1.0 SCOPE

To attract support for the 2007-2013 European Regional development Fund, projects must be eligible in respect of the criteria set out in the:

- West Midlands ERDF Operational Programme;
- relevant European Council and Commission Regulations; and
- National Eligibility Rules, as set by the Department for Communities and Local Government (CLG) in their role as the Managing Authority.

The European Commission and the European Court of Auditors have emphasised the need to strictly comply with the eligibility criteria associated with the Structural Funds Programmes. Failure to do so has led to financial penalties of up to a 100% of the grant.

If the Commission consider that there has been systemic failure on eligibility issues, they are empowered to enforce a flat rate correction to a whole Programme. Where the Agency considers there has been systemic failure within a project, we will be required to enforce a flat rate correction to reduce or stop that project’s funding.

This guidance should be used by all applicants for ERDF funding to determine the eligibility of their application and to assist them when making claims.

This guidance should also be used by Project Sponsors, Appraisers and Project and Contract Managers to ensure that applications and claims for funding are eligible and appropriate in the context of the Programme.

The main body of this guidance is taken directly from the national ERDF User Manual. The national ERDF User Manual has been produced and agreed by the RDAs and CLG, its main purpose being to ensure a consistent interpretation and application of the ERDF rules and regulations across all of the English Programmes.

The information in this guidance note comes from Chapter 2 (Eligibility) of the ERDF User Manual, which is reproduced in its entirety at Appendix 1. It should be read and used in conjunction with all other relevant guidance.

2.0 PURPOSE

The purpose of this document is to ensure that the eligibility rules are strictly adhered to by a project throughout the whole project lifecycle, monitored effectively by the Agency and the appropriate corrective actions are taken when breached.

If there is any doubt regarding any aspect of ERDF eligibility at any point, the Agency’s European Programme Management Team (EPMT) must be consulted.

The changes from previous programme, or previous versions of the rules are as follows:

- Location of project, whereas in the previous programme it was possible to make a case that a project taking place outside of the region could be eligible because the majority of the benefits would be in the region, now, if a delivery organisation is outside of the region it must be demonstrable that all the benefits of their activity are for eligible beneficiaries within the region.
Additionality and Substitution rules prevent substituting ERDF for substituting for national funds. In the current economic climate, the Commission has given a clarification on this which has allowed limited support to be given to projects previously intended to be supported by public bodies, but for which no budget is no longer available, where this has been agreed by the Programme Monitoring Committee. Please consult with EPMT should you wish to support a project in this category.

State Aid. The Agency has adopted a number of bespoke state aid approved schemes to cover this activity. Please consult with the Technical Assurance Manager on the best State Aid fit for your project in the early development stage.

Procurement. The procurement procedures followed should be those of the Agency, or if the applicant organisation’s rules are stricter these may be adopted in agreement with the Agency.

Eligible final beneficiaries (applicants) for ERDF may only be private sector if it can be demonstrated that they will not themselves benefit from the funding. This prohibition includes organisations in the voluntary sector.

Match funding may be provided by named partners in the form of staff time on the project. Backfilling of posts is no longer required, but they must be able to demonstrate that the work is additional to the normal activities of the relevant staff.

Private sector match funding is now permissible, but only in restricted circumstances which are now outlined.

Contribution in kind is only eligible in the case of the donation to the project of land or buildings (or in the case of the staff time previously mentioned). Importantly, as long as the donor is a named partner in the project, title of land or buildings does not have to pass, it just needs to be dedicated to the project for 20 years.

Volunteer or beneficiary staff time is no longer eligible as match.

The guidance now contains definitions of when match is considered to be public or private.

The guidance is now split into capital and revenue with different applicable rules in each.

It should be noted that in the West Midlands Operational programme, capital projects are only permissible for a few demonstrators in Priority 1, financial engineering instruments in Priority 2 and 3 and some limited capital projects in Priority 3, please consult the relevant priority managers before undertaking a project of this type.

Retrospection. Even within these guidelines, retrospection will only be permitted in limited circumstances and the EPMT must be consulted if retrospection is considered necessary for the project.

The project start date can now be from the date of the financial approval (IDG decision at full).

Defrayal. In the case of a consortium, this may now be taken at the level of named consortium partners, not just at the level of the applicant for funding.
There is a major change in terms of revenue generating projects, and any project where the asset supported could be sold, or the users of the asset or service will be charged must consider the separate guidance ADV-GN39 on Art 55 Revenue Generating Projects.

Workshop units and managed workspaces may now be occupied by any company eligible for the programme not just SMEs.

Day nurseries are now eligible where they directly relevant to eligible activity under the operational programme.

The prohibition on support to retail facilities has been strengthened.

Preliminary expenditure of certain types is now eligible in capital projects, but not in revenue projects.

Guidance has been added on environmental impact and on travel to work plans. Most the activities outlined are not eligible for the West Midland operational programme.

There has been a major change in the methodologies used for overheads (indirect costs). Please consult the Overheads guidance ADV-GN 38 on this.

Every applicant organisation is expected to fully have the ability to deliver the project at time of application. Therefore, staff training costs are only permissible if there have been changes to the regulation or procedures during the lifetime of the project which could not be foreseen. Normal organisational training or CPD is not eligible.

Various taxable benefits are now permitted where a contractual requirement of the organisation.

Redundancy payments are now eligible in this programme.

The prohibition on claiming depreciation or the use of assets which were previously supported by national funding has been lifted and the restriction now only applies to ERDF supported assets.

Eligibility of businesses does now include large companies where permitted in the operational programme. The West Midlands operational programme only permits 4% of beneficiaries to be large companies which fulfil the following criteria:

- The project relates to or will result in the improvement of supply chain, knowledge transfer, innovation or implementation of environmental technologies;
- The project falls within one of the ten priority business clusters;
- The project will aid diversification, modernisation, innovation, adaptation to climate change and access to new markets;
- The project will not result in the relocation to the assisted area of economic activities carried on within an EU member state."

As this is an extremely limited derogation, please consult with the EPMT team should you wish to support large companies.
Revenue support to retail businesses is generally not permitted. Agreement has been reached with national authorities to allow the use of retail to support projects in the following priority actions:

- Dedicated support, advice and mentoring to those groups that face barriers to creating sustainable businesses, such as women, certain Black, Minority Ethnic (BME) groups, and the disabled. This would include investment readiness support to help these particular social groups to raise finance.

- Address the low rate of business formation prevalent in areas of multiple deprivation which are concentrated within the two major conurbations, neighbouring districts and the more isolated and remote rural areas. Access to micro finance and business support activity will be available for start up and early stage businesses in these areas, including social and community enterprises.

Please contact the EPMT team if you wish to support retail businesses.

- Motor vehicle manufacturing is no longer an excluded sector.

- There are special rules on financial engineering which are contained in ADV-GN this requires a two stage approval process involving agreement of CLG and BIS. This is a time consuming process and sufficient time should be factored into the planning of any financial engineering instruments.

### 3.0 RELATED DOCUMENTS

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1. INTRODUCTION

- To attract ERDF support, expenditure by projects must be eligible in terms of the Operational Programme (OP), the relevant EC Regulations and the National Eligibility Rules. In the past, the Commission have set out the eligibility rules but under the Regulations for 2007-2013, they “shall be laid down at national level subject to the exceptions provided for in the specific Regulations for each fund”. ERDF eligibility rules apply to all project spend included in the eligible costs, although projects can also include ineligible spend provided this is not used to match fund ERDF. Particular rules apply to Financial Engineering Instruments (FEIs) such as Venture Capital and Loan Funds and Urban Development Funds, as set out in Section 8 of the Implementing Regulation, (EC) Regulation 1828/2006. Chapter 15 of the User Manual provides detailed guidance on these instruments and where appropriate this chapter highlights where the national rules for FEIs are different from the general national eligibility rules.

- Audits on previous programmes by the European Commission and the European Court of Auditors have emphasised the need to strictly comply with eligibility rules. Failure to do so has led to financial penalties of up to a 100% of the grant. If the Commission considers that there has been systemic failure on eligibility issues, they could enforce a flat rate correction to the whole of a Programme.

- It is important to ensure therefore that the rules are strictly adhered to both during the project selection process and after approval. If there is any doubt, the Department for Communities and Local Government (DCLG) should be consulted. Eligibility rules applying to other sources of match funding (for example RDA Single Programme) cannot be used to justify departure from ERDF eligibility rules. However, it is important to note that the majority of cases of clawback of ERDF grant from projects (irregularities) have occurred not because of eligibility issues but as a result of failure to adhere to correct procurement (open and competitive) rules, incorrect application of apportionment methodologies, failure to provide a clear audit trail back to original invoices and/or lack of acknowledgment of ERDF support (publicity). Guidance on procurement is contained in Chapter 17 of the User Manual and guidance on audit trail requirements is in Chapters 4 and 8.

2. THE NATIONAL ELIGIBILITY RULES

- The national rules cover the eligibility of expenditure for ERDF support. Operations must comply with EC Regulations and satisfy the eligibility criteria and rules before they can be approved for grant. If an approved project does not comply, financial penalties up to the total value of the grant approved will be imposed. The national rules also give examples of ineligible activities. ERDF Regulation 1080/2006 also describes ineligible activities.

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1 Article 56(4) of Regulation 1083/2006
3.1.1 Applicability

- These rules apply only to English ERDF Convergence and Regional Competitiveness Operational Programmes. The eligibility rules for 2007-13 territorial co-operation programmes will be subject to discussion with the other Member States involved in the programme.

3. LEGISLATIVE BACKGROUND

- The following EC Regulations set out the Commission’s legislative rules on programme and project eligibility:

3.1.2 General Regulation 1083/06:

- Article 55 sets out the rules on the eligibility of expenditure on revenue generating projects. This is addressed in detail in Annex G of this guidance.

- Article 56 states that:
  - eligibility rules shall be laid down at national level;
  - the eligible period for expenditure commences on the date of submission of the OP, or 1 January 2007, whichever is the earlier; and
  - contributions in kind, depreciation costs and overheads are eligible if the national rules allow for them.

3.1.3 ERDF Regulation 1080/2006:

- Article 7 lists the following ineligible expenditure: interest on debt; purchase of land exceeding 10% of eligible expenditure (except for environmental projects); decommissioning of nuclear power stations; recoverable VAT; expenditure on housing, except for those Member States that acceded to the EU on or after 1 May 2004. Article 7 has subsequently been amended by Regulation (EC) No 397/2009 to allow Member States to spend up to 4% of their total allocation on energy efficiency improvements and renewable energy in existing housing.

4. NATIONAL ELIGIBILITY RULES APPLYING TO ALL ERDF EXPENDITURE

3.1.4 Basic principles

- All ERDF funded projects must.
  - be located in the eligible area;
  - contribute to one or more of the programme objectives;
  - identify and provide details of clear and attainable targets;
  - demonstrate an additional and sustainable benefit to the socio-economic development of the area;
  - have a sound funding package in place, identifying the recipient of the funds and the sources of match funding;
• not duplicate existing activity, but could extend such activity;
• not be a substitute for existing or planned domestic expenditure;
• respect State Aid rules; and
• follow public procurement rules where applicable.

- Project selection criteria will be agreed at an individual programme level by the Programme Monitoring Committee (PMC). The basic principles are explained in more detail below.

3.1.5 Location of project

- As a general rule, activity funded through ERDF must be located within the relevant programme area. Whilst a project delivery organisation could be located outside the programme area, it must be able to demonstrate that all the outputs, results and impacts are delivered in and impact upon on the programme area. Auditors would expect to see evidence that this is the case for example, records of details of businesses including their postcodes that have been assisted.

- In the event that a project assists a business outside an eligible area, on the understanding that the business will relocate into the eligible area as a result of the assistance, and the business subsequently fails to do so, all expenditure relating to that business assist must be removed from the next ERDF claim and the costs deducted from the total eligible cost of the project through an offer letter variation. Because of this risk, it is strongly advised that such investments are not made in the first place. Very exceptionally a project outside the eligible area could be considered provided (a) the project is situated in a NUTS III area (EUROPA - Eurostat - Regions - Home Page) adjacent to the programme area, (b) the results and impacts will be delivered within the programme area and (c) meets the PMC agreed selection criteria for the programme. An example of such a project would be investment in a university business support project where the businesses assisted are located within the programme area but the businesses travel to a university outside the programme area for the support.

3.1.6 Contribution to programme objectives

- The project must be in line with the particular objectives of the programme to which it is applying. Departure from these objectives would first have to be agreed by the Programme Monitoring Committee and by the Commission as a formal programme change. Activity and associated costs funded through such as change would be eligible only once the change had been agreed.

3.1.7 Outputs and results

- Core ERDF outputs and results are defined in the “Combined Technical Note on RDA Core Outputs and ERDF Programme 2007-13 Indicators”, contained in Chapter 11 of the User Manual Where a programme has decided to utilise indicators that are not in the Technical Note, these will be defined locally.
3.1.8 Additionality/Added Value

- This is a fundamental principle of ERDF. Projects should add value to new or existing activity; projects need to demonstrate that the activity would not have taken place without ERDF support. ERDF cannot be used for, or substitute, existing or planned domestic expenditure. If applications do not demonstrate “additionality” they will not be successful. Adding value does not have to mean additional activity as such. Maybe the project would go ahead but on a smaller scale or to a lower quality or for less time. This should be clearly demonstrated in the project application.

3.1.9 Sustainability

- In this context, sustainability is the prospect of the benefits of the project continuing after the period of ERDF subsidy. In the context of capital projects, it is important that the building will continue to be viable once the funding has ended by generating sufficient income to cover running costs. However, some projects, for example business support, may not continue to offer the service once funding has ceased and this is acceptable provided the project has demonstrated a clear exit strategy.

3.1.10 Duplication/displacement/ substitution

- It is important that projects are able to demonstrate that ERDF is not being used to substitute for other public funding streams, although it is reasonable to use ERDF to augment these funding sources. As well as being additional, ERDF funded activity should never displace or compete with other publicly funded activity in the programme area.

3.1.11 State aid

- All projects must be compliant with state aid rules. Further information can be found on the Commission’s DG Competition website at http://ec.europa.eu/comm/competition/state_aid/overview/index_en.cfm and information and advice can be sought from the BIS State Aid Branch – www.bis.gov.uk/bbf/state-aid. Further guidance on the procedure for dealing with State Aid issues that arise in connection with the grant of ERDF support is contained in User Manual Chapter 17 on Procurement and State Aids.

3.1.12 Procurement

- The rules on public procurement are complex and can be found in more detail in User Manual Chapter 17, on Procurement and State aid. Further guidance on procurement can be found on the OGC website at www.ogc.gov.uk/GPS.asp.

3.1.13 Eligible final beneficiaries

- The final beneficiary of the ERDF grant is the organisation that applies for and is subsequently awarded the grant under the conditions set out in the Funding Agreement. Organisations that can apply for funding include local authorities,
statutory or non-statutory public funded bodies, voluntary/community organizations and some private sector organisations (subject to state aid compliance). All organisations must be legally constituted.

- The final beneficiary can recover defrayed costs which are eligible and have been paid by the final beneficiary to implement the project. These are the actual cost of the works or services plus overheads. ERDF is not paid for an organisation’s own benefit. Only actual costs should be included and must not include any profit.

- Consortium partners who are responsible for implementing and controlling specific elements of a project are also treated as final beneficiaries.

- Private, profit-making organisations can also act as sub-contractors. The final beneficiary would need to follow appropriate procurement procedures and a legal contract agreement would need to be in place between the final beneficiary and the subcontractor.

- In some projects, the final beneficiary may ‘pass on’ the grant to SMEs (end beneficiary) who may use the ERDF grant to procure goods, services or works (e.g. under VCLF schemes). End beneficiaries are not subject to the same eligibility rules as final beneficiaries, eg around procurement, though the final beneficiary will need to be satisfied that the funds have been used for the agreed purposes under which the grant was given.

3.1.14 Match funding

- Except in certain circumstances where projects are matched at Priority rather than project level, ERDF will not be the only source of funding for a project. Before an offer of grant can be given, there must be sound evidence that the remainder of the funding package is in place. Evidence for this should be provided in the form of letters of commitment from other funding partners. **All match funding must be spent in accordance with the ERDF eligibility rules.**

- Most of the match funding will take the form of cash payments that will go through the accounts of the project applicant and deliverer. However some match funding may be made available by partners in the form of cash payments that are included in their accounts - for example, the salary of a member of their staff who is seconded or assigned to the project and for whom evidence of the cost can be provided. In this case, evidence of the cost must be provided on an ongoing basis e.g. timesheets along with salary costs and associated supporting accounting records to show payment transactions. There is no requirement to evidence that a seconded or assigned member of a staff in an organisation has been back-filled, provided they are involved in additional activity.

- **Private sector match.** The following advice applies only to those programmes with private sector match funding included in their financial tables. If private sector funding is included in the programme, contributions from companies can be included in the funding package, provided these will contribute towards the total eligible costs of the
project and can be audited to the same standards as other funding sources. It is anticipated that private match contributions could be accounted for by either (a) providing evidence that a cash payment has been credited to the project sponsor’s account, (b) in the case of private organisations seconding staff to a project by providing appropriate evidence as outlined in 4.18 above; (c) providing evidence that part payment for a service or activity being delivered as part of the project (and which will have been procured in line with procurement requirements) has been paid by an end beneficiary SME. For example, this could be the provision of an invoice from the service or activity provider to the project sponsor, recording:

- the gross amount as the full cost of the service or activity,
- the contribution by the SME and and the net amount payable by the project sponsor (ie the gross amount minus the SME’s contribution) and evidence of payment of the SME’s contribution.

The requirements for accounting for private sector match funding in Financial Engineering Instruments are different and are referred to in Section 7, but set out more fully in User Manual Chapter 15.

- The actual salary costs of professional services, associated with the management and delivery of the project, e.g. legal and accounting services (but not legal and/or accounting costs dealing with litigation), environmental assessment work, publication and publicity activities or independent evaluation could also be captured as match funding as long as there is robust evidence of the actual costs.

- The activity supporting the match funding must clearly be part of the activity of the ERDF project. For example, match funding relating to improving open spaces cannot be used to match a project which supports promoting innovation within businesses.

- The project’ is the ERDF grant and match funding combined. Therefore, all aspects of the project must be eligible for ERDF and deliver ERDF outputs. ERDF pays for a proportion of all the project’s activities.

- Contributions in kind are ineligible for ERDF, except for the donation of a building or land, where a clear valuation can be made.

- The freehold or leasehold of land or real estate is eligible as an in kind contribution to the project as long as:-

  a. the value of the freehold or leasehold at the time of full application has been independently valued and supported by a certificate from an independent qualified valuer or duly authorised official body

  b. the certificate states the current market value at the time the contribution is claimed
c. the value given to in kind match funding provided in the form of land is restricted to a maximum of 10% of the total value of the project, ie its eligible value is capped by the same rule which applies to the purchase of land. Note – the 10% cap does not apply in the case of building valuations as contributions in kind, but the value of the building must be the present value, not the value after completion of the project. The Commission has ruled that this restriction does not apply in the case of urban development funds utilising JESSICA\(^2\).

- Discounted sales of equipment, the provision of volunteers’ time, the discounted provision of services or advice (eg solicitors’, accountants’ or SME staff time) are ineligible.

3.1.15 Definition of public match funds

- A public match funder is an organisation which directly or indirectly receives over 50% of its main funding from central or local government. (This does not include payment for work carried out by private enterprises for the public sector.) To decide if an organisation can supply public match funding, work out their previous financial year’s receipts, excluding any EU monies, and the income forecast for the following year, again excluding any EU monies. If over 50% of the net amount (after deductions) comes from central or local government sources, they are able to provide public match funding for ERDF supported projects.

- Non-profit making organisations, whether incorporated or unincorporated, registered with the Charity Commission can supply public match funding. The registration must be maintained throughout the period of the ERDF project. Public match funding can also be provided by private bodies designated or controlled by the State.

3.1.16 Definition of private match funds

- For ERDF purposes, private match funds are defined as any money originating from private enterprise, including:
  
  - public limited companies;
  - private limited companies;
  - partnerships which have no shareholders;
  - social enterprises;
  - co-operatives;
  - self-employed people; and
  - individual investors.

\(^2\) JESSICA is the acronym for the Joint European Support for Sustainable Investment in City Areas initiative. It is focussed on improving access to finance for public/private partnerships and other projects aimed at urban regeneration rather than on access to finance for SMEs.
3.1.17 Retrospective Projects

- All retrospective projects must:
  - include only spend from 01 January 2007 at the earliest and have a project completion date beyond the date of approval;
  - demonstrate that ERDF investment formed part of funding assumptions (i.e. does not displace other funding and the project would not have gone ahead if ERDF wasn’t assumed);
  - have a full audit trail to demonstrate that retrospective activities and associated spend are fully eligible for ERDF;
  - meet the selection criteria for the Programme and be subject to a rigorous ERDF Technical Appraisal;
  - demonstrate value for money;
  - provide evidence to identify the need for the ERDF;
  - provide documented evidence that the project was running ‘at its own risk’ until the approval of ERDF funding; and
  - the project must meet all EC regulatory requirements - in particular, the audit/financial control standards set out in Regulations (EC) 1080/2006 and 1083/2006, procurement and state aid rules and EC publicity requirements.

- It is also possible to apply the retrospective principle to capital projects which are ongoing and which have incurred certain specific eligible expenditure that predates the Offer of ERDF grant (see paragraph 5.20 on ‘Preliminary expenditure’).

3.1.18 Project start date

- Except in the case of retrospective projects, expenditure on ERDF activity cannot be incurred (i.e. spent by the project) until the ‘Start Date’ specified in the ERDF funding agreement. This should be the date of financial approval, not necessarily the date the funding agreement is signed. Financial approval is the date it is endorsed by the relevant PMC, Partnership Board or sub committee or the date it receives financial approval by the RDA as defined in its management and control document. The project must be able to support a full ERDF audit trail from this date. To ensure this, the relevant RDA European team should write to the project sponsor immediately after the project has been endorsed informing them of the start date and that a funding agreement will be issued as soon as possible.

3.1.19 Defrayal of expenditure

- ERDF can only be claimed on expenditure that has actually been paid (with the exception of inclusion of flat rate indirect overhead costs. Guidance is contained in Annex A). For the purposes of ERDF “paid” is interpreted as actually having left the bank account of the final beneficiary, and evidence of this can be required by an auditor (in the form of bank statements). Receipt of an invoice is not sufficient evidence that it has been paid. In the case of consortia bids for funding with one lead partner, expenditure that has actually been paid by any of the named partners in the
bid can be included in the ERDF claim from the lead partner, provided the partners are named in the offer letter.

5. ELIGIBILITY RULES APPLYING TO CAPITAL EXPENDITURE

- There is a wide range of infrastructure provision which can receive grant and individual programmes will have specified the types of capital development permitted in a programme. There must be a clear and demonstrable link between a project and the industrial or economic development of the Programme area. The project must also show that it will lead to a genuine improvement of facilities.

- It is important to note that where investments in infrastructure are included in Programmes (such as the creation of sites of strategic importance), that neither the businesses invested in (grant recipients) nor the occupants/users of the infrastructure being funded (end beneficiaries) need be SMEs, as the restriction noted above does not apply to infrastructure schemes. Instead, in infrastructure investments, it need only be shown that the site created benefits the local economy, providing the necessary jobs to improve the area etc.

- However, there is a significant change from previous ERDF regulations in how revenue generating investments are treated. The majority of buildings supported through ERDF will generate income. Any net income received from rents or entrance fees (after running costs are taken into account) will have to be deducted from the total eligible cost before the level of ERDF grant is calculated. It is essential that the guidance on this rule (Article 55 of the General Regulation) as set out in Annex G is followed.

- Projects must define costs under the capital expenditure categories set out in the text box below for the purposes of grant claims.
Projects must define costs under the following capital expenditure categories for the purposes of grant claims

**Land acquisition**
The cost of purchasing land which is not built upon may not exceed the limit of 10% of the total eligible project costs. A higher percentage may be permitted by the managing authority for operations concerning environmental conservation.

**Building acquisition**
The cost of acquiring a building if there is a direct link between the purchase and the objectives of the project.

**Site investigation**
This should take account of specialist investigations required to identify contamination and recommended particular treatments.

**Site preparation**
This should include demolition works and the general preparation of sites.

**Building & construction**
This should include external/internal refurbishment and conversion of existing buildings, new build premises, provision of services, and landscaping.

**Plant & machinery**
This should include tangible fixed assets used for the purpose of providing a service for the project. If plant and machinery is subject to hire/lease purchase agreements, the capitalised value of leasing and hire purchase can be included. The purchase costs of second-hand equipment are eligible provided they meet the needs of the projects and have not been purchased with the aid of national or community grants.

If there are any mobile or portable items then an apportionment of costs should be provided separately.

**Fees**
This should include fees and salaries for design and supervision but professional fees should not normally exceed 12.5% of the total eligible works costs. Fees include legal consultancy fees, notarial fees, and the cost of technical and financial experts if they are directly linked to the ERDF operation and are necessary for its preparation or implementation.

**Other Capital**
Any eligible capital expenditure not covered by the categories above provided it can be clearly demonstrated that these are directly related to the delivery of the project. This may include expenditure through financial engineering instruments.
Eligible capital costs

- Listed below are examples of some of the types of capital projects which are **eligible** for support under the 2007-13 round of programmes, although the list is by no means exhaustive:

- **Small scale transport investment** including: major transport infrastructure, such as airports, railways, bridges or major roads will be ineligible in Competitiveness programmes, but can be supported under the Convergence programmes if there is provision in the OP. Promoting clean and sustainable transport, particularly in urban areas is specifically supported in Article 5 2(d) of the ERDF Regulation. Examples of eligible transport improvements are bus priority measures, park and ride, bus/rail interchanges, cycle lanes and pathways, community transport schemes, and publicity and signage. Inclusion of small scale travel improvements with a direct linkage for people/communities to new jobs is also eligible. However, vehicles are not eligible for ERDF in any circumstances. Where they are integral to the project, the provision of access roads to new business and/or R&D facilities supported by ERDF are also eligible.

- **Infrastructure** such as: sewerage, drainage and flood protection works associated with the provision of eligible activities such as business and R&D premises.

- **Landfill waste disposal sites** can receive assistance where all or part of the waste is from industry, provided that the site will ultimately be returned to open space or agricultural use after completion of tipping and remains in public ownership.

- **Tourist infrastructure projects** designed to attract or retain visitors from outside the area and which will sustain or generate local jobs and revenue by, for example, increasing the use and/or provision of hotel bedrooms. **Facilities which primarily serve local people are not to be encouraged and evidence of expected use by visitors from outside the area is essential.**

- **Workshop units and managed workspace** can receive ERDF support where they are to be occupied by eligible companies and/or organisations.

- **Brownfield land clearance.** The land reclamation and associated works are eligible for ERDF grant where they are consistent with the programme. Comprehensive applications covering reclamation, site servicing and preparation for final use are preferred to separate applications covering different aspects of the work. In cases where reclaimed sites are to be sold or leased to the private sector, local authorities must certify that land will be disposed of at a market value rate for unspoiled land.

- **Environmental capital works**, particularly where they are linked to biodiversity and investments in **NATURA 2000** sites can be assisted if they are part of a project

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1 Natura 2000 is the European Union-wide network of protected areas, recognised as ‘sites of Community importance’ under the EC Habitats Directive (Council Directive 92/43/EEC on the conservation of natural habitats and of wild fauna and flora). The Natura 2000 network includes two types of
contributing to the economic development of the programme area, such as improvement of town centres and other prominent sites or buildings.

- **Infrastructure projects for R&D, training and business development** where not covered above, are also eligible for support within the terms of the Programme.

- **Day nurseries**, where they are directly related to an eligible activity under the OP.

- The following are **ineligible** for ERDF support:
  
  a. Provision of local social welfare facilities eg hospitals, nursing homes, fire stations, child-minding facilities, sports facilities, parks, public libraries when these are not directly related to the objectives of the Operational Programme.

  b. **Mobile infrastructure** such as buses and boats cannot be funded with ERDF because of the possibility that the asset will be removed from the Programme eligible area and difficulties in ensuring that it will be used solely for the project.

- Note also that the following activities are not normally eligible:
  
  a. **Retail facilities.** The general principle is that support for retail facilities will not assist economic development and that improved performance for one facility will displace similar activity elsewhere.

  b. **Coastal protection, soil conservation and infrastructures;** all with an exclusively agricultural bias, reforestation and prevention of forest fires, insofar as such infrastructures can be financed under EAFRD.

- That proportion of public expenditure incurred in land acquisition not directly linked to productive investment or investment in infrastructure.

- Building and renovation of housing, except for energy efficiency improvements and renewable energy. Annex E of this Chapter advises on how this will be implemented in accordance with Regulation (EC) No 397/2009.

- **Major infrastructure in ports,** on the grounds that port developments and port operations should not need public subsidy. Furthermore, it could distort competition between ports. Subsidy tends to spread the problems caused by excess capacity and can be damaging to otherwise healthy neighbouring ports.

### 3.1.20 Preliminary expenditure for capital projects

- Capital projects can include preliminary expenditure to cover the costs of site investigation works, site surveys, environmental appraisals and/or feasibility studies. **These must be identified in the full application and form part of the original**
grant offer. Appropriate milestones and outputs should be identified to enable any subsequent re-assessment of the application to establish if the project remains viable. Costs for preliminary expenditure must be included in the first claim for grant.

Additional rules for supporting premises for enterprises

- The following rules apply to ERDF support for the development of premises for enterprises:
  
  - the rent requested from the tenants must be at the prevailing market rate in the area, unless a lower rate is compatible with State Aid rules.
  
  - the premises should not be constructed to meet the specific requirements of a single user for the economic life time of the investment.
  
  - activities which enable the creation or maintenance of permanent jobs are eligible as tenants.

  - demand within the programme area, in terms of size and type of premises, must be demonstrated either by evidence of market failure in the eligible area, full occupancy of similar units in the area or by enquiries from potential occupiers.

  - it must be recognised, however, that it may be difficult to judge beforehand the type and size of companies that will move into the site. If the applicant is unable to give clear assurances, such factors as previous usage - if the site is being modernised, the facilities being made available and the type of location will need to be considered. This will need to be judged at the appraisal stage, but in many cases the outcome will need to be checked during monitoring.

3.1.21 Environmental Impact

- All ERDF projects must consider the impact of their activity on the environment to comply with EC Environmental legislation, which seeks to ensure that projects do not have any adverse environmental effects. For some projects an Environmental Impact Assessment (EIA) is required. If this is the case, planning permission cannot be granted until an EIA has been carried out. Applicants are therefore advised to consult the local planning authority at an early stage as possible where there is any question of an EIA being required. DTLR Circular 02/99 provides guidance on EIA procedures. Further guidance on environmental protection can be found on the DEFRA website at www.defra.gov.uk/environment/index.htm

- Projects must also identify whether their project will operate in, or impact upon, designated areas; a NATURA 2000 Designated Site, an Area of Outstanding Natural Beauty, a National Nature Reserve, a Site of Special Scientific Interest, a Scheduled Ancient Monument or Listed Building, a National Park or any other designated area.
• All projects involving major physical development\(^4\) will also be required to produce the following:

  - Biodiversity Audit (using the Regional Biodiversity Audit)
  - Long-term environmental management plan
  - Local labour strategy
  - Employment strategy
  - Transport Impact Assessment.

### 3.1.22 Travel Plans

• A travel plan is a strategy for managing access to a site or development. It considers how all forms of transport can be influenced using a combination of measures, both physical and behavioural. There is an emphasis on reducing resilience on single occupancy car use and increasing travel choice. Travel plans usually focus on the journey to and from work, but can also include business travel, travel reduction, fleet management, visitors and delivery vehicles.

• DCLG Planning Policy Guidance 13: Transport (PPG13) requires that Travel Plans should be submitted alongside planning applications which are likely to have significant transport implications:

  - All major developments comprising jobs, shopping, leisure and service (using thresholds defined in Annex D of the document);
  - Smaller developments which would generate significant amounts of travel in, or near to, air quality management areas and in other locations where there are local initiatives or targets set out in the development plan or the Local Transport Plan (LTP) for the reduction of road traffic, etc.
  - New and expanded school facilities; and
  - Where a travel plan would help address a particular local traffic problem associated with a planning application, which might otherwise be refused on local traffic grounds.

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\(^4\) Under The Town and Country Planning (General Development Procedure) (Amendment) (England) Order 2006 “major development” means development involving any one or more of the following—

(a) the winning and working of minerals or the use of land for mineral-working deposits;

(b) waste development;

(c) the provision of dwelling-houses where—

(i) the number of dwelling-houses to be provided is 10 or more; or

(ii) the development is to be carried out on a site having an area of 0.5 hectares or more and it is not known whether the development falls within paragraph (c)(i);

(d) the provision of a building or buildings where the floor space to be created by the development is 1,000 square metres or more; or

(e) development carried out on a site having an area of 1 hectare or more;”;

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Annex D of PPG13 identifies the threshold development sizes over which a Transport Assessment and travel plan should be developed:

- Food Retail – above 1000m²
- Non Food Retail – above 1000m²
- Cinemas and conference facilities – above 1000m²
- D2 Uses (other than cinemas, conference facilities and stadia) – 100m²
- B1 including offices – 2500m²
- Higher and further education – 2500m²
- Stadia – 1500 seats

As part of the Government’s aim to encourage widespread voluntary take-up of travel plans, we would also want to see Travel Plans produced for reasonably sized projects that are below the statutory thresholds. For smaller projects, demonstrating some of the key principles and elements of travel plans will suffice.
6. ELIGIBILITY RULES APPLYING SPECIFICALLY TO REVENUE PROJECTS

6.1. ERDF Revenue (current) expenditure categories are set out in the text box below.

Projects must define costs under the following expenditure categories for the purposes of grant claims

**Salaries**
This should include staffing costs for personnel directly engaged on the project. The costs should include National Insurance and Superannuation contributions.

**Overheads**
This should include general administration costs associated with the direct delivery of the project, office equipment with an asset life of less than a year, expendable supplies, and other costs that are essential to the effective implementation of the project.

Leasing charges should exclude interest and service charges and must not duplicate capital costs.

**Premises**
This should include rent, rates, heat, light and service charges associated with the premises where it can be clearly demonstrated that these are incurred by the organisation solely for the ERDF project. Where premises are shared the amount charged to the ERDF project should be apportioned accordingly.

**Fees**
This should include any work done by an independent consultant if the work was essential to the project and the costs were reasonable. Costs of independent project evaluations can be included if the work is essential to the project and/or a condition of grant. In both cases there should not be any double counting of fees under capital expenditure. Accounting and audit costs if they relate to requirements imposed by the Managing Authority. The cost of guarantees provided by a bank or other financial institution to the extent to which the guarantees are required by National or community legislation. Fines, financial penalties and expenditure on legal disputes shall not be included.

**Other Revenue**
Any eligible revenue expenditure not covered in the categories above provided it can be clearly demonstrated that these are directly related to the delivery of the project. This could include depreciation, amortisation and impairment of assets that have not been purchased with the help of national or Community grant. Documents showing how depreciation costs have been calculated must be kept for audit purposes. Any expenditure related to marketing and publicity should also be included here.
3.1.23 Eligibility of general revenue costs

3.1.24 Overheads

6.2. The rules applying to overheads are based on the principle that costs attributed to ERDF projects must be directly related to the delivery of the project. However, following the change in the Regulation a flat rate methodology can be applied for indirect overhead costs which includes premises, service and administration overheads.

6.3. To aid with project design, detailed guidance on the calculation of overheads is given in Annex A of this chapter, together with worked examples in Annex B. Annex C gives guidance specific to Higher Education Institutions.

3.1.25 Staff Costs

6.4. Only those staff related costs detailed below can be included in the eligible costs of a project;

- The full actual pay cost including employer’s national insurance and superannuation costs for those engaged exclusively on the delivery of the project or a proportion of it reflecting the time actually expended on the qualifying project. Annual pay (actuals) should be converted to hourly rates to calculate the apportionment.

- Travel and subsistence costs that relate solely to the ERDF project.

- Sick leave and/or maternity payments if they are written into an employment contract. The costs of employing a temporary replacement for an employee away on maternity or long term sick leave are also eligible for ERDF. [However, as this may result in an overall increase in staff costs for the project, the applicant would need approval to amend the budget].

- Costs of staff training necessary to the delivery of the ERDF project. Although note that it is expected that all organisations who submit an application for ERDF grant are in a position to deliver the approved activities. Staff training costs can only therefore be included where it is identified that an individual has specific training needs necessary to the delivery of the ERDF project that could not be identified before the project began.

- Taxable benefits which form part of the contractual terms and conditions of staff engaged in the delivery of ERDF projects. Examples include - bonus payments, childcare payments and company cars. These should be set out clearly in the initial application for grant, they should be proportionate to the role and responsibilities by an individual in the delivery of the project and should figure in the costings approved in the project approval process.
6.5. By way of clarity on benefits that can be included as eligible costs, non-taxable bonus payments or other non-taxable benefits are not eligible, nor are exceptional or extraordinary provision for pension rights.

3.1.26 Depreciation

6.6. The cost of depreciation of assets used in ERDF projects is eligible expenditure provided that:

- the asset was not purchased or improved as part of a previous ERDF funded project;

- the cost of depreciation is not already being met from other sources; and

- depreciation is calculated in accordance with the accounting rules that apply to the sector.

3.1.27 Hire and lease of premises and equipment

6.7. The cost of hire or leasing (including non recoverable VAT) is eligible expenditure but only in respect of the usage that relates directly to the delivery of the ERDF project. Interest or service charges arising on debt incurred including finance leases, hire purchase and credit arrangements cannot however be included in the costs, which are therefore restricted to payments based on the alternative cost of purchasing the asset outright.

3.1.28 Consumables

6.8. The cost of consumables that are used in delivering the project can be included as eligible expenditure. Consumables should be clearly itemised and the cost should be included in the application for grant.

3.1.29 Second-hand equipment

6.9. The purchase cost of second-hand equipment is eligible providing:

- The equipment has not been originally purchased as part of a previous ERDF funded project.

- The price paid does not exceed its market value.

- Whilst it is unlikely that commercially available second-hand equipment has been bought using public money, grant applicants should obtain a declaration from the supplier confirming that they did not receive ERDF grant to purchase...
the equipment in the first place. If a grant was used to purchase the equipment, none of the cost of purchase is eligible for ERDF.

3.1.30 Value Added Tax

6.10. VAT that derives directly from the project and which is not recoverable is eligible but precise rules are complex and if there is any doubt advice should be sought from HMRC.

3.1.31 Revenue costs ineligible for ERDF support

6.11. The following individual revenue costs are not eligible for ERDF support:

- notional costs, for example, where an item usually retails at £x, but the applicant buys it cheaper but claims the difference between the price paid and £x
- payments for activity of a political nature
- provisions – ie money set aside to pay for future events eg sink funds
- contingencies and contingent liabilities
- dividends
- interest or service charges arising on debt incurred including finance leases, hire purchase and credit arrangements
- costs resulting from the deferral of payments to creditors
- costs involved in winding up a company
- payments for unfair dismissal
- compensation for loss of office
- bad debts arising from loans to employees, proprietors, partners directors, guarantors or shareholders
- payments for gifts and donations
- entertainments apart from food and non alcoholic drink provided as part of a meeting
- statutory fines and penalties
- criminal fines and damages
- legal expenses in respect of litigation
- costs incurred by individuals in setting up and contributing towards private pension schemes, or the setting up of such schemes by organisations in receipt of ERDF
- costs incurred by organisations in relocating personnel displaced by the refurbishment or conversion of a building for ERDF use.

This list is not exclusive and any queries about the eligibility of costs not included in the list above should be addressed to EPP/CLG.

3.1.32 Lost opportunity costs

6.12. Lost opportunity costs are the costs that an organisation notionally incur by using an asset for an ERDF project that could otherwise have been sold or rented for profit. These notional costs are not eligible for ERDF support. For example, many organisations rent or hire out rooms on a commercial basis. Notional rent or hire of the
room cannot be included as an eligible cost (as they would constitute in-kind costs). The costs of the room overheads such as electricity or rent actually paid are eligible for ERDF, providing the applicant can show that they have claimed only the costs of the overheads while they were actually using the room. Another example of ineligible lost opportunity cost is the income that a university would normally make by charging for use of laboratory facilities or specialised equipment but that they have forgone by offering the facility at reduced or no cost.

3.1.33 Financial Charges and Guarantee Costs

6.13. Under Article 49 of the Implementing Regulation, the following charges and costs are eligible for ERDF:-

- Charges for transnational financial transactions (most likely to arise under Transnational Co-operation programmes);

- bank charges for opening and administering a bank account or accounts, where the implementation of an operation requires a separate account to be opened;

- legal consultancy fees, notary fees, costs of technical and financial experts, and accountancy and audit costs, if they are directly linked to the ERDF operation and are necessary for its preparation or implementation or, in the case of accounting and audit costs, if they relate to requirements imposed by the Managing Authority (MA) or an Independent Body on behalf of the MA; and

- the cost of guarantees provided by a bank or other financial institution to the extent to which the guarantees are required by National or Community legislation.

3.1.34 Eligibility of businesses for ERDF support

6.14. Eligible businesses will primarily be SMEs in line with the Commission definition, although the regulations do allow for large companies to be supported if this is identified in the regional programme. State Aid and other EC regimes must also be respected alongside ERDF rules.

3.1.35 Definition of an SME

6.15. SMEs are defined by Commission Recommendation 2003/361/EC of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises not owned or controlled by a non SME. This is a detailed definition, and in cases of doubt the Recommendation should be referred to – it is available on the Europa website at Enterprise - SME Definition. Very briefly, it defines an SME as follows:

- An enterprise is considered to be any entity engaged in an economic activity, irrespective of its legal form. This includes, in particular, self-employed persons and family businesses engaged in craft or other activities, and partnerships or associations regularly engaged in an economic activity.
The category of micro, small and medium-sized enterprises (SMEs) is made up of enterprises which employ fewer than 250 persons and which have an annual turnover not exceeding EUR 50 million, and/or an annual balance sheet total not exceeding EUR 43 million.

Within the SME category, a small enterprise is defined as an enterprise which employs fewer than 50 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 10 million.

Within the SME category, a microenterprise is defined as an enterprise which employs fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 2 million.

3.1.36 Eligibility of Business Activity

6.16. The aim of the ERDF funded business support is to establish an enterprise culture without distorting competition or trade. In general, support should not be provided where displacement of other businesses within the programme area is likely to take place as a result. There could be cases, for example, where a business could receive ERDF for advising retailers, theatres/cinemas, pubs, banks etc on improving their performance in areas such as environmental sustainability or equal opportunities, where the issue of displacement does not arise. Cases such as this should be considered on a case by case basis and we recommend that the advice of EPP/CLG be sought.

3.1.37 Businesses ineligible for support

6.17. Sectoral restrictions. There are a number of sectors in which businesses should not be supported with ERDF due to the existence of particular State Aid and other regimes, or because Aid would distort competition. Companies covered by EC Sectoral restrictions are subject to specific rules, dependant on the State Aid regime under which they are being supported. The demarcation requirements of the ERDF programmes also restrict some sectors which are otherwise supported through the EAFRD or EFF.

6.18. In brief therefore, the following are sectors ineligible for ERDF support

- fishery and aquaculture sectors which are supported through EFF
- primary production, processing and marketing of agricultural products, which is supported through EAFRD
- the coal, steel and shipbuilding sectors (excluded by the General Block Exemption EC 800/2008)
6.19. Banking and insurance companies should not be supported, as their activities are non productive and support to one institution is likely to lead to displacement of jobs, except as a deliverer of services or match funding, for example as members of a VCLF consortium.

6.20. Establishments providing generalised (school age) education should not be supported as this is a statutory duty on local authorities.

3.1.38 Applying the Eligibility Criteria to Businesses

6.21. It is the responsibility of the project sponsor or others administering a Business Support project to ensure that the businesses being offered support are eligible, both within the Structural Funds regulations, and also within the terms of the specific project agreed with the ERDF Offer Letter. Sponsors are encouraged to become familiar with eligibility guidance and, if supporting a business in a grey area, to record a justification for any future Audit, based on these criteria.

7. FINANCIAL ENGINEERING INSTRUMENTS

7.1. Financial engineering instruments (FEI) projects use ERDF grant as capital to create funds that are then used as loans or to make investments which are subsequently repaid generating returns that can be reused for further investment. Detailed guidance on financial engineering instruments including VCLF, JEREMIE and JESSICA is contained in Chapter 15 of the User Manual.

7.2. Eligibility issues are covered in Section 7 of Chapter 15. These cover the need for:

- The funds and the investments to contribute directly to the objectives, priorities and targets of the Operational Programme
- Compliance with State aid rules
- Investments to be made in viable firms.

7.3. As set out in paragraph 3.4 and Annex E of this chapter, following the amendment to the Article 7 of Regulation, funds could be used to support the provision of energy efficient measures in social housing.

7.4. The criteria used to select investments and assess the associated business case must reflect these eligibility requirements.

7.5. The grant recipient of the investment is considered to be the end beneficiary and as such the eligibility rules do not apply.

7.6. As indicated in 4.19, the accounting requirements for private sector match contained therein are different from those for FEI. These are set out in more detail in User Manual Chapter 15.