Managing Authority and Programme Monitoring Committee to monitor programme performance and results in line with their responsibilities. The management information provided will enable analysis of performance in terms of geographical area and participant characteristics and so provide essential information to key stakeholders. Where appropriate, statistics will be broken down by gender.

A set of core management information requirements for ESF and co-financed activity will:

• enable progress towards the achievement of financial, output and result indicators to be assessed at priority level;

• provide performance measures for the Managing Authority and the PMC;

• feed into preparation of the reporting requirements set out in the next section;

• allow transfer of data to the Commission as required in the Commission's Implementing Regulation, particularly Annex XXIII; and

• contribute to the wider evaluation of the Programme – where necessary, the core information requirement will be supplemented by other information such as follow-up surveys as set out in the section above.

9.3   Reporting

Reporting will also be the joint responsibility of the Managing Authority, the Monitoring Committee, the partners, the IABs and the IDBs, in accordance with Article 67 of the General Regulation.

As noted above, partners will be responsible for submitting the required robust, verifiable and up-to-date information under the different indicators on a regular basis, as set out by the Managing Authority. Reports on programme performance against key priority indicators will be made to the Programme Monitoring Committee on a twice-yearly basis by the Managing Authority.

An <u>annual implementation report</u> (AIR) for the Programme shall be provided for the first time in 2008 and by 30 June each year and thereafter for the length of the Programme period. The first report will be due by 30 June 2008. The report will be examined and approved by the Monitoring Committee before being sent to the Commission by the Managing Authority. The Managing Authority is setting a voluntary target date of prior submission to the European Commission of 30 April each year. The report will be prepared by the Managing Authority and the IAB jointly.

The Annual Report will include the information set out in detail under Article 67(2) of the General Regulation, which includes:

• progress made in implementing the programme;

- an update on the financial implementation of the programme;

- an indicative breakdown of the allocation of the Funds by category;

- steps taken by the Managing Authority, partners and Monitoring Committee to ensure the quality and effectiveness of implementation;

- measures taken to provide information on and publicise the programme;

- information about significant problems in terms of compliance with community law;

- progress and financing of major projects;

- use of assistance made following financial corrections, in accordance with Article 98(2); and

- cases of modification, in accordance with Article 57.

The Commission will inform the Programme of its opinion on the admissibility of report within ten days of days of its receipt and offer its opinion on the content within two months. Following consideration by the Commission, the Managing Authority and partners, the Monitoring Committee will adopt the AIR and agreed adjustments to the Operational Programme.

An <u>annual review</u> between the Commission, the Managing Authority and partners will also take place, in accordance with Article 68. The review will examine progress made in the proper functioning of the operational programme, the principal results achieved, the financial implementation and other factors, with a view to improved delivery.

A <u>final report</u> on the implementation of the Operation Programme will also be provided, as outlined by Article 67, by 31 March 2017. The same content and procedure (submission to the Commission by the Managing Authority after examination and approval by the Programme Monitoring Committee) for annual reports apply to the final report.

9.4   Indicators and baselines

Article 37 of the General Regulation states that Programme documents should contain "information on the priority axes and their specific targets… the indicators shall make it possible to measure the progress in relation to the baseline situation and the achievement of the targets in the priority axis". Specific indicators, targets and their rationales have been included in the 'Indicators and targets' sections of the priority descriptions in Chapter 4.

In view of the proportionality principle and the requirement to limit the number of indicators to make their monitoring effective, there are not quantified indicators for every target group/activity. Moreover, some data will be collected through individual participants data collection – in line with the partner responsibilities set out above – and some through specific follow-up survey/evaluation work.

The Managing Authority will set out national definitions for each of the indicators as part of guidance to applicants on monitoring. Baselines for each priority are set out here. They have been selected with a view to capturing the key goals of each priority and will be assessed in the second half of the Programme – in some cases, owing to the fact that the areas targeted under Priorities 3 and 4 may alter during the Programme's lifetime, the figures are presented as the most acute currently identified, although specific analyses on the targeted areas will be conducted in the second half of the Programme. It should be noted that attribution of changes in these regional indicators to Programme activity may be difficult to make because of the small size of Programme resources relative to the Lowland & Uplands Scotland economy.

- For <u>Priority 1</u>: business expenditure in RTD as share of GDP (the Programme should contribute to the share increasing);

- For <u>Priority 2</u>: several baselines, including the corporate stock relative to the population, the gross value added of the region relative to the UK and the share of business activity transacted through e-business (the Programme should contribute to the number and shares increasing);

- For <u>Priority 3</u>: changes in the SIMD status of the targeted areas of the priority, as reflected in the number of 15% most deprived data-zones as a share of all the data-zones in the area (the Programme should contribute to these figures decreasing) – these shares vary with the highest currently at 38%, but any change in status for the individual targeted areas will be measured as part of a specially-commissioned evaluation in the second half of the programming period, to allow for the impacts of the Programme to become more manifest; and

- For <u>Priority 4</u>: changes in the gross value added of the targeted areas relative to the UK as a whole (the Programme should contribute to these shares increasing) – again, this cannot be calculated fully at this point as the targeted areas may change through the Programme, though the lowest is currently 68%, but changes for the specific targeted areas finally identified will be measured as part of a specially-commissioned evaluation in the second half of the programming period.

In addition, there will be a set of Programme-wide indicators based on the priority indicators described in Chapter 4. Data will be collected by compiling the priority indicators for reporting to the Programme Monitoring Committee and the annual implementation reports. The indicators are:

- Number of gross jobs created
- Number of gross jobs safeguarded

Baseline indicator	Baseline source	Baseline figure
Priority 1		
Business expenditure in RTD as % of GDP	ONS (2003)	0.58%
Priority 2		
Corporate stock per 10,000 population	NOMIS (2004)	236.6
Gross value added in the region relative to UK	ONS (2004)	71%
Share of business activity transacted through e-business	DTI (2004)	20%
Priority 3		
Changes in the SIMD status for the 15% most deprived data-zones in the targeted areas	Scottish Executive (2006)	Highest at 38%
Priority 4		
Gross value added in targeted areas relative to the UK average	ONS (2004)	Lowest at 68%

ANNEX A: GLOSSARY OF ACRONYMS

CPP – Community Planning Partnership

CRF – Community Regeneration Fund

EAFRD – European Agricultural Fund for Rural Development

EFF – European Fisheries Fund

ERDF – European Regional Development Fund

ESF – European Social Fund

EU-15 – 15 Member States of the pre-May 2004 European Union

EU-25 – 25 Member States of the current European Union

FEDS – Framework for Economic Development in Scotland

GROS – General Register Office for Scotland

GEM – Global Entrepreneurship Monitor

GDP – gross domestic product

GVA – gross value added

IB – Incapacity Benefit

ICT – information and communication technologies

ISDN – Integrated Services Digital Network

IAB – Intermediate Administration Body

IDB – Intermediate Delivery Body

JEREMIE – Joint European Resources for Micro-Enterprises

JESSICA – Joint European Resources for Sustainable Investment in City Areas

JSA – Jobseekers Allowance

LUPS – Lowlands & Uplands Scotland

NRP – National Reform Programme

ND – New Deal

NUTS – Nomenclature of Territorial Units for Statistics

ODPM – Office of the Deputy Prime Minister

ONS – Office of National Statistics

PMC – Programme Monitoring Committee

RTD – research and technological development

SIMD – Scottish Index of Multiple Deprivation

SRDP – Scottish Rural Development Programme

SDA – Severe Disablement Allowance

SME – small and medium-sized enterprise

SEA – Strategic Environmental Assessment

VAT – Value Added Tax

ANNEX B: REFERENCES

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ANNEX C: PROGRAMME DRAFTING

Introduction

Overall drafting on the 2007-13 Programmes has been overseen by the European Structural Funds Division (ESFD) within the Scottish Executive. Specific drafting and research has been undertaken as follows:

- background paper for socio-economic analysis: Training and Employment Research Unit in the University of Glasgow;

- background paper on indicators and targets for the Programme: DTZ;

- ex-ante evaluation of the Programme: Hall Aitken Associates;

- Equal Opportunities Strategic Assessment, led by the ESFD; and

- Strategic Environmental Assessment: RSK Environment Ltd with Ecodyn.

Throughout the development of the 2007-13 Programmes, there has been regular and intensive engagement with external partners, as detailed in the sections below. This has taken place against a background of difficult decisions having to be made because of the sharp reductions in the Structural Funds coming to Scotland.

Programme drafting, engagement and consultation has gone through several stages:

- initial engagement on proposals;

- the development of the National Strategic Reference Framework document; and

- the public consultation on the draft Scottish programmes.

Initial engagement

Following the EU Budget agreement in December 2005, the Scottish Executive initiated active discussion on programme development through a series of stakeholder events held in December 2005 and January 2006 throughout Scotland (Dunfermline, Glasgow, Inverness and Melrose). At these meetings, the Executive set out initial views on the programmes and priorities for discussion. The meetings were intended by approximately 200 representatives of a range of partner organisations, including Local Authorities, the Enterprise Networks, further and higher education institutions, the voluntary sector, environmental bodies and other organisations.

Following these events, discussions on future programming continued through the Scottish European Structural Funds Forum. Chaired by the Scottish Deputy Minister for Enterprise & Lifelong Learning, the Forum brings together senior representatives from the main Structural Funds partner organisations. Programme development was discussed at meetings on 30 January, 2 October and 12 February 2007.

Two important studies were commissioned during this initial phase. First, Hall Aitken Associates were commissioned to do a study of the new delivery options for the Structural Funds programmes in Scotland, making use of comparative case studies from other parts of the EU; the recommendations of Making Every Euro Count are discussed in section 3.2 of this report. Second, a study group of ESFD and Programme Management Executive representatives produced a report on how to preserve and enhance value added activities supported by the Structural Funds; the Adding Value, Keeping Value report is discussed in 3.2 as well.

National Strategic Reference Framework

The National Strategic Reference Framework (NSRF) was produced under the overall co-ordination of the UK Department of Trade and Industry. A Scottish chapter was prepared for the NSRF by the ESFD, taking into account partner views on initial programme proposals as set out in the stakeholder events and the Structural Funds Forum. The DTI held a consultation on the NSRF, which ended on 22 May, with some 45 responses coming from Scottish partners. Taking account of these views, the ESFD provided the Scottish Executive response for the UK Government's Response to the consultation, which was published in October. Partner views expressed in the NSRF consultation were also taken into account in preparing the draft Scottish programmes for consultation.

Public consultation on draft Programmes

A full public consultation was held on the four Structural Funds programmes-the ERDF and ESF Programmes under the Convergence Objective in the Highlands & Islands, and the ERDF and ESF Programmes under the Competitiveness Objective in Lowlands & Uplands Scotland. It began on 24 October and ended on 8 January.

103 responses were received on the consultation document for the Lowlands & Uplands Scotland (LUPS) area and 21 for the Highlands & Islands (H&I) consultation document. The main category of respondents for the LUPS programmes were region-wide organisations (22 responses). In terms of locality, a significant number of respondents were based in the City of Glasgow (16 responses) and a further 8 responses in the City of Edinburgh. In regional terms, the West of Scotland provided 35 responses, the East of Scotland, 28, and a significant number came from the South of Scotland, particularly Dumfries & Galloway (13 responses). At least one response was received from each Local Authority area, with the exception of Inverclyde, as the following table outlines (the table does not include responses that were region-wide).

Aberdeen City	3
Aberdeenshire	2
Angus	1
Argyll and Bute	2
Clackmannanshire	2
Dumfries & Galloway	13
Dundee City	2
East Ayrshire	1
East Dunbartonshire	1
East Lothian	1
East Renfrewshire	1
City of Edinburgh	8
Eilean Siar (Western Isles)	3
Falkirk	1
Fife	2
Glasgow City	16
Highland	2
Inverclyde	0
Midlothian	2
Moray	2
North Ayrshire	2
North Lanarkshire	3
Orkney	1
Perth & Kinross	1
Renfrewshire	3
Scottish Borders	5
Shetland	1
South Ayrshire	1
South Lanarkshire	5
Stirling	1
West Dunbartonshire	1
West Lothian	2

In the Highlands & Islands, there were 21 responses in total. The geographical spread was relatively even, with some areas providing co-ordinated, single responses (eg. Orkney). Responses came from over Local Authority area within the region.

By sector, Local Authorities were the largest group responding to the LUPS consultation (33 responses). A large number of responses also came from the Higher and Further Education sector (26 responses), the voluntary sector (18 answers) and a number of sub-regional umbrella organisations, including Community Planning Partnerships (CPPs) and other local partnerships (16 responses), as well as Scottish Executive agencies and Government bodies (12 responses). Responses were also received from individuals and business organisations.

Local authorities	33
Scottish Executive Agencies, NDPBs, Government bodies	12
Sub-regional umbrella organisations, CPPs, local representatives	16
Professional bodies, Trade Unions, industrial organisations	0
Academic groups	0
Political parties, MPs, MSPs, MEPs	5
Education & skills organisations, Higher Education, Further Education	26
Third sector/voluntary sector	18
Individuals	4
Business organisations	4
NGOs	6

In addition, a series of specific workshops involving external partners were run to focus on specific priorities and themes in November and December. In Lowlands & Uplands Scotland, workshops were held on each priority in the ERDF and ESF programmes, typically involving 15 partners drawn from a wide range of organisations representing Local Authorities, the Enterprise Networks, the voluntary sector, higher and further education, Government bodies and other organisations. The workshops enabled more intensive discussion on the content and delivery of each priority. Workshops were also held on the two horizontal themes – equal opportunities and environmental sustainability – and there were a series of similar workshops involving the Programme Review Group in the Highlands & Islands.

At the same time, there was a parallel consultation the Environmental Reports prepared by external consultants as part of the Strategic Environmental Assessments of the two ERDF programmes. The documents are also available through the website and the end of the consultation was 29 January. The SEA is summarised in another Annex.

Executive summary of partner and Executive responses to the Lowlands & Uplands Scotland consultation

The consultation on the Lowlands and Uplands 2007-13 Operational Programmes was launched on 24 October 2006 and was completed on 8 January 2007. The consultation covered the two programmes for the region under the new Competitiveness Objective of the 2007-13 Structural Funds period: one ERDF Programme and one ESF Programme. The consultation was held in parallel with the consultation of the Operational Programmes for the Highlands and Islands area under the Convergence Objective.

In addition to the written submissions for the consultation, there were two other parallel forms of engagement with partners as part of the consultation, principally through a series of workshops held with partners with the Programme Review Group. A separate consultation has taken place on the Strategic Environmental Assessment of the ERDF Programme and is published separately.

Overall, there was a strong response to the consultation, reflecting the historical active engagement of Scottish partners in the development of Structural Funds programmes. Written responses were submitted by 103 respondents altogether from across the region, reflecting nearly all geographical parts of the region and all stakeholder sectors.

<u>Socio-Economic Analysis</u>

Partners were largely positive about the socio-economic analyses underpinning the Operational Programmes. A number of suggestions were made for their improvement, including more sub-regional analysis, sensitivity to local economic characteristics and a range of thematic issues such as the role migrant labour and the impact of demographic changes. These will be added to the revised Operational Programmes, strengthening the analyses. In addition, following the completion of the SEA, environmental analyses of the region will be included as well.

<u>Priority Content</u>

On the appropriateness, consistency and coherence of the <u>ERDF</u> priorities, respondents were largely positive but there were numerous comments on ways in which the priorities could be refined. Under Priority 1, several respondents asked for targeting in favour of the areas of need within the region while others argued that the support for research and innovation should be defined more widely. Under Priorities 2 and 3, concerns were raised about whether specific areas would be covered under the 'urban' and 'rural' definitions under each priority. Views on allocations were similarly mixed but with little consensus on an alternative funding split.

In responding, the Executive will make several changes to the priorities. To give greater focus to the region-wide support in the Programme, Priority 1 will now be split: the new Priority 1 will continue to focus on research and innovation (though with a wider view of the processes) while Priority 2 will concentrate on access to finance, entrepreneurship and resource/energy efficiency. No spatial targeting will be introduced for this priority. The new Priorities 3 (urban regeneration) and 4 (rural development) will remain, but overall there has been a re-balancing of funding towards the region-wide priorities (1 and 2).

With regards to <u>ESF</u> priorities, again, respondents were satisfied that they broadly addressed the region's challenges and demonstrated concentration and coherence. However, a significant number of respondents asked whether Priority 3 (lifelong learning) could be subsumed within Priorities 1 and 2 (although there was strong counter-arguments put forward). There were mixed views on spatial targeting, some wanted it relaxed for Priority 1, other extended to the other priorities. There were also a number of concrete suggestions of eligible groups and activities that should feature in the priority descriptions.

The Executive welcomes the broad approval of the priority structure and the strategic focus. We believe that the case for a separate lifelong learning remains strong, but will adjust the allocations somewhat to give more funding to Priorities 1 and 2. The suggestions on revising eligible groups and activities will be examined seriously.

Comments were also made about the Programmes' <u>fit with domestic and other EU policies</u>. Respondents felt that more account should be taken of regional/local strategies as well as a number of major national strategies (particularly for tourism and the environment). In terms of parallel EU funding streams, more needed to be done to make Structural Funds complement the Scottish Rural Development Programme, the European Fisheries Fund, the new EU research funding programmes and other EU initiatives. The Executive accepted that strategic fit was paramount for the new Programmes – at regional and local as well as national level - and would provide more detail on how complementarity with domestic and EU policies can be achieved in the final Operational Programmes.

<u>Horizontal Themes</u>

Respondents welcomed the cross-cutting themes of environmental sustainability and equal opportunities and a number of concrete suggestions were made about putting the commitment to these themes into operational practice. With respect to environmental sustainability, the recommendations are part of the Strategic Environmental Assessment consultation and the Executive will set out final views on how to build on the Scottish legacy in these themes as part of the consultation to that response. For equal opportunities, we have conducted an equal opportunities assessment of the Programmes involving stakeholders. Their recommendations will also inform the final shape of the Programme documents. A third cross-cutting theme – social inclusion – has been added for all programmes.

<u>Delivery</u>

On the delivery of the Programmes, respondents believed that the current system of competitive bidding was a strong foundation for the future – it should be 'fine-tuned' not 'overhauled'. As a result, there was some wariness about the proposed use of Intermediate Delivery Bodies, particularly Scottish Enterprise, and respondents asked for greater control and monitoring of the bodies' activities. Several suggestions were made for improving the challenge-fund approach, although several partners did not feel that partnership and minimum project threshold requirements should be introduced. The current structure of peer group appraisal and representative committees should be kept but with the creation of a single Programme Monitoring Committee for the two Programmes. A number of specific recommendations were also made regarding project appraisal and selection.

The Executive fully agrees with the need to preserve the key features of the current system while adopting it to an environment of reduced funding. Peer group appraisal should be maintained. Several of the specific suggestions on

project appraisal are welcomed as is the suggestion of a single PMC for the region. However, while the Executive agrees that partnership should be encouraged and not required in project bids, it believes that a modest minimum project threshold across all priorities in the two Programmes will encourage more strategic, legacy projects and reduce the administrative burdens on partners.

With respect to Intermediate Delivery Bodies, the Executive will limit their use to Scottish Enterprise in the new Priority 1 and South of Scotland partners in the new Priority 4 and will ensure that their activities are closely monitored for performance. Projects put forward by both IDBs will need to secure PMC approval.

Stakeholders were also asked about the role of Community Planning Partnerships. Respondents felt that CPPs could make a positive contribution to the new Programmes, but there were numerous comments on how this could be achieved given the varying capacity of the bodies across the region. The Executive intends to fund a selection of CPPs for a pilot period of two years, but this will be limited to a pot of funding within ESF Priority 1 and the new ERDF Priority 3.

Targeting

The issue of geographical targeting of funding generated a considerable number of comments. Overall, partners acknowledged the value of some targeting given the reduction in funds, but there was little consensus over how it should be applied. In particular, there were concerns about the designation and distinction of 'urban' and 'rural' areas in the ERDF urban regeneration and rural development priorities. Some respondents argued that targeting should be more widely applied across the Programmes with resources directed towards areas of need within the region.

In reflecting on the responses, the Executive believes that spatial targeting should only be applied in ESF Priority 1 and the new ERDF Priorities 3 (urban regeneration) and 4 (rural development). For ESF Priority 1 and the new ERDF Priority 3, a limited list of Local Authority areas would be defined on the basis of areas set out in existing relevant Scottish strategies and the most deprived areas identified in the Scottish Index of Multiple Deprivation. For the new ERDF Priority 4, a limited number of Local Authority areas would be defined using the six-fold urban-rural classification, targeting those Local Authorities with a significant share of their population that are in areas with 'remote rural' or 'accessible rural' areas. Both lists would be updated annually to take account of changes in the eligibility criteria.

In addition, concerns were expressed at the proposal of ring-fencing funding for South of Scotland partners and the justification set out for the proposal. We remain convinced of the value of ring-fencing funding to support a limited number of large, strategic projects for this sub-region. This not only recognises the significant development challenges of the area but also the successful track record in making effective use of Structural Funds in the past

and the area's clearly-articulated Competitiveness Strategy, which shows where Structural Funds can have an additional and significant impact.

ANNEX D: SUMMARY OF EX-ANTE REPORT

Introduction

This report summarises the findings from the ex-ante evaluation of the 2007-13 ERDF Operational Programme for Lowlands and Uplands Scotland, to be submitted with the final version. The structure follows the outline of key components as set out in the Commission guidance[1].

The full report contains the detailed findings and reflect the changes and improvements to the programme which were made through the evaluation process.

Evaluation objectives

Council Regulation (EC) 1083/2006 requires an ex-ante evaluation for each Operational Programme. According to Commission guidance the main concerns are to assess:

- relevance – of the strategy to the needs identified;

- effectiveness – whether the objectives of the programme are likely to be achieved; and

- utility – judging the likely impacts against wider social, environmental and economic needs.

More specific evaluation questions for an ex-ante evaluation concern:

- internal and external coherence; and

- the suitability of implementation systems.

Our approach

Ex-ante evaluation is as much about the *process* of developing the Operational Programme as it is about the final report on the findings. The iterative and interactive nature of the process requires a close working relationship between evaluators and programme developers. Guided by the concern to maximise Community added value, the Hall Aitken ex-ante evaluation team worked closely with the Scottish Executive's Structural Funds Division to take the process forward. This involved:

- the Scottish Executive briefing the team of evaluators and providing documents and information necessary to carry out the work;

- the evaluators gathering and analysing data as it became available and providing their assessment in the form of comments throughout;

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[1] European Commission *Indicative Guidelines on Evaluation Methods: Ex-ante Evaluation*, 2006

- the evaluators attending development and consultation workshops arranged by the Executive;
- the Scottish Executive responding to and implementing the evaluators' comments and recommendations; and
- both teams meeting regularly to discuss progress and develop next steps.

Programme priorities

The strategy of the 2007-13 Operational Programme for the European Regional Development Fund has four priorities, addressing different aspects of competitive under-performance in the Scottish economy. They are outlined in Figure 1 below. A fifth priority – technical assistance – provides funding support for managing and administering the programme.

Figure 1: LUPS ERDF priorities 2007-13

Priority	Aim
Priority 1 – Research and Innovation	To improve the competitiveness of the Lowlands & Uplands Scotland enterprise base through a fuller use of its RTD base
Priority 2 – Enterprise Growth	To improve enterprise formation and growth rates by enhancing the enterprise support environment, particularly with regards to access to finance, entrepreneurship and resource efficiency
Priority 3 – Urban Regeneration	To increase the contributions of the most disadvantaged urban communities to Lisbon goals by supporting their regeneration
Priority 4 – Rural Development	To maximise the contribution of rural areas to achieving Lisbon goals with a view to developing sustainable economic growth

Relevance to the Scottish economy

The starting point for the Operational Programme was an analysis of the Scottish socio-economic background and – resulting from it – a number of key issues which ERDF intervention could address. This chapter summarises our assessment of the conclusions drawn from the socio-economic analysis and how appropriate the chosen priorities are for addressing economic development issues.

Key challenges

The table below sets out the regional strengths, weaknesses, opportunities and threats the socio-economic analysis identified for Scotland.

Figure 2: SWOT analysis summarised from ERDF Operational Programme

Strengths	Relatively strong economic performance in recent years, characterised by low unemployment rates (although this conceals some significant weaknesses) Strong research base – HE and FE protecting more intellectual property than elsewhere in UK Infrastructure enjoyed strong investment in past decade (with Structural Funds support) Sectoral strengths in sectors with strong links between enterprise base and research & innovation (including traditional and renewable energies, life sciences)	Declining productivity (economic growth and GVA) compared to UK averages Low firm formation and entrepreneurship rates Relatively low RTD expenditure and innovation rates – enterprise sectors not making full use of region's research capabilities Substantial regional variations in economic growth and employment performance Significant concentrations of deprivation in some urban communities Part-time and under-employment and low earnings levels in rural areas affect overall regional economic development Distinctive problems for enterprises in rural areas include access to key markets, skills sources and research and innovation	**Weaknesses**

Opportunities	Business start-up and survival rates could be improved by providing appropriate support to would-be entrepreneurs Relative e-business performance lagging behind EU and US Improved resource efficiency could improve cost effectiveness and contribute to climate change goals Strong university research sector providing good opportunities for commercialisation and spin-outs in key sectors Scope for developing technology sectors, including digital media, life sciences and renewable technologies Area contains diversity of potential growth areas – urban and rural	Weakening of enterprise base through weaknesses in entrepreneurship and new firm foundation Vicious cycles of deprivation through continuing decline in worst-off urban areas Reduced capacity to reverse economic decline in rural areas through out-migration of young people Infrastructure deficiencies in rural areas leading to long-term population decline, skills shortages and problems accessing key sources of industrial research and innovation Over-dependence on primary and traditional economic activities in many rural areas	**Threats**

Assessing relevance

The evaluation team provided guidance, commentary and input to the socio-economic analysis from the very early stages. This process helped the analysis to:

• provide a clearer focus on some of the key issues where ERDF resources could add value to existing activity;

• set out clearer evidence of need to underpin any interventions; and

• comment on previous experience through Structural Funds and other interventions.

Taking into account the objectives of the EU cohesion and employment policy, the socio-economic analysis identified several areas where the Scottish economy lagged behind the UK and other EU economies. The key areas for potential intervention that the analysis identified were around:

• developing research and innovation to overcome the limited investment in this key aspect of sustainable economic growth;

- promoting greater business start-ups to address low rates of entrepreneurship;

- addressing spatial imbalances in economic activity that lead to concentrations of disadvantage in urban areas; and

- helping rural economies to develop and diversify to become more competitive.

These issues all relate to key aspects of the Lisbon agenda, through promoting greater knowledge based competitiveness and addressing the disadvantage that holds it back.

The priorities identified to address these key weaknesses have been developed to make sure that while they support and link with existing domestic policies and programmes, they clearly add value by filling gaps in existing provision. The priorities are relevant to addressing the needs identified through the socio-economic analysis.

Evaluating the rationale and consistency of the strategy

The Structural Funds Regulations emphasise that ERDF-funded interventions help 'to anticipate and promote economic change in industrial, urban and rural areas by strengthening their competitiveness and attractiveness, taking into account existing economic, social and territorial disparities'[2]. This section gives an overview of the strategy within the ERDF Operational Programme for the LUPS region and summarises our assessment of how appropriate this strategy is.

Ex-ante evaluators' assessment

The overall vision for the LUPS ERDF programme is to promote sustainable regional economic growth, while at the same time reducing the disparities in growth that affect different parts of the region. This vision clearly sits comfortably within the Lisbon agenda of improving regional competitiveness.

The socio-economic analysis identifies clear market failings in the areas of research and development and finance for business development. Addressing these issues in conjunction with existing mainstream priorities will help the region to further develop its knowledge-based economy.

The regional level economic growth also masks significant areas of under-performance where competitiveness is being held back by multiple disadvantage. Promoting action to help these areas to close the gap will help the region overall to grow more quickly while also overcoming intra-regional disparities. Similarly some rural parts of the region have been unable to sustain the same levels of economic growth because of out-migration and a limited economic and educational base. Targeting actions to help address these structural weaknesses is clearly an area where ERDF funding can be

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[2] COM(2004)492 final

justified. However any interventions need to be linked to clear outcomes and complementary to the domestic policy agenda.

The strategy provides a good level of consistency in that Priorities 1 and 2 will help to unlock economic potential through enterprise and innovation across the region. This should provide the background of economic growth within which Priorities 3 and 4 can help to address some of the structural inequalities and imbalances facing some urban and rural areas. The flexibility facility strengthens the link with the ESF programme.

The geographical focus of the third and fourth priorities should mean there will be no conflict between them. However the region-wide nature of Priorities 1 and 2 will mean there is potential for overlap with Priority 3 in areas targeted. This potential for conflict relates to the area of enterprise start-ups which both priorities cover. However this risk can be avoided through clear operational guidelines when areas under Priority 3 are selected.

The Executive has identified lessons from the past in developing areas for intervention in the current programme, reflecting the need to make the more limited funding allocation count. However the focus on some riskier activities such as RTD support and venture capital reflects the intrinsic level of risk needed in order to address current market failures.

In addition, the decision to allocate resources to large bespoke projects (through IDBs) and also through challenge funding indicates a reasonable balance in terms of risk. The Executive has looked at existing interventions and possible alternative actions to identify where ERDF funding can add most value.

Assessing strategic coherence

This chapter looks at the programme strategy in the context of policies at EU and Scottish level. The Community Strategic Guidelines set out priorities at EU level the strategy needs to support and contribute to achieving the Lisbon objectives. We mapped the priorities of the 2007-13 ERDF Operational Programme for the LUPS area against these and the key domestic policies to assess strategic coherence. This analysis justifies the choice of priorities in the light of these context priorities and the Operational Programme clearly shows where the links are. The strategy chosen also takes account of lessons learned from previous relevant programmes.

Supporting EU policy

Figure 3 below summarises how programme priorities will support the relevant main priorities of the Community Strategic Guidelines. Priority 1 and 2 directly address some of these. However, priorities 3 and 4 also follow the CSG which note[3]:

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[3] COM(2005)0299

- 'Actions supported [should] include measures to promote entrepreneurship, local employment and community development' (ERDF Priority 3)'; and

- 'Cohesion policy can also play a key role in support of the economic regeneration of rural areas' (ERDF Priority 4).

Figure 3: Mapping OP priorities against EU priorities

Community Strategic Guidelines	Support through LUPS ERDF priorities for 2007-13
Making Europe and its regions more attractive places to invest and work • Expand and improve transport infrastructures • Strengthen synergies between environmental protection and growth • Address Europe's intensive use of traditional energy sources	Will not be addressed through Structural Funds but domestic resources Environmental sustainability as horizontal theme – addressed through eligible activities under all priorities
Improving knowledge and innovation for growth • Increase and improve investment in RTD • Facilitate innovation and promote entrepreneurship • Promote the information society for all • Improve access to finance	Priority 1 Priorities 1 and 2 Priority 2
Creating more and better jobs	Priorities 1and 2
Taking account of the territorial dimension of cohesion policy	Priority 4

UK national and Scottish policy

The priorities of the 2007-13 Operational Programme fit with the relevant policies at UK level and UK Government's National Reform Programme. The *policy context* section clearly shows the relationships between the priorities and related policies.

The UK National Strategic Reference Framework explains how the UK – and Scotland – will use Structural Funds to achieve the Lisbon objectives. The strategy in the ERDF Operational Programme links into the NSRF logically. At Scottish level, some key strategies set the policy direction for economic development interventions.

The overarching strategy for developing the Scottish economy is the Framework for Economic Development in Scotland (FEDS) and the new

ERDF priorities are relevant to its key outcomes. The ex-ante evaluation also looked at strategic fit with:

• Smart Successful Scotland

• Closing the Opportunity Gap;

• Scottish Green Jobs Strategy;

• Regeneration Policy Statement;

• Rural Scotland: A New Approach;

• Scottish Sustainable Development Strategy; and

• A Science Strategy for Scotland.

Figure 4 below shows that OP priorities are in line with these strategies and where the links are.

Figure 4: Fit with Scottish strategies

Strategy	Priority 1	Priority 2	Priority 3	Priority 4
Smart Successful Scotland	x	x		x
Closing the Opportunity Gap			X	x
Regeneration Policy Statement			X	
Scottish Green Jobs Strategy		x		
Rural Development Strategy				X
Sustainable Development Strategy	x	x	x	X
Science Strategy	x			

Ensuring environmental sustainability

The Operational Programme addresses the cross-cutting themes – equal opportunities, environmental sustainability and social inclusion – through its various aspects. For this summary we will comment briefly on how it promotes environmental sustainability.

Informed by relevant domestic strategies – the Scottish Sustainable Development Strategy, the Green Jobs Strategy and the Scottish Biodiversity Strategy – each of the priorities support environmental sustainability through

one or more types of eligible activity. These include sustainable commercial use of renewable technologies under Priority 1 and activities to raise environmental awareness in communities and enterprises under Priority 3. The Executive also took the recommendations from the commissioned Strategic Environmental Assessment into account.

Financial resources

The financial allocations were based on unit costs of the different interventions developed through data from the Annual Implementation Reports and the EKOS Beneficiaries Survey. Some unit costs are clearly easier than others to quantify and others (for example ha. of land improved) are perhaps more difficult to accurately put a cost against.

The relative allocations across the Priorities have been the subject of detailed consultation and discussion with key stakeholders. The proposed allocations reflect the extent to which ERDF resources can address current gaps and weaknesses, and therefore add value to the domestic investment.

Spreading funding allocations almost evenly across the whole funding period 2007-13 carries certain risks in terms of sustainability and the n+2 rule. Ideally funding would increase considerably after the first year and decrease gradually from there towards the end in 2013. Only then supply would be in line with demand. It would encourage projects to develop exit strategies and prepare for operating without Structural Funds. It would also be a better response to lessons learned from previous funds regarding n+2. The Executive does not control overall annual allocations as the European Commission determines these. However, flexible intervention rates may offer scope for lowering risks.

The funding allocation percentages for the LUPS ERDF programme are:

- Priority 1:   24.5%

- Priority 2:   32.5%

- Priority 3:   27.0%

- Priority 4:   13.6%

- Priority 5 (TA):   2.4%

The Executive has allocated most funding to Priority 2 (Enterprise Growth) which seems appropriate as this clearly support the Lisbon goals and is a key weakness identified in the socio-economic analysis.

Priority 1 (Research and Innovation) will receive just under a quarter of the overall amount. While this allocation is relatively modest, the programme guidance makes clear that the funds will be focused on adding value to the significant innovation and research spend currently managed through domestic strategies. This allocation should therefore be appropriate.

Priority 3 (Urban Regeneration) is allocated just over a quarter of the total. However projects under this Priority will be able to take advantage of additional funding from ESF for certain eligible activities, therefore this level of allocation is appropriate.

Priority 4 (Rural Development) is allocated the smallest amount in the ERDF programme (13.6%). This reflects the relatively small proportion of the population and business base within more remote parts of the LUPS region. Nonetheless the funding under this priority will need to be carefully targeted at clear areas of market failure so that it can make an impact during the programme period.

Quantification of objectives: indicators and forecasts

The Operational Programme identifies a set of output, result and impact indicators. This section gives a brief overview of how the indicators were developed before providing the ex-ante evaluators' assessment of how appropriate the indicators – as well as related targets – are.

Developing indicators

The Scottish Executive commissioned a study that aimed to identify a suitable set of indicators and targets for the 2007-13 programmes. The specification for the research took into account lessons from previous programmes by stressing that this set of indicators would have to be scaled down and simplified compared to existing ones. As ex-ante evaluators we attended and contributed to two workshops that were part of the development process. However the approach taken – whereby indicators were developed in advance of activities – has not benefited the quality or relevance of the indicators.

The results of the process needed further refinement to make the indicators appropriate for effectively measuring progress *and* meet the Commission requirements. This summary report sets out our comments on the near-final version of programme indicators and makes some recommendations.

Assessing indicators' relevance

Experience from previous programmes has shown projects do not benefit to any great extent from the data collected, so the indicators are designed to be the minimum required to monitor the programme. Where more detailed, or different, indicators are required these should relate back through the programme to support its delivery, and integrate with national and regional strategies.

The indicators chosen do reflect the activities that will take place under each priority, so there is a distinct logic behind their choice – a causal chain that runs through the programme.

There are practical difficulties associated with tracking beneficiaries post-intervention which mean that much of the longitudinal data will have to be collected at programme level, rather than by individual projects. These difficulties are a lesson learned from previous programmes and addressed in the choice of indicators. This is a positive result for the programme as it will yield more reliable data over time and reduce the onus on projects to track beneficiaries that they may have no dealings with.

Some work needs to be done in determining how some of the data for the indicators can be effectively collated, and the information fed back to projects, programme managers and other stakeholders. All indicators should be assessed to see if baseline work is needed at this stage.

Assessing numerical forecasts

The numerical forecasts in the Operational Programmes have been developed based on the most recent and comparable information from similar programmes from Annual Implementation Reports. Additional information on the unit costs of different outputs was gathered through a Beneficiaries Survey commissioned by the Scottish Executive. They have also been subject to widespread internal discussion and consultation with key stakeholders, including those involved in delivering similar interventions.

The main question is the use of current unit costs for a programme that will continue to deliver to 2013. If the programme is trying to drive down unit costs then this is a reasonable basis for calculating targets, but delivery agents should be told that they will have to be more efficient (in line with the reduced TA allocation). But if we assume that costs will rise in line with Treasury inflation estimates, then we need to discount the targets by around 2% per annum. Otherwise the targets are unattainable because the unit cost in year 7 will be 12% greater than in year 1.

The targets need to be assessed for achievability across the programme, because the demand curve for projects is different from the supply curve (actually straight line) of resources. So at all times there is likely to be a disparity between demand and supply that must have an effect on targets.

There is also a question over whether the £200k project threshold will have an effect on targets, as larger more strategic interventions are being encouraged. But it is not clear what impact this change will have on delivery.

Targets and indicators by priority

ERDF Priority 1

The research and innovation priority raises the issue of causality. Job creation is somewhat incidental to the main aim of the priority, which is R&D activity, although acknowledging it is more the application of R&D. The indicators identified for this priority focus primarily on outputs and hard outcomes (jobs, patents and expenditure). However given the Lisbon objectives of building a knowledge economy it may be worth considering whether the skill level of jobs

created should be measured as an impact/ outcome; particularly given that the information will be gathered through a specifically commissioned survey.

Using the AIR as a base for unit cost is logical but only if the interventions in the new programme are on the same scale as before.

ERDF Priority 2

Priority 2 – Enterprise Growth - the indicators for this element of the priority again combine outputs (in terms of participating businesses) and hard outcomes in terms of jobs created and safeguarded and business start-ups. Again the Executive might want to consider whether the type of jobs (in terms of skill level and earnings) should form part of the net jobs increase indicator. For example, there may be no net job increases in a business, but it may have generated higher level jobs rather then unskilled ones, through the ERDF investment. GVA per job will also be an important indicator in addition to overall GVA as a measure of whether productivity (and therefore competitiveness) is increasing.

The indicator for environmental resources could be more explicitly measurable and relate more clearly to improving business efficiency through energy saving, and or carbon-reduction. There are some useful examples in the Executive's (ERDF funded) Loan Action Scotland evaluation.

The logic behind the targets seems sound but the problem with a unit-cost based estimate, rather than a demand-based estimate projected over the life of the programme, is that it assumes that the same scale of intervention will be needed. If the activities are properly targeted, and make use of best practice, the cost per business assisted should be much higher, with a high success rate.

ERDF Priority 3

The indicators suggested for Priority 3 (Urban Regeneration) comprise output indicators on participating businesses and the number of community facilities upgraded and results indicators around jobs created and land rehabilitated. Given that Priority 3 highlights the key role of social enterprises in deprived areas it would be useful to break down the jobs and business indicators for social enterprises as well as SMEs. This will make it easier to evaluate the role that social enterprises play in these areas and has been done for some of the ESF indicators.

The indicator of land rehabilitated is not a relevant one to the activities proposed. Activities relate to small-scale conversion, refurbishment and adaptation of premises, therefore an indicator looking at the square metre-age of business space would be much more relevant.

The impact indicator relating to changes in the relevant rankings within the SIMD should be more explicit about what ERDF funding is trying to achieve in terms of increasing SME activity and enterprise in deprived communities. The SIMD is a composite indicator which looks at various measures of deprivation including income and employment. However it only provides a relative indication of how one area compares to others rather than whether an actual

improvement takes place. So an area can move up the rankings without actually improving, if other areas (which do not receive funding) worsen. The Executive should consider whether the SIMD is the most effective way of assessing improvements in economic performance in deprived communities, rather than other indicators, such as level of benefit claims, local employment levels or earnings against a clear baseline.

The logic is appropriate for these targets but the scope of this priority is very wide so estimating the targets at this stage is difficult. As far as the unit costs are concerned, the AIR figure for jobs created would be preferable. Experience suggests that a figure of around £15k per job, in difficult circumstances, is more realistic. And the figure for jobs safeguarded is more likely to be the AIR figure.

ERDF Priority 4

The indicators for Priority 4 again focus on outputs and numbers of jobs. Given the importance of diversifying the rural economy and adding value, it may be worth considering indicators that measure the quality or skill level of jobs or the GVA per job, rather than just looking at job numbers. Some labour intensive sectors add very little value to rural economic growth.

There needs to be a recognition in these indicators that rural Scotland is starting from a different baseline in terms of job diversity, earnings and skills.

There is a problem with the unit cost calculation for these targets, because the numbers are higher than in Priority 3, with less funding available. As the business base is a fraction the size, the proportion of businesses the target represents in the area is going to be many times that in Priority 3, so it seems less realistic. Quoted costs per job from rural development studies suggest that costs may be higher in rural areas than urban areas. Including some measure of sustainability of jobs over time might be appropriate, although this can only be measured by post-intervention survey.

Delivery arrangements

The Scottish Executive as Managing and Certifying Authority will work with the newly appointed Intermediate Administration Body (IAB) for the LUPS area to implement the ESF and ERDF programmes. They will use a combination of challenge funding and direct allocations of block funding to a number of Intermediate Delivery Bodies (IDBs) to deliver elements of the programmes. The IDBs are existing domestic delivery organisations who will support specific major projects.

The mix of challenge and block funding was identified as the most suitable approach for Scotland through in-depth research, including a comparative study across the EU and stakeholder consultations. Some aspects of Priority 2 (Urban Regeneration) will be piloted through a small number of IDBs and the lessons from these pilots used to develop further phases of intervention.

Selecting delivery bodies

<u>Intermediate Administration Body</u>

The Executive selected the IAB through an open tendering process. Unlike in previous funding periods, one single body will be responsible for managing and administering the ESF *and* the ERDF programme. This arrangement is likely to ensure better coordination and integration of EU-funded activities – as recommended in previous evaluations. This is particularly important considering the increased focus on strategic fit for the 2007-13 period.

At tendering stage, the Scottish Executive set out the tasks and key duties of the IAB, as well as a set of key criteria against which the body's performance will be measured. The latter cover:

• application processing;

• claims processing;

• project monitoring;

• management reporting;

• communications; and

• secretariat functions.

The performance criteria and the targets seem appropriate for effective delivery. The requirements as outlined in the tender document, reflect a shift of the IAB's focus from a purely administrative role to more project support and development. This had been an issue from stakeholder consultations, particularly in the face of smaller project numbers that result from lower funding levels. As well as setting clear quality criteria, the tender document left some scope for contractors' judgement on the most effective way to implement processes.

The successful tenderer – East of Scotland European Partnership – has been the Programme Management Executive for the East of Scotland Objective 2 Programme for some times. Building on this experience the organisation is well placed to carry out the role of IAB effectively.

Considering the length of the funding period, it seems appropriate to limit the contract with the IAB to three years initially. After that the Scottish Executive will decide on extensions on an annual basis.

<u>Intermediate Delivery Bodies</u>

The principles and criteria the Executive has been applying when selecting IDBs seem appropriate. The approach is ring-fencing money and allocating it to a number of bodies or partnerships with a history of effective use of Structural Funds money to fund a small number of major strategic projects. Scottish Enterprise as the main economic development body will receive substantial funding under Priority 1 on the basis of pre-determined key projects, which is likely to ensure strategic fit of activities with Smart Successful Scotland and the Lisbon objectives. As a major rural area the

south of Scotland needs dedicated strategic intervention. South of Scotland Alliance will be the suitable body for delivering this and creating a strategic legacy. The partnership has a clear strategy and has a good history of making best use of Structural Funds.

In selecting appropriate Community Planning Partnerships to pilot the Priority 2 measures, the Executive should consider their track record of effectiveness in delivering against their existing Regeneration Outcome Agreements.

Procedures

Procedures for dealing with applications and claims seem appropriate. Particularly plans to introduce a two-stage application process, which many stakeholders had called for, will improve efficiency. Projects unlikely to receive funding can be filtered out. We recommend that the IAB should provide advice and support for organisations producing their project outlines. Target timescales for processing are likely to ensure smooth running and help prevent 'n+2 risks'. Projects will be appraised by appropriate committees who will provide the necessary knowledge and experience but also strategic direction.

The Scottish Executive has an online application system that will be used for project applications and claims across programmes. The lack of such a system had been a point of criticism in previous programme evaluations. The system will ensure consistency and many organisations will already be familiar with it.

The introduction of a minimum project size of £200,000 is a new approach for Scottish Structural Funds, and its impact on the type of project being developed is difficult to anticipate. The Executive should therefore keep this under review along with the proposed intervention rate over the programme period.

The evaluation strategy for the 2007-13 programme will follow a similar structure to that used for the 2000-06 programme but take into account recommendations from previous evaluations, most importantly the mid-term evaluation of the Objective 3 programme. One key recommendation was to undertake more monitoring visits. The new monitoring plan envisages monitoring visits to 10% of volume as well as 10% of value of all projects which is in line with EU regulations and seems appropriate. The IAB is responsible for these visits which cover challenge fund *and* non-challenge fund projects. The Scottish Executive, in turn, will carry out detailed monitoring visits to the IAB as well as verification and compliance visits to a percentage of projects. It is important that distribution of funds across geographies and sectors is monitored, as recommended in the Objective 3 mid-term evaluation. Overall monitoring and evaluation provision, including reporting arrangements, seem appropriate.

The administrative burden the programme entails is – to a large extent – the result of Commission regulations for implementation. However, the Executive has taken steps to reduce administration requirements while following the regulations, such as a reduction of IABs. The threshold for minimum project

size, a planned 2-stage application process and a move towards multi-year funding also offer opportunities for reducing the administrative burden, so does the Executive's encouraging of partnership working.

A communications strategy underpins communication between the Scottish Executive and the IAB and any publicity on the programmes. Marketing and PR channels are clear with the Scottish Executive's Structural Funds Division acting as the Managing Authority's contact point. We recommend putting increased emphasis on dissemination of good practice, for example by setting up a searchable project database.

The role of partnerships

The implementation arrangements offer opportunities for constructive partnership working where appropriate and the Operational Programme itself was developed through a partnership approach. The Programme Monitoring Committee as a key body for delivering the programme will reflect this through its membership.

Whether partnerships at project level should be a requirement for delivering the new Structural Funds programme has been the subject of many lengthy discussions. Stakeholders agreed that certain elements of partnership working could benefit project success but downsides included potential disparity of power and costs of developing and managing partnerships. The Scottish Executive has taken the approach of encouraging but not prescribing partnership working which provides some flexibility in that partnerships are likely to be used where appropriate. The implementation of a minimum project size will encourage organisations to work together to develop appropriate partnership arrangements where this will add value to delivery.

Risk appraisal

Figure 5 below summarises the main risks we have identified in the context of programme implementation.

Figure 5: Summary of risks from implementation provisions

Risk	Recommendation
IAB does not meet performance criteria and Managing Authority decides not to extend the contract	Closely monitor performance and develop alternative strategy if necessary
IAB has more experience of managing ERDF – gaps in knowledge and experience	Ensure staffing profile reflects the wider remit
IAB is biased towards its traditional geographic area	Management group should be broadly representative of all parts of the LUPS region and application processes transparent and accountable.
IAB does not have the right staff and skills in place over time	IAB should develop an appropriate workforce plan that will minimise the risks of staffing problems; particularly towards the end of the contract period.

CPPs turn out to be unsuitable as IDBs	SE should pilot this approach initially to highlight any issues with the delivery capacity and effectiveness of CPPs. A robust evaluation framework should be developed for the pilot.
Lack of awareness among advisory groups and project sponsors of targets, indicators etc.	Have a robust communication strategy in place that covers how various players will be informed and updated.
Monitoring is less consistent for projects funded through IDBs.	A requirement to report on a small number of core indicators should be part of commissioning process.

Conclusion

The final version of the 2007-13 ERDF programme for Lowlands and Uplands Scotland is the result of a process of extensive consultation, as well as interactive and iterative working between the Scottish Executive and ex-ante evaluators. We consider the Operational Programme and its provisions fit for using ERDF money effectively to address existing market failures and add value.

More specifically, we can confirm that:

• a socio-economic analysis of the area was undertaken that meets the requirements of Commission guidance;

• the Programme has a valid and consistent strategy so priorities and their eligible activities address the needs identified by the socio-economic analysis;

• the strategy is strategically aligned with the Lisbon Strategy and relevant strategies at EU, UK and Scottish level;

• the implementation system is suitable for delivering funds effectively;

• lessons learned from previous interventions have been taken into account; and

• the Programme addresses the horizontal themes – equal opportunities, environmental sustainability and social inclusion – through its various aspects.

We have made some final recommendations on indicators, financial allocations and numerical forecasts for the Executive to consider in the Operational Programme they will submit to the European Commission.

Executive Response to Final Ex-Ante Evaluation Report

The ex-ante evaluation process has been a highly valuable, iterative process that has resulted in continual improvements to the quality of programme development and the final Operational Programme. Recommendations have been made on – and responded to – the different drafts of the Programme by the evaluators. Consequently, while the above summary represents the final set of comments by evaluators, it does not fully capture the process of

dialogue that has marked the process as a whole, resulting in a higher quality Programme.

The Executive has take on board the final recommendations by the ex-ante evaluators in the completion of the Programme.

ANNEX E: NON-TECHNICAL SUMMARY OF STRATEGIC ENVIRONMENTAL ASSESSMENT

Introduction

This is the non-technical summary of the SEA Statement, which details how the Strategic Environmental Assessment Environmental Report prepared for the Scottish Executive's Lowlands and Uplands Scotland European Regional Development Fund Operational Programme 2007-2013 and comments received during consultation have been taken into account in the development of the final Operational Programme. The full Statement is available separately.

The Environmental Report was prepared by RSK ENSR and subject to a full consultation on the draft Operational Programme and the Environmental Report from 13 November 2006 to 29 January 2007. Responses came from five bodies: the key designated environmental bodies for the Strategic Environmental Assessment (Historic Scotland, Scottish Environment Protection Agency, Scottish Natural Heritage) as well as the Royal Society for the Protection of Birds Scotland. In the full consultation on the Operational Programmes (as described in a previous annex), there were a number of other comments made on the environmental implications of the Programme made by partners.

The ERDF Programme will be the main focus of European support for economic development in the Lowlands and Uplands of Scotland over the period 2007-2013. EU and national legislation require that a Strategic Environmental Assessment (SEA) be undertaken to establish the impact of the Programme on the region's environment prior to adoption.

Full details of the assessment process and findings are provided in the Environmental Report. The purpose of this Statement is to detail how the findings of the SEA process, including recommendations made in the Environmental Report, and comments received from the statutory consultees, other organisations and the general public during consultation have been taken into account in the final approved Operational Programme.

The Programme has a level of environmental protection built in through European requirements for ERDF monies to be used sustainably. In addition, there is a level of existing environmental protection within Scotland for a range of environmental aspects. However, there are a range of additional measures which the Scottish Executive could look to include within the Programme. These were detailed in the Environmental Report. This Statement looks at the degree to which these have been taken into account in the final adopted Operational Programme.

Key changes to the Operational Programme

A number of changes have been made to the Programme based on the findings detailed in the Environmental Report and the responses received during consultation. Full details are given in the Statement. The bullet points detailed below address some of the issues and recommendations raised by the SEA.

Award criteria

The Executive will make use of the following:

- Ensure that built development will be on 'lower' quality land (and out with the 1:200 yr flood plain) wherever practical and that there are no negative impacts on biodiversity and habitats

- Support for environmental technologies

- Ensure that development will comply with existing regulatory controls

- Promote re-use of contaminated sites

- Support development of low-emission public transport, where possible

- Promote energy efficiency within buildings and the use of renewable energy, where possible

- Encourage green design for urban / townscape projects

Indicators and monitoring

The Executive will introduce the following Programme indicators for which data collection will be ongoing:

- Area rehabilitated

- Number of energy-saving and resource-efficiency projects

- Number of businesses implementing Environmental Management Systems

- Number of renewable energy projects

A thematic evaluation of environmental impacts at the mid-term point in the Programme. This will collect data and make assessment of Programme impact on the following:

- Greenhouse emissions CO_2 and equivalents

- Number of premises/floor space refurbished/constructed to BREEAM standards

- Percentage of waste reduced or materials recycled

- Hectares of derelict/vacant land reused

- Number of projects ensuring sustainability and improving the attractiveness of towns and cities

- Area of contaminated land remediated

Priority-specific issues

A number of recommendations were also made in the Appendix of the Environmental Report regarding mitigation and environmental opportunities for each of the draft Programme priorities. Whilst these priorities have changed, the activities supported have not significantly, so the recommendations, and the Executive's response to these, remain valid.

For all four priorities (Research and Development, Enterprise Growth, Urban Regeneration and Rural Development), the Executive will:

- Encourage development on lower-quality sites and discouraged from adjacent biodiversity sites;

- Target areas with lower life expectancy, although this will occur under the Urban Regeneration priority;

- Target areas with smaller settlements, particularly through the Rural Development priority;

- Ensure that projects do not adversely contribute to flooding risks;

- Encourage investment in energy-efficiency, waste-recycling and other environmental technologies;

- Support development of local enterprises, particularly under the original Priorities 2 and 3;

- Encourage efficient energy use within buildings;

- Support green design in townscape projects; and

- Ensure developments do not have an adverse impact on the historic environment.

How the Environmental Report has been taken into account

The findings of the Environmental Report have been taken into account in the development of the final Programme in a number of ways. Small changes have been made but the key change has been the development of the set of bullet points detailed in the section above. These have been developed largely to enhance the potential positive impacts of existing Programme objectives but also to ensure that the environmental impact of the Programme is monitored.

How consultation comments have been taken into account

During the public consultation, around 100 responses were received which made specific mention of the Environmental Report. The most detailed responses came from statutory Consultation Authorities. Some of the comments received were positive or did not lend themselves to a response or action on the part of the Executive. For the remaining comments, a range of issues were raised which have been responded to in detail in the Statement.

Alternatives

In the case of the ERDF Operational Programme, the assessment of strategic level alternatives was extremely limited as the Programme's development is strongly led by economic requirements and constraints already established at EU and the national level, including priorities stipulated by European Guidelines and the National Strategic Reference Framework. The Consultation Authorities felt that the issue of alternatives had been dealt with sufficiently in the Environmental Report.

Monitoring

To meet the needs of the SEA process and European requirements regarding structural funding, a range of monitoring will be undertaken by the Executive on the Programme over the coming years. This will include a number of environmental indicators. In particular, as part of a mid-term Programme evaluation the impact of supported activities on a broader range of environmental indicators will be assessed. The coming months will be used to establish Programme delivery mechanisms including the detail of the monitoring framework.

Scottish Executive statement

The Executive has taken full account of the recommendations of the Environmental Report and the SEA Statement, summarised above. This has been an iterative process involving continuing dialogue with the SEA consultants and the designated environmental bodies and has improved the quality of the Programme significantly.

ANNEX F: SUMMARY OF ENVIRONMENTAL SITUATION

Introduction

A list of baseline data that was collected and analysed is shown in Section 5.3 below. Due to the size of the study area and the fact the Operational Programme has not yet been finalised, this section details those key environmental aspects considered to be relevant to the scope and potential influence of the Programme. It is recommended that when the Operational Programme is finalised and sites are identified, addition data is collected and analysed which will be more targeted toward the areas identified for development.

The establishment of an environmental baseline will help to establish what the key environmental trends and issues in the region are and therefore where there are either concerns regarding the Programme or where the Programme may have a positive environmental effect.

Data to be addressed

The area of the Lowlands and Uplands stretches from Aberdeenshire and Moray in the north east, in a south westerly direction through Angus, Stirlingshire, Fife, the Lothians and the Borders to Galloway and Ayrshire.

Data and information have been gathered through desk-based research. This has draw on a range of sources, including Scottish Executive Publications and Statistics, Scottish Natural Heritage (SNH), the Scottish Environment Protection Agency (SEPA) and Historic Scotland (HS).

Due to the size of the study area and the strategic nature of the assessment has not been possible to identify or describe all areas in detail. Therefore the general characteristics of the area are discussed, including general landform, soil characteristics and land use. The general environmental issues affecting the study area are discussed in the following chapter.

It is recommended however that a further review of the SEA is carried out when the Operational Programme has been finalised and sites have been identified. At that stage it will be possible to focus the SEA on specific areas and identify the environmental characteristics and issues relevant to the programme.

Geographical area

Geographically, Scotland can be divided into three distinct areas: the Southern Uplands, the Central Lowlands (or Central Belt) and the northern Highlands and Islands. For the purposes of this study the East Coast Belt has been included with the Central Lowlands. The Highlands and Islands have been considered in a separate assessment.

The Southern Uplands

In general terms the Southern Uplands are the fertile plains and hills bordering England. The region boasts magnificent scenery, albeit of a gentler nature than that found in the Highlands with the highest peak in the area being only 2763 feet (815 m) high.

There are a number of large water bodies in the Southern Upland area, many of which have been dammed for the purposes of water supply or power generation. The largest of these include Lochs Doon, Ken and Bradan, Clatteringshaws Loch and Daer Reservoir in the west and Talla, Fruid, Megget, Gladhouse and Whiteadder Reservoirs in the east. In addition there are a number of important rivers, in particular the Rivers Tweed, Border Esk, Annan and Nith, which have significant numbers of migratory salmonids.

Several different soil patterns are found in the Southern Uplands. These result both from natural processes and human influence. The patterns are reflected in a variety of habitat types and land uses. One of the main controlling factors is altitude. In the east of the region, the soils gradually change with increasing height. Further west, soil patterns are often more complicated. This is typified in lowland Galloway with glacial deposition greatly influencing the character and composition of the soils. The Galloway Hills are more similar to parts of the Highlands and Islands than the easterly hills, being more rugged with large areas of bare rock, thin covers of glacial deposits and shallow soils.

Land use in the Southern Uplands is governed by certain limiting factors, such as slope, temperature and wetness. The altitude at which good quality pasture is possible declines from east to west as rainfall increases. Soils in the western Southern Uplands may be stonier and shallower than their eastern counterparts. Agriculture is by far the biggest land use in the Southern Uplands, although forestry has undergone a great deal of expansion in recent decades.

The Central Lowlands

The cities of Edinburgh, Glasgow and Dundee together with numerous towns, most of the population and the majority of Scotland's industry are located within the Central Lowlands. This broad valley averages 50 miles across and runs WSW to ENE across the centre of the country. It is geologically distinct from the surrounding regions, being composed of Devonian Old Red Sandstone, peppered with ancient volcanoes, as against the older sedimentary rocks forming the Southern Uplands or the ancient metamorphic melange, comprising the Highlands to the north.

The Central Lowlands extend across Scotland between the mountains of the Highlands and the hills of the Southern Uplands. The soil distribution is influenced mainly by the material deposited following the last period of glaciation frequently containing many smaller particles, and can produce poorly drained soils, especially in the west where rainfall is higher. Moving towards the drier east, the soils gradually change in their composition. This is typified with Gleys first, then brown forest soils with gleying and, further east,

freely drained brown forest soils, which are found on coarser sandy material. This latter soil is particularly evident in river valleys. On the higher ground, such as the moorlands and upland areas of Cumnock and around Muirkirk, peats and peaty gleys are in evidence.

Human activity has significantly influenced the vegetation found within the central lowlands. This is typified by the widespread planting of non-native plantation woodland, both coniferous (for commercial forestry) and deciduous (in estates). Following the decline of heavy industry, grasses, herbs and rushes have invaded former mining and industrial areas between Edinburgh and Glasgow.

There are a number of significant river catchments within the Central Lowlands. The most notable being the Rivers Clyde and Forth and the lower reaches of the River Tay, which open into significant estuaries and support three of the major cities of Scotland (Glasgow, Edinburgh and Dundee respectively).

Apart from agriculture and forestry, the major land use in the Central Belt is urban and industrial. The two largest conurbations, Edinburgh and Glasgow, accommodate a substantial proportion of the Scottish population. The legacy of land use for mining and other industry is evident and has transformed the nature of the landscape. Towns, buildings and roads are often located on the best quality soils in a given area as the soils are usually associated with other environmental factors such as good drainage.

For the purposes of this assessment, the eastern coastal belt, running from the north east, around Fraserburgh, down the east coast of Scotland, has been incorporated into the Central Lowlands area. This region has few major population centres apart from the cities of Aberdeen and Dundee.

The Eastern Belt forms the main agricultural zone in Scotland. Cereals and root crops are grown in many parts of the region and market gardening is also common. On parts of the coast itself, there are large areas of windblown sand. Here, the soil profile development is limited, due largely to the effects of continual deposition of sand. Where the soils have been longer established, a greater variety of grasses can survive, making the land suitable for grazing or for use as golf links. The main restrictions on land use in the coastal strip are periodic drying out (due to free draining soils and low rainfall levels), and exposure to strong winds. Where these limitations cause particular problems, the land is generally used for pasture rather than crop production. There are further pressures associated with the use of the dune soils for recreational activities, which include caravanning and camping. These can result in compaction and increase the susceptibility to erosion.

Population

In terms of population, Scotland has one of the most urbanised and unevenly distributed populations in Europe with around 80% of the population located within the Central Belt and a third of the population living within the main population centres of Glasgow, Edinburgh, Aberdeen and Dundee. The rural

areas of Scotland, which account for 89% of the land mass are inhabited by just one third of the population.

The following table shows the projected population change over the next 30 years (in thousands).

	1994	2004	2011	2021	2031
England	48229	50094	51967	54605	56832
Scotland	5102	5078	5120	5127	5065
Wales	2887	2952	3037	3165	3256
Northern Ireland	1644	1710	1767	1830	1860
United Kingdom	57862	59835	61892	64727	67013

Designated natural heritage sites

Scotland has over 1400 sites designated as Sites of Special Scientific Interest (SSSI), representing approximately 12.6% of the total land area of Scotland. Approximately half of these sites are located in the Lowlands and Uplands area. The following table represents the local authorities with the largest total area of designated sites[4]. These five areas contain almost three quarters of Scotland's SSSIs, which collectively represent almost 3% of the total land area of Scotland.

	Total area of Local Authority (ha)	No. of Sites	SSSI Area (ha)
Dumfries & Galloway	667297	96	75384
Perth & Kinross	541890	113	69167
Aberdeenshire	633881	82	39805
Scottish Borders	474263	91	28523
North Ayrshire	90384	28	23247

In addition to a significant proportion of designated SSSIs, the above council areas also contain the majority of cSAC (candidate Special Area of Conservation), SPA (Special Protection Area) and Ramsar sites located in Scotland. In general terms the main urban centres tend have a much lower percentage of designated sites in comparison with rural areas.

It is recognised that natural heritage interests do not solely relate to designated SSSIs, Natura 2000 or Ramsar sites and will include sites such as National Parks, NSAs and NNRs, however the analysis of SSSIs is intended to give a general impression of the most significant Local Authority areas in terms of natural heritage interests and further detailed studies should be carried out as more information is available on specific projects. Furthermore

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[4] SNH, 2004, SNH Facts and Figures: Designated Areas and Sites, data accessed at: www.snh.org.uk/pdfs/publications/corporate/factsandfigures/0304/contrents.pdf

the health of such habitats and populations should also be assessed as the Operational Programme is finalised.

Air Quality

The pollutants which determine air quality in Scotland include the gases sulphur dioxide and oxides of nitrogen from combustion processes, ammonia from agriculture and volatile organic compounds from motor vehicles and industrial processes.

Although pollutants present in Scotland's atmosphere are emitted from sources both within Scotland and elsewhere in Europe, it is the localised concentration of pollutants, for example as a result of high levels of traffic congestion, which are highlighted for the purposes of this study.

Efforts to improve in air quality in certain areas has resulted in number of Air Quality Management Areas (AQMAs) being declared in Scotland. These include:

• An area of Aberdeen city centre which covers Market St, Union St, King St (between Castle St and Roslin Terrace), Virginia St, Commerce St, Guild St (between Market St and Stirling St) and Holburn St (between Great Southern Road and Union St).

Designated due to elevated levels of both nitrogen dioxide (NO_2) and Particulate Matter < 10 μm (PM_{10}).

• An area of Chapelhall extending along Main Street, Bellside Road and Lauchope Street and extending to cover a number of properties close to the junctions of these roads.

Designated due to elevated levels of Particulate Matter < 10 μm (PM_{10}).

• An area of Coatbridge, extending along Whiflet Street and North Road and encompassing buildings fronting the road.

Designated due to elevated levels of Particulate Matter < 10 μm (PM_{10}).

• An area covering Edinburgh city centre, including the main link roads in to the city centre.

Designated due to elevated levels of Nitrogen dioxide (NO_2).

• An area of Glasgow city centre bounded broadly by the M8 motorway to the north and west, the River Clyde to the south, and the High Street and Saltmarket to the east.

Designated due to elevated levels of Nitrogen dioxide (NO_2).

• An area encompassing a 60m wide corridor along the A803 Kirkintilloch Road, Bishopbriggs between the council's border with Glasgow city and a point 30m north of Cadder Roundabout.

Designated due to elevated levels of Nitrogen dioxide (NO_2).

- An area encompassing part of the centre of Motherwell to the north of the civic centre in the vicintiy of Merry Street, Menteith Road and Arbles Road.

Designated due to elevated levels of Particulate Matter < 10 μm (PM_{10}).

- An area encompassing part of Central Road, Paisley between Smithhills Street and County Square and the service road for the Piazza Shopping Centre adjacent to Central Road.

Designated due to elevated levels of Nitrogen dioxide (NO_2).

In addition to the designated AQMAs, the following table indicates the sites which are routinely monitored under Local Air Quality Management.

	Monitoring parameters
Aberdeen	CO, NO NO_2, O_3, GE10, SO_2, NO_X as NO_2, PM_{10}
Bush Estate	NO_X as NO_2, O_3, NO_2, NO
Dumfries	CO, NO, NO_2, NO_X as NO_2, GR10
Edinburgh Centre	CO, NO, NO_2, O_3, GE10, SO_2, NO_X as NO_2, PM_{10}
Edinburgh St Leonards	CO, NO, NO_2, O_3, GE10, SO_2, NO_X as NO_2, PM_{10}
Eskdalemuir	NO_X as NO_2, O_3, NO_2, NO
Glasgow Centre	CO, NO, NO_2, O_3, GE10, SO_2, NO_X as NO_2, PM_{10}
Glasgow City Chambers	CO, NO, NO_2, NO_X as NO_2
Glasgow Kerbside	CO, NO, NO_2, GE10, NO_X as NO_2, PM_{10}
Grangemouth	CO, NO, NO_2, GE10, SO_2, NO_X as NO_2, PM_{10}

It is recognised that there are other areas which have not been declared AQMAs but nevertheless may have reduced air quality or which may be declared an AQMA if a further reduction in air quality is observed. Furthermore it is recognised that the presence of an AQMA should not be used as the only tool in assessing the significance of air quality in a given area.

Land contamination

Land may become contaminated as a result of various human activities. The contamination of soil with toxic chemicals may have direct effects on human health, particularly if houses and gardens are built on the land in question. For example, vegetable gardens or allotments sited on polluted land may result in contaminated produce from the direct uptake of toxins or the deposition of contaminated particles on the growing plants.

Within Scotland there are a large number of sites that have been classed as either vacant or derelict. It is likely that a significant proportion of these sites have pollutants present in the soil as a result of previous land uses on site.

Given that it is largely industrial processes which give rise to land contamination, the majority of contaminated land is typically located within the industrial centres of the Central Belt and other larger conurbations.

Approximately 0.12% of Scotland's land is classed as vacant or derelict. The table below represents the ranking of local authority areas by area of total vacant and derelict land. Cumulatively this represents approximately half of Scotland's vacant and derelict land and hence represents a significant proportion of contaminated sites[5].

	Total Area of Council (ha)	No. of Sites	Area of V&D Land (ha)	% of Council Area Classed as V&D
North Lanarkshire	47213	380	1315	2.79
Glasgow City	17736	853	1313	7.40
Renfrewshire	26875	170	1002	3.73
Fife	137385	224	897	0.65
West Lothian	43162	67	653	1.51

In addition the Councils above, South Lanarkshire, North & East Ayrshire and Midlothian have significant areas of vacant and derelict land, as do the main urban centres of the central belt and along the east coast, including Dundee and Aberdeen.

The following table represents known contaminated land, by Local Enterprise Company area. The term 'contamination' differs from the statutory definition in the Environmental Protection Act 1990, and refers simply to the presence or absence of a number of potential contaminants. Scottish Enterprise Fife contains 337 hectares of known contaminated land, representing 28 per cent of the total of land known to be contaminated in Scotland. The Scottish Enterprise Ayrshire area has 210 hectares of known contaminated land, representing 18 per cent of the national total. This area also has the largest number of contaminated sites (75) accounting for over 40 per cent of all derelict sites with known contamination in Scotland. In addition Glasgow, Dunbartonshire and Lanarkshire have significant amounts of contaminated land.

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[5] Scottish Executive, 2006, *Vacant & Derelict Land Survey 2005 (ENV/2006/1)*, National Statistics Publication: Edinburgh

	Area (ha)	% by area	No of Sites
Fife	337	28	6
Ayrshire	210	18	75
Glasgow	154	13	23
Dunbartonshire	121	10	25
Lanarkshire	92	8	18
Forth Valley	56	5	2
Edinburgh & Lothian	55	5	4
Dumfries & Galloway	49	4	2
Renfrewshire	17	1	4
Tayside	1	-	2
Borders	-	-	1
Grampian	-	-	-

Of the 1,186 hectares of derelict land in Scotland that is known to be contaminated, coal is the most common contaminant, affecting 443 hectares (48%) of known contaminated derelict land. Other significant contaminants include gases (7%), asbestos (3%), Chromium (3%) and other combustible materials (10%).

Over the past 10 years in Scotland there has been a decrease in the amount of derelict and urban vacant land recorded in the Vacant & Derelict Land Survey, from 13,571 hectares in 1995 to 10,570 hectares in 2005. This is partly attributable to land being brought back into productive use, and partly due to land being removed for definitional reasons or due to naturalisation. The 2005 survey recorded an overall increase of 41 hectares compared with 2004; the area of urban vacant land increased by 82 hectares and derelict land decreased by 41 hectares.

Water quality

The major causes of pollution in Scottish rivers are sewage effluent, diffuse agricultural pollution, acidification, urban drainage, mine drainage and point source agricultural pollution.

Based on SEPA's water quality data for 2004, 72% of Scotland's rivers were classed as either excellent or good water quality (A1 or A2)[6]. A further 10% were classed as Fair (B) while just under 3% were classed as poor (C). In addition 50km or 0.2% of watercourses were seriously polluted (D) and a further 15% of watercourses are currently unclassified.

In general terms, sewage effluent and urban drainage affect the larger population centres, particularly those in the central belt and on the east coast. Mine drainage affects areas of former coal mining activity, and is of particular

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[6] Scottish Environment Protection Agency, 2005, *National Water Quality Classification 2004*, data accessed at: www.sepa.org.uk/pdf/data/classification/water_qual_class_2004.pdf

note within southern and central Scotland whilst diffuse and point source agricultural pollution is most prevalent in predominantly rural areas.

Acidification is a significant pressure on water quality in Scotland and is caused by emissions of sulphur and nitrogen, mainly from industry and motor vehicles. Acidification is a problem over wide areas of Scotland where geology and soils are base poor and are unable to neutralise acid deposition. For the purposes of the study area, acidification is a particularly significant issue throughout Dumfries and Galloway and parts of the Trossach.

In the Central Belt the water quality of the previously heavily polluted rivers such as the Almond, Clyde, North & South Calder and Kelvin have dramatically improved mainly as a result of upgrades to sewage treatment works or closure of polluting industries. The improvement in the South Calder Water at Motherwell following upgrades in sewage treatment and the closure of Ravenscraig steelworks is indicative of improving water quality trends throughout the central belt.

From a Scotland wide context, the net length of poor quality rivers and streams in classes C & D was reduced by 36 km in 2004, giving a total reduction of 402 km since 1999. It is now clear that the improvement target for the period 1999 – 2006, a 351 km reduction in class C&D waters, will be comfortably exceeded.

Historic environment

The historic environment is defined by the Public Appointments and Public Bodies etc. (Scotland) Act 2003 as any or all of the structures and places in Scotland of historical, archaeological or architectural interest or importance. These will include:

• Scheduled Ancient Monuments;

• Historic Buildings;

• Designed Gardens and landscapes;

• Archaeological sites;

• Townscapes;

• Historic landscapes; and

• The wider setting of the features listed above.

There are two world heritage sites within the study area: Edinburgh Old & New Towns and New Lanark. It is not anticipated that the ERDF Programme would be focused on these areas.

Scotland as a whole has a large number of listed buildings and conservation areas; around 45,000 and 650 respectively[7]. The vast majority of the listed buildings, just over 87% of the total number, are located within the study area.

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[7]Data collected from Historic Scotland website (www.historic-scotland.gov.uk)

The table below represents the ranking of local authority areas by number of listed buildings. Cumulatively this represents 50.8% of the total number of listed buildings within the Lowlands and Uplands area.

	No. of Listed Buildings	As % of Total for Study Area
Fife	4912	12.5
City of Edinburgh	4889	12.4
Aberdeenshire	3682	9.3
Dumfries & Galloway	3412	8.7
Perth & Kinross	3121	7.9

In addition to the above local authority areas, Scottish Borders, Angus, and City of Glasgow have a significant percentage of the total number of listed buildings within the study area: 7.6%, 5.5% and 4.7% respectively.

There are over 650 conservation areas in Scotland. Local authorities have a duty to identify and designate areas of historic or architectural interest. The designation aims to safeguard and enhance the sense of place, character and appearance of Scotland's most valued historic places.

Conservation Areas can include:

• building groups, where the whole is more than the sum of the parts;

• visible archaeology, such as historic street, plot layouts, and town walls;

• important set pieces of public realm (squares, railings, setted street surfaces);

• trees, rivers, lades, for both amenity and cultural value;

• open spaces, public parks, designed gardens and landscapes;

• places of memory, such as the Culloden battlefield.

Scotland as a whole has a large number of scheduled ancient monuments; around 7,786. The majority of the scheduled monuments, just over 61.9% of the total number, are located within the study area. The table below represents the ranking of local authority areas by number of scheduled ancient monuments. Cumulatively this represents 66.3% of the total number of listed buildings within the Lowlands and Uplands area.

	Scheduled Ancient Monuments	As % of Total for Study Area
Dumfries & Galloway	932	19.3
Perth & Kinross	751	15.6
Scottish Borders	723	15.0
Aberdeenshire	398	8.3
Angus	393	8.2

In addition to the above local authority areas, East Lothian (6.1%), Fife (5.4%), Stirling (4%), and South Lanarkshire (3.7%) contain a significant number of scheduled ancient monuments, shown as percentage of total within the study area.

Due to the scale of the study it has not been possible to identify all sites at this stage. It is envisaged that appropriate sites will be identified and considered in greater detail throughout future development of the programme.

Climate change

The global climate naturally exhibits long-term fluctuations. However, current trends are unlikely to be entirely natural in origin and there is evidence that human activities are having an impact. These bring wide-ranging implications for Scotland and could affect a whole range of aspects from flood risk, water resources, agriculture, tourism, habitats and species to health. In Scotland:

- 1901-2000 surface temperature rose by 0.61°C;

- By 2100, temperatures are predicted to rise by 3.5°C in summer and 2.5°C in the winter; and

- Rainfall patterns will change to considerably wetter winters and drier summers.

Carbon Dioxide and Energy Use

Emissions of carbon dioxide (CO_2) contribute to global warming. In 2002, Scotland emitted 44 million tonnes of CO_2 resulting from the production and consumption of energy. CO_2 can also be emitted from other activities such as land-use which disturbs peaty soils. Relative to 1990, overall energy consumption fell in 2002 by just over 2%, partly due to improvements in energy efficiency and the move towards less energy-intensive sectors, however, this has been largely balanced by the increased use of energy for transport.   High CO_2 emissions are concentrated in the main urban areas, where houses, traffic, businesses and factories are located.

Renewable Energy

The Executive is committed to having 18% of electricity generated in Scotland from a range of renewable sources, including biomass by 2010. This is to rise to 40% by 2020. By 2002 renewable contributions had increased by around 13% since 1990. This is primarily from existing hydroelectric generators but wind, newer small-scale hydro schemes and thermal renewable sources are beginning to contribute.

ANNEX G: EQUAL OPPORTUNITIES IMPACT ASSESSMENT

Background

1.   All public authorities in Scotland have a statutory general duty to promote Equal Opportunities and prohibit discrimination in the exercise of public functions under the Equality Act 2006. This means that listed public authorities must have due regard for the need to:

•   eliminate unlawful discrimination;

•   promote equality of opportunity, and

•   promote good relations between people with different equality barriers.

2.   In addition to the general duty, Scottish Ministers have used their powers to make a statutory order placing more specific duties on the Scottish Executive and other public authorities. The specific duties require these bodies to undertake an Equality Impact Assessment when introducing new policies, or changing existing policy in a significant way. This will entail:

•   assessing and consulting on the likely impact of the policies they are proposing to adopt;

•   monitoring any adverse impact of their policies;

•   publishing the results of their assessment, consultations and monitoring; and

•   ensuring public access to the information and to services arising from the Policy

3.   In recognising the duty, the European Structural Funds Division within the Scottish Executive needs to ensure that the implications of the changes proposed in the new round of European Structural Fund Programmes have been thoroughly assessed from all aspects of equality as part of the consultation and development process.

Deciding on the need for an Equality Impact Assessment

4.   All Departments within the Scottish Executive play a part in determining and contributing to Scottish Economic Development. Our approach is set out in the *Framework for Economic Development in Scotland.* This sets out an overarching vision to raise the quality of life of all the people of Scotland through increasing the economic opportunities for all on a socially and environmentally sustainable basis – and defines the Executive's economic objectives.

5.   From 2007 to 2013 Scotland will again benefit from European Structural and Cohesion Funds to support social and economic development. Agreement on the EU budget was finally arrived at in December 2005, and the share of regional aid for each Member State decided. With enlargement has come re-direction of EU funds towards the new Member States. Scotland, like many other Member States and regions of Europe, will receive significantly

reduced levels of funding which for the new programmes will amount to under half of the amount available under the previous 2000 to 2006 programmes..

6.   The reduction has required Structural Funds programmes to be more targeted than ever before, focusing not only on activities which have the highest value added, but also those which will leave an economic development legacy in Scotland post-2013.

7.   Consequently, following Scottish Executive guidance, we considered whether we needed to undertake an Equality Impact Assessment covering gender, race, age and disability aspects of equal opportunities.

8.   Although similar assessments were undertaken in England, Wales and Northern Ireland, only in Scotland did we decide to go down the route of a full Impact Assessment. The other regions decided that the underlying economic development policy had not changed and therefore no Impact Assessment was required.

The impact assessment process undertaken in Scotland

9.   The steps taken to assess the impact of the change in the new European Structural Funds Programmes were as follows:

i). **An Equal Opportunities Working Group** was pulled together to advise on the Scottish European Operational Programmes' content and the delivery mechanism. It met for a full day on 29 March 2006 at the Scottish Executive's Offices in Glasgow. The workshop attendees came from the Voluntary Sector, Ethnic Minority Community, Business, Academic, Local Authorities, Single Issue Groups and the Programme Management Executives for the 2000 to 2007 programmes. The actions arising are summarised below.

ii).   At its meeting on 26 April 2006 the **European Structural Funds Equal Opportunities Forum,** which meets twice a year to advise on equal opportunity aspects of the current programmes, was asked for a view on the outline of the new programme and the elements we should consider in an Impact Assessment. The actions arising are outlined in section 12.

iii).   As part of the **EQUAL Initiative's Good Practice Event** in Scotland on 13 September 2006 views were canvassed by the Head of the ESF Objective 3 Managing Authority on adverse impacts which emerging proposals for the new programmes might have on particular groups. The actions arising are outlined below.

iv).   **A joint meeting of the Equal Opportunities Forum and the Impact Assessment Working Group** was held on 22 November 2006 at the Scottish Executive Offices in Europa Building, Glasgow. This was timed to coincide with the formal consultation period which ran from October 2006 to 8 January 2007. This meeting mainly focussed on the Consultation from an Equal Opportunities view point with regard to the new Programmes. A series of questions, based on those in the formal Consultation were asked, which again

informed the final draft programmes and the delivery process. Representatives were invited from a wide range of equality groups in addition to the usual Equal Opportunity Forum members, however attendance was low. The reason for this may have been that there had been extremely good input from a wide range of bodies in the initial stages, and their views had been taken into account in the development of the draft which had been published and was then at the formal consultation stage. Some bodies may have preferred at that stage to enter a view as part of the formal process registering their input in that way.

v)   We therefore proceeded to contact those absent from the Forum and the Workshop in order to obtain their views and feedback from the questions relating to the consultation. We tried this in various forms, e-mailing, suggesting meetings at our offices or for us to go to their offices, asking for feedback either by telephone or by e-mail. Again the response was poor so we considered that we should approach some individuals to ensure we had a wide enough spectrum of views at this later stage. Further responses from the Disability Rights Commission and the Empower Theme B EQUAL Initiative Development Partnership were received, and these also informed the assessment.

vi)   The European Structural Funds Equal Opportunities Advisor produced a list of the key research documents which helped with the evidence base for some of the analysis incorporated into the early Operational Programme proposals.

Formal Programme consultation summary of responses on equal opportunities

10.   One of the items specifically consulted on from October 2006 to January 2007 was equal opportunities. 68 respondents addressed the issue of equal opportunities under Question 10.35:

i)   Of the 68 respondents who answered, 52 positively welcomed the approach to equal opportunities in the operational programmes or thought it was well integrated as a horizontal theme. Five felt that it was unclear how equal opportunities would be implemented or that they needed more information before commenting, in one case, referring to the forthcoming Equal Opportunities Impact Assessment being developed by the Scottish Executive. One respondent felt that it was not well integrated stating that the design of the delivery system at the outset of the process negated the impact of equal opportunities as a horizontal theme as many equality groups were supported by projects run by the voluntary sector which they felt may have more limited access to funds under future programmes. Eight respondents, while offering comments in response to the issue of equal opportunities, did not specifically comment on whether the principle was well integrated into the programmes.

ii)   A number of specific comments were made in relation to equal opportunities. These are summarised below:

- respondents felt that the programmes still placed too heavy an emphasis on gender equality and wanted more consideration of race and disability issues in line with recent legislation and public sector guidance. Specifically, it was also suggested by one respondent that ERDF Priority 2 should take account of access issues for disabled people when providing funding for refurbishment of learning and training centres. Another respondent also thought that the programmes failed to highlight the significant discrimination faced by disabled and the most disadvantaged groups in accessing learning and employment.

- It was suggested by four respondents that corporate social responsibility also be integrated as a horizontal theme, requiring businesses in particular, to provide employment to the socially excluded.

- A number of respondents emphasised the importance of the new programmes building upon the experience and expertise of the 2000-2006 programmes (seven respondents). In particular the importance of integrating equal opportunities into the application, evaluation and monitoring processes was highlighted by four respondents who emphasised that appropriate weighting should be given to the issue in the selection process. Two respondents also emphasised the need to continue the role of an equal opportunities champion to monitor progress in implementing equal opportunities into the programmes. Clear guidance and support would need to be available to ensure that organisations are aware of their responsibilities with regard to equal opportunities legislation, including the recent, Age Discrimination Legislation, and the impact this may have on project impact and delivery. One respondent suggested that the mid-term evaluation report should monitor equal opportunities and implementation and seek adjustments if no progress is being made.

- Two respondents welcomed the integration of equal opportunities but felt that this should not be pursued to the detriment of other good projects. One also suggested that this should be monitored to ensure that this was not funding "more of the same" from the current programmes.

- Ten respondents for the South of Scotland welcomed the integration of equal opportunities and highlighted that this was in line with the South of Scotland Competitiveness Strategy.

- One respondent felt that lack of spatial targeting could affect the implementation of equal opportunities.

- Finally another respondent referred to the approach under LEADER+ and suggested that equal opportunities should be built into an approach that also considers community and economic sustainability.

11.   All the above was discussed at an Equal Opportunities Steering Group, which consisted of the Chair and Secretary of the Structural Funds Equal Opportunities Forum plus officials from the European Structural Funds Division. This Group identified the equal opportunities issues which needed to be addressed in redrafting the programmes before the final proposals went forward to Ministers in March 2007.

So what changed because of the Equal Opportunities Assessment?

12.   First of all, in January 2006, when we were just starting to discuss the broad outlines of the areas on which European Regional Funds should be spent from 2007 to 2013, particularly in the Equal Opportunities workshop in March 2006, it was emphasised to us that equal opportunities had to be at the core of the new programmes. If we were serious about economic development and closing the opportunity gap going together, we had to build all aspects of equality in from the start. It should not be an add on, nor should a small piece of the funds be set aside to address equality issues, as Priority 5 had been in the ESF Objective 3 Programme for 2000 to 2006.

13.   Officials started off talking generally about funding going to disadvantaged individuals and groups. However, it was emphasised by a number of our contacts that, although it was important to fund projects which helped under-represented groups get into the labour force and progress and develop in the workplace, we should recognise in the wording used in the Operational Programmes that the barriers faced could be due to discrimination and ignorance as well as disadvantage or lack of skill. The early drafts took this point on board, not just in terms of wording, but also when thinking about the types of strategic projects which would be funded in the new programmes.

14.   There was early general agreement that Equal Opportunities should be a Horizontal Theme for each of the 4 Scottish Programmes. This meant that every project to be funded would have to show how it intended to address equal opportunities across all aspects of the project, including recruitment of beneficiaries, and access to the development or business opportunities provided. The other Horizontal Theme on which there was general agreement was Environmental Sustainability. However, during the Impact Assessment and the formal consultation period, it became clear that there was some reading of Equal Opportunities as being in effect Social Inclusion. Officials decided to make sure that the role of Equal Opportunities in the programmes was clear by adding in Social Inclusion as a third Horizontal Theme to be addressed, and the wording in Chapter 8 on Equal Opportunities was tightened up to make clear what was expected.

15. Monitoring of how the programme was performing to assist the under-represented groups who should be better represented in terms of the Programme funding was emphasised. It was clear that some of the previous programmes had had such a large number of projects running, that it had been impossible to gather satisfactory information to monitor performance for particular target groups. It was therefore important to ensure that the new

programmes had fewer, more strategic projects which were carefully monitored. Calls for projects aimed at particular sections of society, or groups of people facing specific barriers could then be made to ensure that minority groups were not overlooked because they had less expertise in accessing European funding when competing with other 'old hands'.

16.   There was general, but not universal agreement that larger more strategic projects were likely to have more impact on issues such as the pay gap, gender under-representation, and employer attitudes. However, most felt it was important for all partnerships to be covered by the Equalities Duty, including Community Planning Partnerships, and that again monitoring and evaluation of the equal opportunities aspects of all partnerships would be required. When putting local partnerships together specific action might be required by the new Intermediate Administration Bodies (IABs) to ensure that some smaller less engaged groups which may get a negative press are included where appropriate, for example groups working with those suffering from mental health problems, or gypsies.

17.   Some people commented that there was a need to move away from using case studies, instead identifying how organisations changed, what processes allowed these changes and in particular how attitudinal change was achieved in organisations. A key lesson to be learned is to build on individual commitment to equal opportunities and commitment at an organisational level to take equal opportunities forward beyond individual projects. The Equal Opportunities Adviser for the last programmes had prepared a Report looking at the processes and key elements of projects which are successful at mainstreaming equal opportunities, and this will still be used to revise the current Structural Funds Equal Opportunities Good Practice Guide. However, for the new programmes, Structural Funds Division will take more responsibility for ensuring that equal opportunities are addressed by having Champions for specific client groups and for the horizontal themes among the case officers with portfolios of projects to monitor.

18.   It was agreed that the reduced level of funding required more targeting of funds on projects which can make a real impact. A number of possible ways of targeting were proposed. The bulk of those taking part in the Equal Opportunities Impact Assessment were in favour of minimum project size, although they felt that £1 million would be too large as a minimum project size, and the final decision was to have a £200,000 minimum project size for the LUPS area, and none in the H&I area. They also thought that the funds should be aimed at those facing multiple barriers including discrimination, and needing significant help to contribute to economic development. Generally special targeting was welcomed, although there was a feeling that thematic targeting should also be considered – particularly mentioned were the young NEET group, ex-mining communities, low paid female workers, ethnic minorities and asylum seekers. The eligible areas for ESF Priority 1 and ERDF Priority 3 in the LUPS area should be those which are already prioritised by the Executive in strategies such as the Regeneration Policy Statement, Workforce Plus, Closing the Opportunity Gap, and the NEET

Strategy, and this was added into the operational draft Chapter 4. The key target groups in Chapter 4 were also revised to take account of some of these comments.

19.   Equal opportunities has become a key appraisal issue when considering which projects should be assisted. There will be more rigorous scoring of this element so that projects are not being assisted simply by making a good Equal Opportunities statement. Each project will be asked to benchmark itself at the outset of the project, and state where it will have moved to at the end of the project activity. It must show that it has built in equal opportunities as a key part of the project, and be able to show the sustainability of these changes in the organisation or partnership. Conditions could be added to the offer letter where appropriate requiring better monitoring of minority participation and the impact of the project on these groups. This will be monitored by the IAB during the project's lifetime.

20.   When the new operational programmes are approved and start, the Programme Monitoring Committee will be asked to consider having a new Equal Opportunities Forum with a more representative membership, and a reviewed remit.

21.   Projects based on the EQUAL Initiative model with a large Lead Partner and a number of smaller organisations delivering the activity will be encouraged by the IAB as these organisations often have excellent active equal opportunities policies. This could range from projects for a number of different voluntary organisations working with the same target group, to a project linking a number of ethnic minority organisations. To help with this process, for the first time, early expressions of interest will be sought from any group or organisation wishing to take part in the programme, and the IABs will work to ensure they can participate either in a partnership, or on their own if appropriate.

22.   Some additional eligible activities were added into the programmes in Chapter 4 as a result of the Impact Assessment. In particular, actions around acquired disabilities, and access to re-skilling to allow individuals who acquire a disability during their working life were added. This can be particularly needed for people who have mental health problems. Projects to educate employers to understand the needs of certain groups seeking to enter the workforce were also added as eligible, along with help for employers to adapt work for people who have suffered some change in health status.

Final steps in the process

23.   The final steps, on the basis of the information we gathered, were to amend and revise the Operational Programmes, the application and appraisal process, and the monitoring and evaluation plan for the programme period.

24.   This Equal Opportunities Impact Assessment will be published on the European Structural Funds Division website, and will be submitted to the

European Commission to form a part (in summary form) or our Operational Programmes.

25.   The Equal Opportunities Commission have requested a copy of this Impact Assessment and we look forward to their response which we will share with colleagues within the Scottish Executive to help them when they are undertaking similar processes.

26.   The IAB will be required to ensure public access through their websites, and through a full communications plan, so that all groups, whatever their interest, have access to information about the new programmes, and the evaluations carried out.

27.   The monitoring and evaluation plan will cover the gathering of information on groups being assisted. Quarterly progress reports will be submitted by projects and these will be checked against the targets proposed in their application, and against the programmes targets.

28.   As part of the annual implementation report which is approved by the Programme Monitoring Committee, sent to the Commission and published, we will produce a section on equal opportunities assessing the impact of the programme each year.

29.   Some comments were received about too much emphasis on gender issues, and also some comments against the targeted approach concentrating scarce resources on fewer areas and on larger projects. Although these comments were considered, and the underlying socio economic analysis revisited, it was decided that these aspects of the programme should not be amended.

32.   We made a few substantial changes in the new European Structural Fund programmes which we believe will improve the contribution they will make to economic development and equal opportunities for the people of Scotland. We also made a lot of small changes which may well be the most significant ones for the groups representing some of the most vulnerable individuals covered by these programmes, but who tend to be less vociferous and have less contact with the Scottish Executive.

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European Structural Funds Division
Scottish Executive

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ANNEX H: INDICATIVE BREAKDOWN BY CATEGORY OF ACTIVITY

The following tables set out the required indicative breakdown of activities for the programmed use of the Funds, employing the categorisation in Annex II Part B of the Implementing Regulation. The priority theme table has been used to calculate the Programme earmarking target in Chapter 4 (the shaded sections in the first table indicate earmarking categories). Allocations in the territorial dimension table reflect the urban targeting of Priority 3 and rural targeting of Priority 4. Allocations cannot be split further by area type as it cannot be predicted at this stage which areas will receive support.

Allocations between activities may change during the programming period and the figures below should not be used as targets.

Priority theme table			
Code	**Category**	**Allocation: %**	**Allocation: total**
1	R&TD activities in research centres	6.00%	22,568,845
2	R&TD infrastructure and centres of competence in a specific technology	6.00%	22,568,845
3	Technology transfer and improvement of cooperation networks ...	6.00%	22,568,845
4	Assistance to R&TD, particularly in SMEs (including access to R&TD services in research centres)	6.00%	22,568,845
5	Advanced support services for firms and groups of firms	6.80%	25,567,395
6	Assistance to SMEs for the promotion of environmentally-friendly products and production processes (...)	3.25%	12,219,517
7	Investment in firms directly linked to research and innovation (...)	4.88%	18,329,515
8	Other investment in firms	13.00%	48,878,667
9	Other measures to stimulate research and innovation and entrepreneurship in SMEs	12.18%	45,776,719
10	Telephone infrastructures (including broadband networks)	0.54%	2,037,692
11	Information and communication technologies (...)	1.08%	4,075,479
14	Services and applications for SMEs (e-commerce, education and training, networking, etc.)	8.53%	32,056,732
15	Other measures for improving access to and efficient use of ICT by SMEs	2.03%	7,632,435
26	Multimodal transport	1.35%	5,075,626
40	Renewable energy: solar	0.27%	1,015,086
43	Energy efficiency, co-generation, energy management	1.56%	5,850,198

50	Rehabilitation of industrial sites and contaminated land	3.24%	12,196,959
52	Promotion of clean urban transport	1.35%	5,075,626
55	Promotion of natural assets	1.02%	3,834,966
57	Other assistance to improve tourist services	1.36%	5,113,322
61	Integrated projects for urban and rural regeneration	11.15%	41,922,952
85	Preparation, implementation, monitoring and inspection	1.20%	4,511,789
86	Evaluation and studies; information and communication	1.20%	4,511,789
	Total	**100.00%**	375,957,844
	Earmarking	**78.93%**	296,752,749

Form of finance table

Code	Category	Allocation: %	Allocation: total
1	Non-repayable aid	80.00%	300,766,276
2	Aid	10.00%	37,595,784
3	Venture capital	10.00%	37,595,784
4	Other forms of finance	0.00%	0

Territorial dimension table

Code	Category	Allocation: %	Allocation: total
1	Urban	27.00%	101,508,618
2	Rural areas	13.60%	51,130,267
0	Not applicable	59.40%	223,318,959

ANNEX I: MAJOR PROJECTS

Access to finance project under Priority 2

Major projects are defined under Article 39 of the General Regulation: projects whose total costs exceeds €25 million. The scope for major projects in the 2007-2013 LUPS programme is likely to be restricted to ERDF Priority 2, and to focus on access to finance.

The Scottish Executive has given consideration to the JEREMIE initiative over the past 12 months. It has been closely involved with the European Investment Fund (EIF) in discussions on how the initiative might work in Scotland, and has been working with the EIF on the evaluation stage of JEREMIE in Scotland. At the time of writing, no firm decision has been taken as to whether to proceed to the second stage. Any such decision will depend on the value and costs to Scotland of doing so, and be informed by the evaluation work. If a decision to proceed with JEREMIE is agreed, then the amount of ERDF invested in the initiative will certainly make it a major project.

If a decision is taken not to proceed beyond the first stage of JEREMIE, we shall still want to invest substantial amounts of ERDF in other mechanisms to ensure the availability of finance for new and innovative SMEs in Scotland. ERDF would be made available to support a range of provision spanning the various early stage finance needs of SMEs. Consideration would be given to making ERDF awards to investor-readiness, to micro-credit initiatives, and to fill identified gaps in the finance market, such as risk capital, at higher levels.

Some of these schemes will of course be relatively small in scale. As discussed in the socio-economic analysis, the recent CSES evaluation of venture capital and loan funds in Scotland has, however, identified continuing market failure both at the level covered by the Scottish Co-investment Fund and above. Regardless of whether JEREMIE moves to stage 2 or not, the evaluation stage is also expected to provide further evidence of the need for ERDF involvement in venture capital schemes in Scotland.

The Scottish Co-investment Fund (SCF) has proved to be a powerful catalyst for stimulating private investment and also a valuable mechanism for assisting young and innovative SMEs to gain access to capital for development and expansion. Despite an investment deal limit of £2 million, it is anticipated that demand will continue at a level that will not be met for some time by realization of current investments. It is proposed that if JEREMIE does not proceed, a very substantial further ERDF investment that would qualify as a major project should be made in the SCF from the new programme. A higher deal level (£2 million – £5 million) is covered by the new Scottish Venture Fund which has not yet received ERDF support, but which has already made an initial investment and would be usefully enhanced by the award of ERDF. Although the level of an award to the Scottish Venture Fund may not be on the scale we would propose for the SCF, it would still be substantial and could also qualify as a major project.