EU COHESION POLICY IN A GLOBAL CONTEXT: COMPARATIVE STUDY ON EU COHESION AND THIRD COUNTRY AND INTERNATIONAL ECONOMIC DEVELOPMENT POLICIES

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Preface

This is the Draft Final Report for the project *EU Cohesion policy in a global context: comparative study on EU Cohesion and third country and international economic development policies* (CCI No.2009.CE.16.0.AT.068 and 2009.CE.16.C.AT.034) submitted to DG Regio by the European Policies Research Centre, University of Strathclyde.

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1. INTRODUCTION

The overall aim of the study is to provide a better understanding of the specificities of EU Cohesion policy in a global context through comparative research on Third Country and international economic development policies. It will involve the benchmarking of Cohesion policy against other economic development policies, identifying the commonalities and differences in policies, and the lessons to be learned from these other policies. It will also provide best-practice examples for the future development of Cohesion policy.

Specifically, the objectives are:

(i) to undertake a comparative assessment of regional development policies in selected OECD countries on the basis of selected themes which are of importance for EU Cohesion policy and covering all aspects of the programme cycle (strategy development and programming, programme management and implementation, financial control and audit, monitoring and evaluation);

(ii) to undertake a comparative assessment of EU Cohesion policy and the development policy lending of selected international financial institutions (IFIs), with a particular focus on conditionality, taking into account the different management systems in place (grant vs. loan support, programme management under a shared management system vs. project management under a direct management system);

(iii) on the basis of the above assessment, to provide a theoretical and empirical framework to identify the commonalities and differences in policies; and

(iv) to draw important policy and practical lessons for the future development of EU Cohesion policy based on 'best practice' examples from around the world.

This paper provides a synthesis of key themes and issues emerging from in-depth research of nine case studies under Task 3 of the research. It includes an assessment of how the management of individual processes is carried out in practice, identifying strengths and weaknesses and analysis of the operational experience with using specific mechanisms, such as the use of incentives and conditionality, targets and indicators, managing policy risk, or ensuring financial control under different types of system.

The paper focuses on two key headings deemed most relevant from the perspective of the research task. The first is performance management, including: the use of contracts and co-financing; the use of programmes, targets and guidelines; conditionalities (ex ante, ex post, structural, governance); incentives/sanctions (reputational, financial); and, the role of evaluation and reporting in policy feedback. The second is assurance, including: the scope of assurance systems, the operation of systems (e.g. division of responsibilities); and the role of audit.

Following a section that briefly summarises the economic development approaches of the Task 3 case studies, Sections 3 and 4 highlight key issues emerging from the research under the headings of performance management and assurance, illustrated with representative examples. These points inform recommendations for Cohesion policy performance management and assurance systems which are set out under each heading. An Annex provides a comparative table summarising key points for each case covered.

2. TASK 3 CASE STUDIES

The objective of Task 3 was to undertake in-depth research of nine case studies with particular relevance for EU Cohesion policy and to provide a comparative analysis according to the themes identified in Task 1. The selection of case studies for in-depth analysis was agreed with the Commission on the basis of different criteria: relevance for EU Cohesion policy, taking into account the limitations of transposing other systems and experience on to the particular approach of Cohesion policy; geographical spread; institutional context; and specific features of the shared policy instrument. On the basis of these criteria, the cases below were selected (see also Annex for comparative table summarising key points for each case).

- *Canada*. A confederal system, with regional development agencies operating in different ways, with different powers, according to regional needs and institutional contexts. The Atlantic Canada Opportunities Agency (ACOA) is one of the oldest agencies; it represents the interests of Atlantic Canada in federal government policy making and has a mandate to coordinate federal efforts in matters relating to regional economic development. Of particular interest is a detailed process of setting strategic objectives and outcomes, and an annual performance and assessment system.

- *Germany*. The Joint Task for the Improvement of Regional Economic Structures (GA) provides an example of a formal, rules-based approach to the use of conditionalities in a federal context. GA co-funds regional-level activities based on nationally-agreed eligibility conditionalities and award criteria. There is a joint approach to assurance: the federal level is responsible for compliance but verification of expenditure is the task of the *Länder*.

- *Japan.* Cluster-based regional development policy emphasises the importance of promoting agglomeration and spatial concentration, so as to improve competitiveness and value-added in global competition. A traditionally centralised unitary system operates, but in recent years there has been a change in emphasis from a top-down and rigidly hierarchical system to something which is much more akin to a bottom-up and flexible system, not dissimilar to the emerging policies in many EU countries. There has been recent decentralisation of some economic development to prefectures, and coordination through 'regional bureau' and informal agreements

- *Poland.* This is an example of a regionalised unitary regime in a new Member State with closely aligned domestic regional policy and Cohesion policy administrative systems. It has several instruments that involve conditionalities: state-regional contracts that are currently being reformed, use of a performance reserve, and conditionalities linked specific instruments – regional contracts, performance reserve, conditionalities attached to key projects.

- *Switzerland.* The Swiss approach involves a federal fund, use of earmarked transfers and co-financing. The centre sets specific project selection criteria. Contractual conditionalities operate through the use of integrated targets and performance assessment under programme agreements. There is a consensual approach to the use of conditionalities through *Raumordungskonferenz.* Sanctions are used, but mediation provisions are offered.

- *United Kingdom.* English RDAs are set targets by national ministries in the context of the Single Pot budget. RDAs are evaluated regarding the extent to which they have met targets set. There is an outcome-focused approach in monitoring and evaluation. Reputational incentives are important.[1]

- *USA.* This is an example of a federal country with strong powers at state level but also active sectoral policies at federal level and generally weak regional policies. The Appalachian Regional Commission is a regional economic development agency that represents a partnership of federal, state, and local government. The ARC delivers economic development support through multi-annual strategic plans, with short, medium and long term outcome targets and performance assessment.

- *EBRD*. This international financial institution focuses on large projects, with a structured appraisal process. Conditions are placed on loans through covenants in loan agreements. Some transition impacts are excluded, reducing the perceived restrictions of a loan, making it more attractive to clients. Sanctions involve cancellation of loan and potential debarring. A comprehensive monitoring and evaluation process is used.

- *World Bank*. The Bank uses a combination of project-based assistance and sectoral budget support (through development policy loans). It has used structural conditionalities linked to external environment but as specific obligations that trigger funding rather than measures of impact. More recent moves to reduce conditionalities focus on the impact of specific interventions. It has a leading role in developing impact evaluation as a performance management tool.

[1] It should be noted that, since the research started, the UK Government announced that the RDAs in England would be abolished.

3. PERFORMANCE MANAGEMENT

In recent years, increasing weight has been attached to managing the performance of policy instruments that are implemented across administrative boundaries, not least on grounds of policy efficiency. Arrangements between levels of government are unavoidable in a regional development context characterised by complex interactions and incentives between supra-national, national and sub-national actors (Keating, 2003). Since regional policy uses national funding, it is incumbent on national regional policy departments to justify the value-for-money and appropriateness of their regional development spend, even where (as is increasingly the case) policy delivery is a regional responsibility. The expansion of the regional policy agenda to incorporate a broader range of sectors issues and objectives has provided further impetus for ensuring a coherent and efficient system. Moreover, in a number of countries, ongoing moves to improve efficient policy management have been reinforced by the economic crisis.

International Financing Institutions (IFIs) face similar policy management challenges in complex multi-level systems. Ensuring a close correlation between initial objectives and results is challenging because of asymmetries in information, capacity and funding between the 'donor' and 'recipient (or between the 'principal' and 'agent'). The principle-agent dynamic and sharing of risk between levels creates uncertainty, making it difficult to guarantee that the funding provided will achieve the desired effects,[2] i.e. ensuring that the beneficiaries of funding follow the strategic objectives outlined by their principals.

A key challenge, particularly under Cohesion policy, is to find an approach that includes conditionalities in order to guarantee efficient delivery while incorporating the principles of subsidiarity and partnership. Conditionalities can be important in responding to the uncertainties and risks associated with principle-agent dynamics. However, requiring compliance with conditions can undermine ownership, and is not always an effective way to reach intended outcomes. Inflexibility or reluctance to change may undermine policy efficiency.[3] There is, therefore, vigorous debate on the use of contractual mechanisms, conditionalities, indicators, sanctions/incentives and evaluation.

3.1 Macro-level resource allocation mechanisms

Systems for the multi-level governance of development policy require mechanisms to allocate funding between tiers. In IFIs this applies to how decisions are made to decide levels of lending to recipient countries. In national regional policy systems this concerns the process whereby

[2] Grossman, S., Hart, O., (1983). An analysis of the principal-agent problem. *Econometrica* 51, 7–46, Martens, B., 2002. Introduction. In: Martens, B., Mummert, U., Murrell, P., Seabright, P. (Eds.), *The Institutional Economics of Foreign Aid*, Cambridge University Press, Cambridge, pp. 1–43. Milner, H., 2004. *Why Multilateralism? Foreign Aid and Domestic Principal-Agent Problems*. Columbia University, NY.

[3] Koeberle, S.G. (2003) *Should Policy-Based Lending Still Involve Conditionality?* The World Bank Research Observer, Vol. 18, No. 2, Washington, DC; Dollar, D. and Svensson, J. (1998) What Explains the Success or Failure of Structural Adjustment Programs? *Policy Research Working Paper,* World Bank, Washington.

the level of resources allocated to different regions is decided. Such macro-level mechanisms for resource allocation can help ensure that the ultimate beneficiaries follow intended strategic objectives by including specific considerations or criteria.

3.1.1 Case study insights

In this context, there is a fundamental difference in the approach taken to resource allocation between national regional policy systems and IFIs.

- In national regional policy cases, algorithms or criteria weighted towards specific priorities are often used to decide the overall funding envelopes available to regions. These mainly have a pro-equity bias (e.g. *United Kingdom, Poland*) and focus on socio-economic indicators such as GDP, unemployment rates etc. This approach ensures that funding is automatically allocated to the neediest regions but does not take into account other issues, such as management and administrative capacity, experience of implementing regional development programmes, strength and commitment of regional civil society etc.

- On the other hand, as some academics have noted of the *World Bank***'s** aid programmes: "The Bank does not just lend money and produce ideas: it packages the ideas and the money together".[4] This is clearly seen in World Bank's use of Country Assistance Strategies (CAS). These provide an overall strategic context for individual Bank lending operations in a country over a specified period of time (typically, four years). It comprises: a country-owned vision; diagnosis or analytical underpinnings for the Bank's support; a results based framework; and, a selective programme of Bank's lending and non lending activities. CASs are expected to be fully aligned with a country's own development strategy and goals and are developed by Bank officials in consultation with the recipient government and local stakeholders (e.g. civil society, private sector). Crucially, indicative country allocations are set out in the CAS; and are based on, *inter alia*, financing requirements, the sustainability of the country's debt, and absorptive capacity. Within this, lending by the Bank through the International Development Association (IDA) is allocated through a Performance Based Allocation (PBA) system (World Bank, 2009a). The main factors that determine the allocation of IDA resources to a country are its commitment to and ownership of a reform programme, and its track record of using Bank funding. This is assessed by the Country Policy and Institutional Assessment (CPIA). The CPIA assesses the quality of a country's present policy and institutional framework. This use of a more discretional approach to resource allocation at the macro-level gives IFIs a greater degree of leverage when it comes to setting conditionalities and ensuring compliance.

[4] Gilbert, C, Powell, A., and Vines, D. (1999) 'Positioning the World Bank' *Economic Journal* 10., F-598-633.

3.1.2 Cohesion policy recommendations

The approach to resource allocation among Member States under Cohesion policy is much closer to national regional policy systems than IFIs. The Commission allocates funds to Member States on the basis of automatic statistical criteria: eligible population, national wealth, regional wealth and unemployment rate. Each Member State then decides on the specific details of how the resources are divided up among the regions by taking into account their geographical eligibility and other criteria such as per capita income and unemployment rate. In effect, budget allocations to Member States are decided in advance. Generally, funding allocation is not based on considerations such as financial requirements, track record, institutional environment etc. although absorptive capacity is taken into account through the capping of Cohesion and Structural Funds receipts in new Member States (at 4% of national GDP).

- A key issue, therefore, is how Cohesion policy can overcome the lack of leverage resulting from the absence of a discretional resource allocation system. One option would be for the Commission to include assessments of the policy and institutional environment, commitment to reform, and the record of the Member State or region in making Cohesion policy in resource allocation decisions. Such assessment could cover and rate Member State economic governance, structural policies, policies for social inclusion and equity, and public sector management and institutions, as well as track records of using EU funds. It should be noted that this would extend Cohesion policy performance management governance changes far beyond existing Commission competences and would require putting in place ambitious assessment mechanisms.

3.2 Funding agreements: contracts and co-financing

Funding agreements are necessary to make the conditions attached to programmes or grants legally enforceable. The case studies reveal forms of funding agreements that vary in terms of scope, content and formality: contracts, covenants, memoranda of understanding etc.

3.2.1 Case study insights

In several countries, there is a growing emphasis on the coordination of various funding streams through national-regional contracts or co-financing arrangements. Increasingly, funding packages for regional projects involve multiple sources of finance with co-funding arrangements being used to coordinate national and regional interventions. This gives national authorities the opportunity to ensure that national priorities are appropriately reflected in the projects in receipt of support while boosting the participation and commitment of sub-national participants.

- In *Germany*, the GRW (regional policy joint task) co-funds regional-level activities based on a federal-state framework plan and nationally-agreed eligibility and award criteria.

- In *Switzerland*, in accordance with the Law on Regional Development, efficient allocation of funds is mainly ensured via the principle of 'cantonal participation', requiring co-financing contributions of 50 percent to implementation programmes (Art.16-2).[5] Within this, funding can be used flexibly by the cantons based on global grants delegations. An exception is the support of infrastructure loans, for which cantons are obliged to contribute 50 percent on an individual basis. They also have to assume 50 percent of any incurred loss, encouraging them to take precautions to avoid such losses (Art.8-3). Project promoters are required to contribute a sizeable share of funding (e.g. at least 20 percent) to the project depending on their financial resources.

- Co-financing is also used by IFIs. The *EBRD* usually provides, in the form of debt or equity, up to 35 percent of the long-term capital of a single private sector project. Additional funding by sponsors and other co-financiers is required. The *World Bank* only finances adequately funded programmes and WB staff ascertains the overall financing of a programme from all sources before funding is given.

- In the *United States*, the ARC has varied matching requirements for its projects in its quest to leverage other sources of funding. The ACOA Business Development Program in *Canada* has a range of funding arrangements. It offers unsecured, interest-free loans towards eligible costs. Loans have varied levels of assistance, repayable on a time schedule tailored to the circumstances. Contributions to non-commercial organisations are non-repayable.

Co-financing can be a crucial instrument of performance management, ensuring that funding and priorities are consistent in shared management systems while strengthening the commitment of different partners to efficient performance. On the other hand, they clearly rely on the availability of sufficient funds at lower levels. Moreover, this can raise issues of ownership: a perception that limited funds are being drawn from existing interventions to actions favoured by higher levels.

Where significant resources are being shared, *contractual mechanisms* provide a bindingbasis for ensuring efficient performance. Various types of contractual arrangements are apparent across different regimes. Such instruments usually include provisions to negotiate the integration of sectoral and regional development funding. This can be accomplished through the use of national-regional contracts or other less formal agreements. However it is important again to consider the enforcement environment.

- For instance, in *France* the CPER are protocols of political intent with a non-binding character rather than contracts in the strict legal sense. These contracts do not imply

[5] This also applies to tax allowances, i.e. the canton has to adopt a ruling comparable to federal arrangements. Due to differences in tax rates between federal and canton levels, this means in practice that cantons have to give up more tax income, see Schweizerischer Bundesrat (2005) *op.cit.*, p.66.

any direct consequences regarding the implementation of actions contained in them. A strengthening of their legal position has been resisted because of potential adverse effects in the form of appeals and making partners more reluctant to commit funding.

- In *Poland*, regional contracts up to now have involved very limited input from the regional side. Instead they have served as an instrument to facilitate central spending on regional projects or, more recently, to co-finance Cohesion policy projects.
- In *Switzerland*, global grants are accompanied by performance-based contracts (promoted by a programme on the 'management with performance mandate and global grant' (*Führen mit Leistungsauftrag und Globalbudget,* FLAG).
- For IFIs, the *EBRD* includes covenants in its loan agreements. These are legal requirements for a client to undertake specific actions as a condition of the loan. In order to ensure their implementation, a covenant needs to be realistic and ownership by the client needs to be strong.

Contractual arrangements offer several benefits. They can strengthen linkages between regional and local policies to national priorities. By increasing policy-making responsibility, they may also contribute to the development of local capacities. Contracting also performs a legitimising function: giving governments the opportunity to submit their policies to the agreement and compliance of other authorities can spread responsibility and accountability.

More challenging aspects of contracting can include high transaction costs in terms of negotiation and administration. As with co-financing arrangements, there is also a danger that contracts are dominated by one side, often at the higher level. In all cases, questions of enforceability were paramount. In some national regional policy systems, the legal basis of the 'contracts' is ambiguous as they are protocols of political intent with a non-binding character rather than contracts in the strict legal sense. Therefore, contracts do not imply direct consequences regarding the implementation of actions contained in them. Attempts to strengthen their legal position need to take into account possible adverse effects such as lengthy appeals, discouraging partners from committing funding. Nevertheless, funding agreements should be designed so that conditions attached to resources are obligatory and enforceable, with provisions set out for actions in the event of non-compliance.

3.2.2 Cohesion policy recommendations

Within the Cohesion policy framework, the hierarchy of Community Strategic Guidelines, National Strategic Reference Frameworks and Operational Programmes provided a framework for negotiation between the European Commission and Member States on the strategic orientation and content of Cohesion policy interventions. At the apex of the current planning system are the Community Strategic Guidelines for Cohesion (CSG) drafted by the Commission and approved by the Council of the EU. These specified an indicative framework for intervention linked to the Lisbon Strategy for Growth and Jobs and the Integrated Guidelines.

The CSG relate to National Strategic Reference Frameworks (NSRFs) drawn up by Member States as a basis for the design of operational programmes. Operational Programmes, developed by Member States or regional authorities were 'nested' within the framework set by the CSG and the NSRF. The design, content and geographical coverage of OPs were also subject to a series of EU regulatory requirements. Again, the Commission had the authority to appraise the proposed programmes in order to determine whether they contribute to the goals and priorities of the NSRF and to the CSG. Other regulations, notably with respect to eligible expenditure and the scope of the intervention of the individual Funds, also helped the Commission to determine the type of interventions planned by Member States and regions.

However, the practical application of these funding agreements has been criticised.[6] One basic challenge is lack of clarity and consistency within and across strategic documents. For funding agreements to be effective, objectives and required deliverables need to be clearly articulated in the related documents. Although all strategies and programmes are approved by the EU they vary significantly in terms of how clearly they state their objectives, theoretical underpinning, instruments, indicators and targets and timescales for achieving objectives. This lack of clarity increases the scope for agency Member States to drift away from stated objectives as programmes are rolled out. Cohesion policy funding agreements between the Commission and Member States mainly contained conditionalities linked to financial management and control systems. and not to the performance of the policy. Some conditions have been introduced in relation to EU strategic frameworks, including implementation of EU legislation and institutional capacity. The application of these conditionalities however has been uneven across Member States and programmes. [7]

- Given this, it can be argued that the development of a national contractual framework between the Commission and Member States could provide a stronger mandate for performance management. A more contractual approach could detail specific themes, priorities, conditionalities and enforcement arrangements. The Fifth Cohesion Report proposes the development of national partnership contracts, based on the Common Strategic Framework, would set out the investment priorities, the allocation of national and EU resources between priority areas and programmes, the agreed conditionalities, and the targets to be achieved.[8] The contract would be the product of discussions between Member States and the Commission on the development strategy presented in their National Reform Programmes.

[6] Casovala, P (2009) *Operational rules and results in Cohesion policy programmes: analysis and proposals for conditionalities* Barca Report Working Paper

[7] De Rynck S, McAleavey P, 2001, "The cohesion deficit in Structural Fund policy" Journal of European Public Policy 8 541 – 557

[8] COMM (2010) 5th Report on Economic, Social and Territorial Cohesion - "Investing in Europe's future" (10 Nov. 2010)

- However, some caveats must be noted. First, for this to be achieved, sufficient capacity would have to be available in the Commission to make funding agreements more context-specific and meaningful, overcoming the 'distance' between the Commission and those developing strategies and programmes in Member States. Currently, the Commission lacks capacity to provide 'in depth' scrutiny and input into detailed negotiations during the development of documents. Providing detailed, context specific input on a 'programme by programme' basis is demanding. The shift toward Country Assistance Strategies and Performance Based Allocation has been accompanied by a significant investment in capacity on the part of the *World Bank*.

- Second, taking into account administrative complexity and the need for Cohesion policy to be responsive to change, the emphasis should be on the negotiation of contracts which could be adapted to specific circumstances and provide sufficient flexibility to be adjusted to changing economic and social circumstances. The benefit of some flexibility in implementing Cohesion policy in different administrative cultures and socio-economic contexts is clear.

- A further issue to be considered under a more contractual approach in Cohesion policy is who would play the role of an independent arbiter or 'honest broker'? Who would decide whether contractual requirements have been compromised? Thus a key requirement is that assessments of contractual compliance must be conducted in an objectively verifiable manner. .

3.3 Programmes, targets and guidelines.

A related instrument for performance management is the use of programmes with associated targets and guidelines. As part of this, in most national regional policy cases, there is a broad change in support policy towards the use of programmes as the basis for the disbursal of funds. National and sub-national inputs into the development of programmes vary according to the institutional context and the share of funding responsibilities between levels. In more centralised cases (e.g. England, Poland) there is strong input from the central level through the provision of guidelines on content and structure and the right of final approval. In federal systems, regions enjoy much more autonomy on setting the programming framework for how funding is spent. There is also increasing use of programme strategies in some IFIs. For instance, the World Bank uses two types of strategic plan to guide its interventions: the Country Assistance Strategy, which outlines work in a country; and (for low-income borrower countries), a Poverty Reduction Strategy Paper. The aim is to strengthen country ownership of the agenda.

- In *England*, Regional Development Agencies were required to develop a strategic vision for each of their regions, and central government issued statutory and non-statutory guidance to the Agencies on the formulation of the Regional Economic Strategies (RESs). Although the overarching framework produced some common components in the RESs, the methodological approach taken to drafting the RESs and the content of the strategies reflected regional differences. The shifting balance in RDA activities between the implementation of programmes inherited from central government and interventions organised under the RES, in favour of the latter, increased agencies' flexibility to prioritise spend in different areas. On the other hand, there is an argument that the increased responsibilities of RDAs, in a context of limited associated spending, acted as a *de facto* constraint on their operations.

- In *Poland*, the Ministry of Regional Development played a leading role in determining the content of the current generation of ERDF Regional Operational Programmes, 2007-13. At the outset of the programming period, the Ministry developed guidelines (or *wytyczne)* to ensure that resources are allocated according to its priorities. Several of these guidelines are 'horizontal', concerning formal requirements that apply across regional and sectoral programmes (e.g. relating to eligibility, financial control, project generation, monitoring and evaluation). However, some focus specifically on the content of the ROPs. With such a strong framework in place, it is interesting to note criticism in Poland concerning the close similarity between the ROPs in terms of objectives and priorities.[9] It should be noted that a new hierarchy of Polish strategic programmes is being elaborated, related to the new national Strategy for regional

[9] See Bienkowska, E. (2008) *Nowa koncepcja polityki regionalnej – obszary refleksji.* Presentation by Minister for Regional Development, Warsaw, 22/4/08.

Development. It is based on national and regional documents in the fields of socio-economic, regional and spatial development.

- Recent years have seen an increasing use of programmatic approach in the ***World Bank***. A Country Assistance Strategy (CAS) provides an overall strategic context for individual Bank lending operations in a country over a specified period of time (typically, four years). It comprises: a country-owned vision; diagnosis or analytical underpinnings for the Bank's support; a results based framework; and, a selective programme of Bank's lending and non lending activities. CAS are expected to be fully aligned with a country's own development strategy and goals and are developed by Bank officials in consultation with recipient government, and local stakeholders (e.g. civil society, private sector).

- In the case of ARC in the ***United States***, five-year strategic plans incorporate input from private citizens, local governments, regional and local development districts (LDDs), state governments, with some input from federal agencies. There is a combination of bottom-up and top-down dynamics: explicit and detailed guidelines are provided at Congress level and the associated ARC Code. Bottom-up input in setting policy directions comes through the priorities put forward by each of the state governments. Projects for ARC approval are included in these statements. State plans incorporate input from stakeholders including the LDDs. Although there is a five-year framework, there is flexibility for year-to-year changes.

3.3.1 Cohesion policy recommendations

Programming is key for managing performance in multi-level systems and it is a fundamental component of Cohesion policy. However, programmes can be costly to design and administer, and ensuring that they serve as active management instruments presents several challenges. High levels of staff turnover, weak analysis, time constraints and an excessive number of regulatory requirements can have an impact on programme design and management. Operational programmes have been criticised for being open to a range of interpretations from different actors, for being too abstract and general.[10]

- Regulations that impact on how programmes are designed should be reviewed in this context. Requirements concerning the content of operational programmes should take a focused approach so that programmes are not overburdened by a high number of objectives. Instead, programmes should focus on a limited number of particular policy actions, based on close analysis of specific territorial or socio-economic conditions and specific theories and arguments of how qualitative change can be supported. As already noted, the EU budget review and the recently published Fifth Cohesion Report

[10] Casovala, P (2009) *op cit*.

propose a revised strategic programming framework that reflects some of these issues. This approach would consist of: a Common Strategic Framework (CSF) adopted by the Commission translating the targets and objectives of Europe 2020 into investment priorities. The EU2020 agenda provides an important overarching thematic framework but it is quite broad in scope. Member States and regions would select the relevant components of the EU2020 agenda, and build specific strategies around them.

- This emphasises the need for partnership and the negotiation of indicators and targets, combining 'top down' and 'bottom up' inputs on which relevant and realistic conditions can be built. For instance, the EU could set out a choice of potential thematic priorities, based on the key priorities of the EU2020 strategy. Each Member State or region could select the priorities (and attached indicators) that it saw as most appropriate for its own case. Member States and Regions could then set specific targets for the medium term. Ex ante evaluation could assess whether these targets are too high or low, and the Commission could, if necessary, dispute the targets during the negotiations. The process would boost performance management as it would allow comparisons to be made between priorities (and actions) in terms of the extent to which they could and did achieve their goals.[11]

- Programmes should be clearer and more results-based. They should have more explicit links between the results framework and accountable (rather than higher level) outcomes. Lack of progress against targets should be reported at EU level and justified. Programmes should avoid overloading the results matrix with indicators (stressing validity, feasibility and measurability). There should also be flexibility to revise indicators periodically and in a consensual way according to processes of learning or the impact of external events. There should be more use of completed evaluation reports in the design of new strategies.

- It is important to reiterate that this would demand a significant expansion in analytical capacity both on the EU and Member State sides. At the EU level, a more systematic approach to the setting of indicators and targets has been adopted in the 2007-13 period, but it is still not possible to aggregate achievements.[12]

3.4 The project level

Despite the shift towards programmes, the project level remains significant in the shared management of policy. This can concern the establishment of project selection criteria or the designation of key or major projects. In *Poland*, part of the guidance issued to regional

[11] Bachtler, J. and Mendez, C (2010) 'The reform of Cohesion policy after 2013: more concentration, greater performance and better governance? *IQ-Net Thematic Paper No. 26(2)* p12.

[12] Pacillo, L. (2010) *National Strategic Reports, Overview of core indicators and evaluation results*, Evaluation Network Meeting, February 25th 2010, Brussels.

governments for operational programmes referred to appropriate selection criteria. In *Switzerland*, appraisal of cantonal implementation programmes at the federal level includes assessments of selection criteria from a national perspective. In *Germany*, project applications are assessed by the Land but these are based on a list of compulsory criteria set out in the GRW Coordination Framework. In *England*, the RDAs followed common internal procedures for the appraisal and selection of projects, based on central guidance provided by the UK government. Within this, there is flexibility to reflect regional specificities.

- In several cases, the identification and negotiation of key or major projects is a fundamental part of funding allocation processes. In order to avoid fragmentation and optimise impact, there is an increasing focus on larger, more strategic projects in programmes or contractual arrangements. This can relate to large infrastructure projects regarded as investments of regional or even national-level significance. In *France*, by definition, contracts work via the implementation of key projects. In order to respect funding commitments, only those projects which are ready to be implemented from a technical and financial point of view are included in the contract. In *Poland,* the Ministry of Regional Development requested an indicative list of key and major projects that would be included in regional programmes. Regions proposed a list of potential major projects and a final selection was approved by the Ministry. In *Spain*, the central level is formally responsible for the approval of large projects (above the investment value €6 million).

- The development activities of some IFIs remain project focused. The direct management of major projects is a central feature of IFI management activity. All *EBRD* projects must meet three criteria— they must help the country move toward a market economy, i.e., have transition impact; they must take risks that supports private investors and does not crowd them out; and it must apply sound banking principles. *EBRD* is also considering a proposal that it seek a presidential decree or equivalent that approves the basic terms of major projects as a condition for project approval. This reduces the risk that projects with agreed objectives lose momentum in the case of any subsequent changes to policy or personnel.

3.4.1 Cohesion policy recommendations

Under Cohesion policy, selection criteria play an important role in guiding projects towards particular strategic objectives. There are several basic types of selection criteria: eligibility criteria, entry criteria and quality criteria. Of particular interest are the quality criteria as these relate to the degree of fit with overall strategic objectives, anticipated impacts and efficiency.

- How selection criteria are applied is also important. This includes the relative weight given to different criteria and the way in which qualitative indicators are employed. Funding may be allocated according to an automatic procedure or according to more complex approaches such as scoring or weighting systems.

- Pre-negotiated key or major projects can also be used. For instance, in the case of infrastructure support sufficient knowledge on the level of funding and time needed to complete a project and produce a specific result may be available from the outset.[13] In this case, sub-national authorities may have to propose to the Commission major projects which are very detailed in terms of lead in time, strategic fit, environmental impact, costs etc. This has the merit of targeting aid on those actions perceived as representing an optimal use of resources.

- However, it is important to note that this approach may limit the scope for flexible responses to emerging challenges in a fluid policy environment.[14] For priorities where the information available at the outset is less certain, for instance in priorities related to innovation, it may be more useful to ensure that there is clarity in the definitional, diagnostic and theoretical rationale of project plans.

3.5 The use of grants or loans

The different incentives built into loan and grant mechanisms can have implications for outcomes and performance.

3.5.1 Insights from cases studies

- A basic distinction can be made between national regional policies and IFIs in the share of funding allocated to grants or loans. Most of the development assistance provided by IFIs take the form of loans, with a small proportion of grants and technical assistance. In recent years, there has been increasing debate as to whether IFIs should move from making subsidised loans to giving grants.

- Although regional policy funding is primarily in the form of grants, instruments of a revolving nature such as loans and venture capital funds are gaining importance. At the micro level, funding packages can combine grants and loans to beneficiaries. One mode may be more appropriate for certain interventions. For instance, loans may be more suitable to measures related to the redevelopment of industrial sites or investment in innovation. In *Switzerland*, interest-free or low-interest loans are granted for interventions in the field of added value–oriented infrastructure (e.g. development of industrial estates, research institutes, rather than basic infrastructure)). These are seen as an appropriate instrument, since the provider of the loan can closely manage the process of repayment. In the *United Kingdom*, the RDAs use loans for some business support measures.

[13] Casavola, P. (2009) *op. cit.* p20.

[14] Morrissey, O. (2005). Whither Conditionality? Selectivity versus Monitoring. Paper presented at *UNU-WIDER Jubilee conference, WIDER Thinking Ahead: The Future of Development Economics*, 17–18 June, 2005, Helsinki.

3.5.2 Cohesion policy recommendations

Loan funding is already a part of Cohesion policy actions. It is a prominent component of financing of Trans-European Networks (TENs), with the choice between direct grants and loan financing being judged by reference to the ability to pay of recipient authorities, the scope for a revenue flow from the investment and the incentives for private investment. The perceived benefits of loan funding are: contributing financial and managerial expertise from specialist institutions such as the EIB Group and other International Financial Institutions, as well as ensuring long-term sustainability through the revolving character of funding.

- A key question is to what extent increased use of loans under Cohesion policy would improve performance management and increase leverage? On the one hand, grants allow greater political scope and leverage for donors to obtain recipients' commitment to conditionalities or reforms because they do not burden them with the need for repayment. However, grants are more prone to be squandered because the enforcement environment is weaker: grants carry zero opportunity costs (unless donors credibly threaten to withhold funds in cases of mismanagement). Loans, on the other hand, have to be repaid and thus provide a stronger incentive for careful use of resources by recipients. The enforcement environment is, again, crucial. Long grace periods and maturities may weaken the disciplinary effect of loans. In practice, borrowing countries generally attach priority to repayment of *World Bank* lending as non-payment carries a huge reputational risk and potential loss of confidence in the economy.

- An important incentive for timely and effective implementation of loan funding is its revolving nature. With revolving funds, financing can continue beyond the period of programming with local or regional authorities using the same funding to pursue similar objectives.[15]

- It should also be noted that the use of loans generally requires much more analytical capacity from the donor since, contrary to grant, risk assessment and capacity of reimbursement assessments have to be carried out.

3.6 Use of conditionalities

Of particular relevance to this study is how conditionalities are structured and applied in the management and implementation of programmes and projects. Studies demonstrate wide differences among economists and policymakers on the relationship between conditionalities and programme performance. Some see conditionality as a key element of the relationship

[15] See comments of Graham Meadows in House of Lords (2008), *The Future of EU Regional Policy*, 19th Report of Session 2008-09 (Norwich: HMSO).

between funders and recipients;[16] others regard it as ineffective (arguing that changes in performance are rarely related to conditionality)[17] or even having negative consequences (for legitimacy and fairness)[18]; and some focus on the implementation problems associated with the use of conditions (such as conflict of objectives, multiplicity of goals, lack of ownership).[19]

3.6.1 Insights from case studies

The definitions, functions and contents of conditionalities have multiplied across national regional policy systems and IFIs. A basic categorisation can be made:

First, *macro-fiscal conditionality*. This type of conditionality aims to promote macroeconomic stability and lay the basis for sustainable growth. Under this approach, the disbursal of development funding is linked to macroeconomic indicators, such as: inflation rates, levels of government domestic and external government debt, and a country's ability to finance its deficit.

- Traditionally, IFIs such as the *World Bank*, have used this type of conditionality. However, these conditions do not try to capture or measure the contribution of development funds to overall policy objectives. Rather, they are specific obligations, such as agreement to maintain an adequate macroeconomic policy framework, which must be met for the IFI to make disbursements in a development policy operation. The approach is to set macroeconomic thresholds that identify levels (e.g. of inflation, deficit etc.) above or below which action would be automatically triggered. However, a number of important caveats limit the usefulness of automatically applying fiscal conditionality. In many cases the thresholds, and hence the related conditionality, may overlap. For example, there may be cases where inflation is high, domestic financing is excessive, and external debt large. The content of the World Bank's conditionality in policy-based lending has broadly moved away from its traditional focus on short-term macroeconomic adjustment and removing major economic distortions towards support for medium-term institutional changes that are complex and often inherently unpredictable.

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[16] Hopkins R *et al* (1997) The World Bank and conditionality, *Journal of International Development*, 9(4), 507-516.

[17] Killick T (1997) Principals, agents and the failings of conditionality, *Journal of International Development*, 9(4), 483-495.

[18] Raman K R (2009) Asian Development Bank, policy conditionalities and the social democratic governance: Kerala Model under pressure? *Review of International Political Economy* 16(2) 284–308.

[19] Agostino M (2007) World Bank conditional loans and private investment in recipient countries, *World Development*, 36(10), 1692-1708. Koeberle S G (2003) Should policy-based lending still involve conditionality, *The World Bank Research Observer*, 18(2), 249-273. Kapur D and Webb R (2000) Governance-related Conditionalities of the International Financial Institutions, *G-24 Discussion Paper Series*, no. 6, UNCTAD, United Nations.

Second, *structural conditionality* attempt to capture the relationship between interventions and the broader socio-economic environment. However, the complexity of contemporary economic development policy and the tendency towards the use of programming means that these conditions do not try to capture or measure the contribution of development funds to overall policy objectives. Rather, they seek to ensure a broader supportive framework for the development funds to be effective. The approach is based on a set of conditions that must be satisfied or guaranteed for the principal to make disbursements in a development policy operation; which are considered to be key preconditions for effective use of the funds. These conditions can include: implementation of a limited number of policy and institutional actions or reforms (for instance related to the agricultural sector, the business environment etc.) that are deemed critical for the implementation and expected results of the supported program.

Third, *outcome or performance-based conditionality* requires the recipients of funds to reach certain goals related directly to their own programmes. Although difficulties in establishing causality between actions and achievement of certain goals must still be considered, outcome conditions allow recipients of funding more scope to demonstrate progress and impact. A key issue here is the nature of the conditions selected and the process of how associated indicators and targets are set.

- In the *United States*, the ARC sets annual performance goals, tracking various indicators to measure success in terms of both outcomes and 'process'. For each of its goals, it lists a top-line number that illustrates the progress in meeting each goal: jobs created, people trained, households served by new infrastructure, and miles of road completed in the ADHS. Then it lists goals in terms of leveraging additional matching funds or additional private investments induced from the projects. The performance measures for each strategic goal are selected by the federal Co-Chair and the states. Thus, the selection process reflects collaborative partnership.

However, there are challenges in aligning inputs from principles and beneficiaries in the identification of targets and the aggregation of monitoring data.

- Up until the recent reforms in the *United Kingdom,* RDAs were set targets to measure progress related specifically to their regional economic strategy. Each RDA identified the key regional outcomes and supporting output measures relevant to them, and sets their own outcome targets after consultation with stakeholders, deciding themselves how to measure progress towards the overarching target set at central government level. While such a flexible approach allowed regional specificities to be recognised, a potential drawback was that outputs would no longer be fully comparable across regions. Aggregation of results at national level and alignment with national indicators and targets is more challenging. In several cases, the link between national and regional level targets is unclear (as in *Poland*).

- In this context, *Switzerland* provides an interesting case. Projects under the New Regional Policy are set a series of conditions. They are required to be: aligned with the priorities of the economic development strategy; and focused on innovation and entrepreneurship in export-oriented added-value systems. Projects should also contribute to the strengthening of functional regional centres.[20] Moreover, specific conditionalities are outlined for different intervention types. In order to receive a grant, one of the following conditions needs to be fulfilled: promotion of regional entrepreneurship; strengthening of regional innovation capacity; exploitation of regional potentials and development/ improvement of added-value systems; or support of cooperation between public and private bodies, between regions, or with large agglomerations. Under the NRP, a model of 'integrated performance and effectiveness management' operates. Cantons are responsible for indicator definition for their programmes but this has to be adapted to the requirements of the NRP. This concerns the definition of cause-and-effect models for bundles of measures; the definition of objectives regarding outputs, outcomes and impacts; the definition of quantified and qualified target indicators; and the clarification of indicator measurement. Data are gathered at the cantonal level and are periodically sent to the central government agency (SECO) to ensure the comparability of NRP implementation in different regions. This also allows for aggregation of project data across levels and themes.

Finally, *conditions related to governance and delivery* are increasingly important, particularly where there is a focus on building administrative and institutional capacity. Conditions may cover issues of governance, participation and accountability in the delivery of the intervention. These conditionalities may be seen as less intrusive or onerous for the beneficiaries of funds. That is not to say that requirements to mobilise a wide range of partners or ensure transparency, for instance under procurement conditions, are straightforward in all cases. Conditions can also be related to compliance with regulations such as those applying to environmental and ethical standards (as in the cases of *Germany* and *Canada*).

- Over the past two decade, the use of conditions relating to public sector reform by the *World Bank* has increased.[21] In recent years, the content of conditionality has strongly emphasised improvements in public sector governance: support for government efforts to strengthen public financial management, fiduciary arrangements, public expenditures, and public sector reforms now account for the largest share of conditionality. The use of conditionality has increased in the social sectors and declined in the areas of environment, rural development, and urban development, as well as in trade and economic management. However, reforms in the financial sector and private sector development continue to be important areas of Bank engagement, but with a focus on improving business environments rather than on privatisation. In particularly sensitive policy areas, conditionality has declined and now focuses more on

[20] Schweizerischer Bundesrat (2007) Botschaft zum Mehrjahresprogramm des Bundes 2008-2015 zur Umsetzung der Neuen Regionalpolitik (NRP) und dessen Finanzierung, 07.025 pp.2491-2.

[21] Dreher A (2004) A public choice perspective of IMF and World Bank lending and conditionality, *Public Choice*, 119, 445-464.

long-term institutional issues.[22] There has also been considerable learning on what constitutes effective conditionality. Again, the World Bank has identified 'good practice' principles for the use of conditionality (ownership, harmonisation, customisation, criticality, transparency and predictability) which are relevant here.[23]

3.6.2 Cohesion policy recommendations

Conditionalities are already present in Cohesion policy. Conditionalities are already present in Cohesion policy. Some are linked mainly to procedural compliance (such as the approval of management and control systems) or spending (the n+2 rule). Other conditionalities, related for instance to the transposition of Council Directives, the investment of sufficient domestic sources to ensure the viability of co-funded actions or administrative capacity building are also present within a number of OPs. However, the approach is not systematised across Cohesion policy and its modalities reflect ad hoc agreements between the Member State and DG REGIO geographical units concerned rather than a comprehensive, systematic approach to conditionalities.

The Fifth Cohesion Report proposes the use of a number of different conditionalities to enhance the effectiveness and impact of Cohesion policy. Although macroeconomic conditionality raises a number of questions; there is scope for enhancing the use of structural conditions in cohesion policy. Efforts to extend the use of conditionality need to take account of political and methodological considerations. Taking into account the wide range of actions implemented in diverse contexts, Cohesion policy faces methodological challenges in developing realistic, measurable targets for indicators on which performance-related conditionalities can be based.[24] Targets may not be met for reasons that are outside of the control of programme management. Performance is difficult to assess in the short to medium term because the achievement of objectives and the effects of programmes only become tangible after the end of the programme period. There are also capacity issues: the monitoring system would need to be strengthened to monitor or measure outcomes and impacts on a comparative and robust basis - and if conditionalities are based on unsatisfactory indicators, then they cannot be effective or be applied fairly.[25] Nevertheless, ensuring that European priorities - including Europe 2020 – are effectively reflected in actions supported by Cohesion Policy is a priority for the Commission and conditionalities, as part of a coherent and consistent multi-level governance system, are key means through which the Commission can influence the

[22] World Bank (2005) *Review of World Bank Conditionality.*

[23] Ibid. Other internal IFI evaluations include: IMF (2006) Outcomes-based conditionality: its role and optimal design, International Monetary Fund. IDB (2004) Instruments and Development: An Evaluation of IDB Lending Modalities, Inter-American Development Bank.

[24] Samecki, P. (2009b) *Evaluation of Cohesion Policy*, Sixth European Conference on Evaluation of Cohesion Policy, 30 November 2009, Warsaw.

[25] Samecki, P. (2009b) *Evaluation of Cohesion Policy*, Sixth European Conference on Evaluation of Cohesion Policy, 30 November 2009, Warsaw.

decision taken by the Member States. This is therefore key for the credibility of the whole Europe 2020 governance system.

Discussions at EU level have raised several possible options for the future:[26]

- *Macro-fiscal or macro-economic conditionality* relates to the macroeconomic policy framework of Member States. In theory at least, this already exists for the Cohesion Fund where the suspension of EU funding is possible in situations where budget deficits become excessive, although this sanction has never been enforced. Against a background of financial crisis, the extension of macro-fiscal conditions to other funds in the budget that are organised under 'shared management' could strengthen economic governance in the EU and ensure sound macroeconomic conditions which are necessary for the effective implementation of the funds. However, macro-fiscal conditions operate at some 'policy distance' from Cohesion policy actions in the context of the Stability and Growth Pact. There is also a danger that the introduction of measures to meet macro-fiscal conditions could impact on other areas of Cohesion policy support (e.g. austerity measures can have a direct impact on support for social programmes under education, health and welfare). Related to this is the issue of how the enforcement of such conditions and the suspension of payments could avoid affecting beneficiaries who are not responsible for macro-economic measures?

- *Structural conditionality*. There is a stronger argument for increased use of structural conditions in Cohesion policy. Making the disbursal of funding conditional upon the existence or guarantee of a specific set of policy and institutional preconditions or reforms deemed critical in fields where Cohesion policy is active is justifiable. Such reforms strengthen effectiveness by creating transparent, direct links between the funds and strategic, regulatory and institutional change. Moreover, the introduction of reforms would have a direct impact on the efficiency of Cohesion policy interventions. A key instrument here would be new National Reform Programmes or future national partnership contracts between Member States and the Commission. These could include specific, detailed descriptions of policy and institutional actions or reforms deemed critical in fields where Cohesion policy is most active, as well as descriptions of the most relevant policy or commitment (for instance related to the agricultural sector, business support, research and innovation, environment etc.) that could be monitored as programmes are rolled out.

- *Outcome or performance-based conditionality*. Cohesion policy programmes and projects are already monitored against the achievement of stated output and result indicators and targets. The case studies reveal increasing support for conditions that try to capture the performance of an intervention against specific, realistic and

[26] DG Regio (2010) *High Level Group Reflecting on Future Cohesion Policy: Increased Coherence in the Delivery of EU Strategic Priorities*, Meeting no. 3, 2 January 2010, Brussels.

measurable targets, agreed on the basis of dialogue between donors and recipients. This has the potential of giving recipients more space to decide which policy directions they wish to take. It can also contribute to streamlining the conditionality burden and move towards a framework in which the contractual terms of the funding agreements are more balanced between donors and recipients. The development of appropriate conditions and related indicators and targets applies to all stages of the programming cycle: at programme design stage, with the inclusion of preconditions; the development of operational, objectively verifiable indicators, encouraging good practice in implementation; and, the inclusion of conditions that will produce information and insights for future learning - identifying 'what works'. Again, this model assumes the development of appropriate capacity on the part of the Commission, Member States and regional authorities.

- *Conditions related to public administration, particularly financial management and control* are increasingly stressed, particularly by the World Bank. Cohesion policy conditionalities could more strongly emphasise improvements in public sector governance: support for government efforts to strengthen public financial management, fiduciary arrangements, public expenditures, and broader public sector reforms.

3.7 Use of sanctions and incentives

The use of sanctions or incentives is crucial to the operation of conditionalities: credible penalties or rewards must be in place to ensure adherence to the conditions set. Incentives and sanctions can be financial, administrative or reputational. Financial incentives refer to the availability of funds based on performance. For instance, performance-related awards can be offered to promote better programme or project implementation. On the other hand, delays, suspensions or cuts in funding can be used to sanction beneficiaries when conditions are not met. Administrative incentives/sanctions are changes to rules and regulations that affect regional policy actors such as relaxation or tightening of budgetary rules, decreased or increased oversight. Finally, reputational incentives and sanctions 'benchmark' the performance of programmes and projects against one another, mainly to highlight good practice among peers or the public at large.

The use of incentives and sanctions in regional policy is challenging. The indicators associated with them must be clear and measurable and must capture performance under the control of the beneficiary. This can be difficult to achieve in regional policy because outcomes can be difficult to measure, there may be a substantial lag between inputs and impacts. As a result, performance measurements can be skewed towards short-term, tangible outputs that may not be the most strategic or efficient choices in the long-term. There is also some concern that by encouraging competition among beneficiaries, some incentives may limit the scope for innovation, risk-taking cooperation and exchange of experience. If one authority has developed an innovative or efficient approach to management and implementation, it may be unwilling to share this competitive advantage with others. A final challenge is how incentives and sanctions can be applied. Fundamental to all of these approaches to conditionality is the enforcement environment. To what extent should the use of incentives and sanctions be automatic and to what extent should their application be based on dialogue? The approach taken varies according to the type incentive or sanction, the size and scope of the intervention and the division of powers and responsibilities among parties involved.

3.7.1 Insights from case studies

A clear distinction can be made between national regional policies and IFIs in the use of sanctions and incentives.

- Clearly the ultimate sanction for IFIs is the suspension or cancelling of loans. The finance contract is therefore a potential sanction to ensure that projects meet their objectives. The *World Bank* can suspend or cancel loans if a country falls behind in repayments or project implementation. However, the use of ex-ante conditionalities has limited the use of sanctions. Under the current approach, the World Bank releases funding only after prior critical actions have been completed. These are listed in the schedule to the legal agreement and will have already been fulfilled before the loan is made. In the past, where a series of tranches were involved as part of a programmatic approach, the bank used triggers to release funds. Triggers attempted to link the performance of a current intervention with the critical prior actions agreed for the next tranche. However, this approach was abandoned as it was considered too rigid. Incentives in IFIs tend to be implicit.

- By adopting increasingly selective, performance-based allocation systems for funding, both the *World Bank* and *EBRD* are effectively issuing a 'stamp of approval' that is perceived as an important reputational incentive. The related sanction is public blacklisting of any beneficiary organisation found guilty of misconduct or corruption.

- A graduated approach to non-compliance is ordinarily used, beginning with reminders, and includes incentives and eventually sanctions. Sanctions are progressive; they start by withholding new loans and eventually proceed through delayed and suspended disbursements.

For national regional policies, in theory, the type of intervention (e.g. budget support, programming, projects, loans, grants) and the division of administrative responsibilities decide the use of incentives or sanctions. In federal or regionalised systems, where sub-national authorities have a high degree of autonomy, the scope to employ incentives or sanctions is often narrower. However, no national regional policy case study provided a concrete, practical example of sanctions being enforced. This illustrates the methodological and political challenges associated with attaching sanctions to conditionalities and the potential for negative behavioural responses.

- In the *United States*, the ARC generally does not employ explicit incentives or sanctions for poor performance. ARC is a collegial organisation that does not have the authority to insist on formal conditions of reform or changes in governance. On the one hand, the lack of explicit performance-based sanctions weakens enforcement. For instance, an implicit conditionality priority is that ARC funding is targeted to economically distressed counties. However, the lack of structural economic and governance conditions, supported by the threat of sanctions, can come at the expense of long-term reform. For example, distressed counties have generally been economically deprived on a long-term basis. Yet, targeting funding to these locales without requesting structural reforms may reduce the effectiveness of the funding and in the worst case, it could create a moral hazard situation where distressed counties are rewarded by remaining in their current status. The strength of not imposing strict conditions on grants and projects is that the ARC is able to maintain its role as a collegial partner for regional and local communities.

- As an instrument of business-support, the ACOA in *Canada* has particularly narrow scope to employ and enforce sanctions. The nature of the funding is such that it is not expected that every business will succeed. Enforcement of conditions (related largely to financial regularity) is through a closely managed system of Letters of Intent, Applications, Project Managers and Advisory Boards. Reporting and payment schedules are designed to avoid negative outcomes.

- In *Switzerland*, the cantons have a high degree of autonomy, and the possibilities of the federal level to enforce legal compliance are generally limited.[27] Nevertheless, the New Financial Equalisation (NFA) has introduced control and reporting procedures to monitor project progress and target achievement. Although not yet operationalised, specific funding mechanisms induce or prevent certain behaviour: under the NFA, financial (dis)incentives can be used as awards or sanctions depending on the achievement of objectives.[28] If targets have not been reached, the Confederation can impose a delay pending improvements, demand a refund, or settle the deficiencies in the following programme period. Since the NRP, in addition, works with a bottom-up approach, there is an increased probability of failure. Consequently, the programme agreements contain specific information on adaptation modalities, consequences of non-compliance, and mediation procedures. Guidance documents state that if, during the implementation phase, it becomes apparent that a project cannot reach the pre-defined targets, or that it is not financially viable in the medium-to-long term (i.e. lacking economic sustainability), the premature termination of the project should be envisaged and public funding contributions should be stopped. This is an important

[27] Linder, W. and Vatter, A. (2001) Institutions and outcomes of Swiss federalism: The role of the Canton in Swiss politics, *West European Politics*, 24, p.114.

[28] According to a report by the Federal Audit Office (see Box on p.21), this option has so far not been used very much.

element of the target-oriented approach adopted under the NRP, based on checks of agreed targets and indicators. As the cantons are in charge of project support, they must also decide on the potential termination of a project. Related criteria are defined in the framework of the programme agreements.[29] These generally set out that if a contract objective is reached only partially or not at all, the canton is obliged to inform the Confederation immediately in writing, providing a justification. The partners then negotiate any further measures.

- Where regional funding is formula-driven and reflects the economic situation of regions, there are few financial incentives or sanctions in operation. In these cases, reputational mechanisms may be used. In the *United Kingdom*, budget allocations to the soon-to-be abolished RDAs were formula-driven, and there was limited scope for financial incentives or sanctions. The performances of RDAs were 'benchmarked' against each other as reports summarising RDA performance were submitted to parliament and made public twice a year. Though these performance-related incentives for the RDAs were purely implicit, they constituted a strong reputational incentive for agencies to meet conditions.

- Financial incentives are also used in some cases. *Poland* has used a performance reserve in Cohesion policy programmes, and there are plans to create a similar 'effectiveness reserve' to improve the performance of the new territorial contracts. Among other things, it will set aside, in advance, an amount of funding in the regional policy budget of the state, to be released following the achievement of specific targets in the contracts. The reserve will be allocated every three years in the course of a given generation of territorial contracts. Its overall budget will be set out in the State's Multi-Annual Financial Plan. The basis for allocating the reserve will be the evaluation of findings contained in the annual strategic report's assessment of regional development and spatial trends. The report will indicate the most efficient and effective regional development interventions, based on indicators set out in the contracts. The reserve will be divided according to quantitative and qualitative criteria. Quantitative criteria will relate to the extent to which the contracted resources have been spent. These criteria will act as a threshold, deciding whether regional governments can have access to the reserve. Qualitative criteria will then establish a ranking of eligible regional governments as a basis for the percentage share of reserve funds. Quantitative criteria will be based on the indicators used in the contracts. It is interesting to note that up to five percent of the reserve allocated to the regions can be used as a bonus or incentive for staff working in the implementing body. Beyond this, up to 10 percent of the reserve allocated to a region can be used to fund actions of the highest added value, decided by the region. There are some

[29] Schweizerischer Bundesrat (2005) *op.cit.*, p.43 and p.54; Staatssekretariat für Wirtschaft (SECO) (2008) *The Federal Government's Regional Policy*, Bern, p.22.

concerns that this may put the onus on quick rather than strategic spending and prompt a focus on competition rather than cooperation among regions.

- Additional remuneration of staff working in bodies managing and implementing programmes and projects is used as an incentive in some cases. *EBRD* projects do not just use external, client-related incentives to ensure performance during implementation, but also internal, staff-related incentives. Staff most closely associated with a project's implementation are paid performance bonuses depending on how well their projects do in terms of delivering on, for instance, transition impact. The difficulty of the environment is taken into consideration in order to ensure that there is no incentive for to focus efforts on more straightforward interventions. Given that Banking Staff are at the frontline of dealing and working with clients to ensure their compliance with loan covenants, this ensures that staff have a strong interest in ensuring beneficiaries deliver on the performance objectives.

- A less direct means of incentivising staff is by building their commitment to the region they are working in. For instance, in the *United States*, a large share of ARC staff are either from the region or have worked in the region for a number of years. Intensive involvement with beneficiaries over a period of years in identifying opportunities, preparing proposals, mentoring, monitoring and helping them meet reporting requirements has built strong knowledge of the region 'on the ground', facilitating the consensual selection of relevant priorities, targets and indicators. Moreover, it has strengthened staff commitment to 'making things work'. This intensive involvement with clients and local stakeholders is also instrumental in preventing fraudulent activity and defaults. This highlights the need for stable institutional conditions and good governance.

- In this context, it is worth noting the experience of the *United Kingdom* where a performance fund for the RDAs was short-lived. It concerned a very small proportion of the RDAs total budget; it was taken from the RDA's 2003-04 budget allocation, making it seem less of a true performance reward; and it proved to be less important than reputational incentives.

3.7.2 Cohesion policy recommendations

In comparison to IFIs and national regional policy systems, the Cohesion policy enforcement environment is constrained. In common with all of the cases, Cohesion policy faces the methodological challenges for setting incentives and sanctions that arise from a shared management policy . Beyond this, when it comes to the use of sanctions, Cohesion policy does not benefit from the leverage associated with discretionary, loan-based funding (as under IFIs).

For instance, in cases such as the *World Bank* and *EBRD* discretional funding mechanisms provide an incentive motivation for meeting ex ante conditionalities. Beneficiaries perceive a reputational incentive in the 'stamp of approval' received when they are deemed suitable for support. Conversely, the threat of sanctions in the event of default is often enough to encourage beneficiaries to meet conditions. This preventative function is possible due to the material damage the suspension or withdrawal of loans would have and the potential damage to the reputation of national economies and public administrations. Such an enforcement environment, requires: funding of sufficient financial size and status (i.e. the importance attached to it in public policy systems) to make incentives and/or sanctions significant; a discretionary resource allocation mechanism; the extensive use of loan funding; and, a credible guarantee that incentives and sanctions will be used. Within the Cohesion policy framework, the situation is different. As already noted, Cohesion policy funding is allocated from EU to Member State level automatically rather than on a discretionary basis. The preference given to grant-based instruments rather than loans further constrains leverage. In some Member States, it is arguable that the size and status of Cohesion policy is sufficiently important to increase leverage but this is certainly not the case in all Member States.

In part, the shared management system within Cohesion policy limits the ability of either the Commission or Member States to impose or enforce sanctions. It may be difficult for ministries in Member States to agree to something that adds budgetary risk in a tight financial climate. Political tensions between different departments or regions may also be created or exacerbated, when funds are reallocated from one to another. Moreover, there is also a concern that the least-developed regions with greatest need may be most at threat of sanctions, given their generally lower levels of administrative capacity. This would go against the principles of solidarity, social and economic cohesion, basic principles of Cohesion policy.

Despite these challenges, the development of strong incentives and credible sanctions is crucial if Cohesion policy conditionalities are to have any impact. A hierarchy of incentives and sanctions could be developed to match the structure of macro-fiscal/structural/performance conditionalities (set out in Section 3.6.2):

Macro-level sanctions, are already available in theory under the Cohesion fund. These could be extended.

- The flow of payments to Member States could be automatically delayed or suspended if certain macro-fiscal conditions are breached (e.g. relating to excessive budget deficits). This would strengthen the preventative function of Cohesion policy conditionality and entail a stronger macroeconomic monitoring role for the Commission. Enforcing such sanctions at least once would be necessary to strengthen their credibility. However, as noted above, imposing such sanctions would be challenging given the indirect relationship between Cohesion policy actions and macro-economic conditions. It would be likely to create political tensions among Member States and it is not clear how such sanctions would avoid punishing those beneficiaries most in need of support. [30] Moreover, any macro-level sanctions would have to be framed such so as to avoid playing a pro-cyclical role.

Incentives or sanctions related to the *structural conditionalities* could be attached to the development of national strategic documents or contractual arrangements, agreed between the Commission and national or regional authorities.

- The example of the *World Bank*'s use of a Performance Based Allocation (under the IDA) suggests that making the disbursal of funding conditional on the development of high quality strategies that demonstrate commitment to and ownership of reform programmes could strengthen impact. For instance, extra funding could be allocated to those national partnership contracts that make the strongest commitment to institutional initiatives or structural change (i.e. through explicit guarantees and specific, detailed plans and timetables). Subsequent disbursal of funds could be informed by a review of progress towards these commitments during the programming period. This would require the establishment of clear criteria to avoid lengthy discussions on whether or not commitments are strong enough. It would also be important to avoid discriminating against those Member States and regions with sufficient institutions which could therefore not compete for reward.

For *performance-based conditionalities*, the need for incentives and sanctions to be applied through dialogue between principals and beneficiaries (rather than introduced automatically) is clear. Detailed technical standards and criteria are powerless to ensure appropriate outcomes unless the priorities of all stakeholders are correctly aligned from the beginning, and remain so. Given the constrained enforcement environment and the scope for political resistance, performance-based sanctions should be used with caution:

A distinction can be made between targets (i.e. quantifiable objectives which will be closely monitored and will lead to a policy dialogue if they are not met) and conditions (i.e. sub-sets of these targets which will lead to a sanction if they are not met). This would facilitate agreement on more quantifiable objectives and foster a performance-based implementation mechanism.

- The use of sanctions for performance-based conditionalities should be proportional. Cohesion policy actions vary in terms of scale and complexity from simple grants for small amounts to community or voluntary groups to large-scale funding for complex projects (e.g. multi-partner major infrastructure projects). The use of sanctions should take into account the purpose, value and duration of a project, its outputs, associated conditions, the level of enforceability needed and the nature and the risk of non-compliance.

[30] See initial responses of EU regions to proposals for macro-fiscal conditionalities in 'Regions reject linking EU funds to budget rules' *Euractiv,* 19 November 2010.

- Member States could be made responsible for sanctioning underperformance. This would allow funds to be re-allocated across programmes within the country instead of being lost to the EU. For instance, this was done in Portugal during the final stages of the 2000-2006 period; following an analysis of programme performance, funds were reallocated to specific programmes or to new types of interventions in line with new strategic goals. Clearly, such an approach would face difficulties in federal countries where national competencies are weaker in the domain of regional development, and adjudication on the performance of sub-national programmes may be more challenging. In such contexts, it may be preferable to encourage the application of performance conditionalities within programmes, e.g. between priorities or actions.[31]

- With the emphasis on prevention and contractual approaches, the application of sanctions to structural and performance-based conditionalities should happen in a gradual way. As in *Switzerland*, national contracts and programme agreements could set out specific information on the consequences of non-compliance and subsequent mediation procedures prior to the use of sanctions. A gradual approach to the imposition of sanctions is used in the IFIs, beginning with reminders, and includes incentives and eventually sanctions. Sanctions are progressive; they start by withholding new loans and eventually proceed through delayed and suspended disbursements.

On the other hand, there is considerable scope for Cohesion policy to extend the use of incentives:

- The Commission to retain a share of funds to be allocated on a competitive basis at EU level via specific calls, using a model comparable to the Regional Innovation Programmes or Innovative Actions in 2000-06. Allocating a limited share of funds in this way would not undermine the decentralised approach to Cohesion policy implementation.

- The use of a performance reserve, where the progress of Member States and regions in implementing programmes is benchmarked and rewarded, could be considered as an incentive. This instrument was used in some EU15 Member States during the 2000-06 period. However, it should be noted that it was widely acknowledged to have been unsuccessful. As with performance-based conditionalities, there are inherent difficulties in measuring good performance. This is a particular challenge in the EU context because performance concepts and definitions must not only be clear, but also acceptable to programmes across the EU. There are concerns that a performance bonus may make programmes and project selection more conservative and risk-averse, an approach that would not encourage regions to investin innovative economic activities.

[31] Bachtler and Mendez (2010) *op cit* p14.

[32] It may lead to a focus on quick rather than strategic spend, as well as competition rather than cooperation among regions. Not only was it administratively burdensome with limited performance-oriented benefits, but there was also evidence of perverse behaviour through the setting of artificially low targets.[33] For such an instrument to work in the future it would clearly be dependent on the quality of targets set, real competition and comparison on carefully chosen criteria that allow objective comparison between different regions/programmes (size, content, level of development etc.).[34]

- Other financial incentives could include a performance bonus for meeting objectives and targets. This is already possible on a voluntary basis in the current regulations, although very few Member States have taken up the option.

- Financial incentives for administrative staff could also be considered. As in Poland, a share of the performance reserve could be allocated as a bonus or incentive for staff working in a managing authority or implementing body. Similarly, EBRD uses internal, staff-related incentives linked to the impact of interventions. It is important to note that the difficulty of the environment or the complexity of the intervention is taken into consideration in allocating such incentives. The use of financial incentives at the project level could be encouraged. In Poland, the idea of a 'bonus system' to encourage applicants to prepare projects which contribute in an effective way to the attainment of development objectives is being discussed. This would be introduced for those who spend available resources in the best and most effective way. A similar approach already operates for some business aid schemes in Portugal. Also at project level, incentives could be used to encourage the use of expertise and peer reviews at the project preparation stage.

- A less direct means of incentivising staff is by building their commitment to the region they are working in. As noted in the case of ARC in the *United States*, staff who have long-term experience of working with beneficiaries in a region develop a strong knowledge of the region 'on the ground' and a strong commitment to the implementation of development programmes. High staff turnover is a feature of public administration in several Member States and this can have an impact on the use of incentives and sanctions and performance management in general. The need for stable institutional conditions and good governance is, therefore, reiterated.

[32] Florio, M (2009) 'Getting incentives right: do we need ex post CBA?' *Sixth European conference on Evaluation of Cohesion policy*, Warsaw 30th November – 1st December, 2009.

[33] Barca (2009) *op.cit.*

[34] DG Regio (2010) High Level Group Reflecting on Future Cohesion Policy: Focus on Results, Meeting No. 3, 25 January 2010, Brussels.

- A move towards loan funding and financial engineering in cohesion policy would provide increased leverage for incentives and sanctions. The prospect of using recycled funds and/or the threat of withholding or clawing back loans could strengthen the enforcement environment.

- Existing non-financial incentives could be strengthened. Benchmarking of performance in Member States can stimulate competition amongst regions. This could include the strengthening of competitions such as RegioStars and publicity for, or exchange of, good practices among managing authorities. The exchange of best practice is also an area where the Commission to take a more proactive role. This could be extended to Monitoring Committees, with the Commission providing information on best-practice projects and management practices from across Europe.[35]

3.8 Using feedback mechanisms: reporting

By delivering usable, timely and accurate information for programme management and accountability, reporting can be a crucial instrument of performance management. This includes assessments of whether particular policy objectives have been achieved. However, emphasis is also placed on lesson-drawing, feeding into adjustments of ongoing interventions and informing future plans. Of particular relevance to complex, multi-level policy systems, the transparent provision of periodic and up-to-date information on the performance of programmes also contributes to ensuring the accountability, and, ultimately, legitimacy of policy expenditure.[36] In short, periodic reporting is crucial for maintaining an overview of policy performance.

3.8.1 Lessons from case studies

- In *Switzerland*, for the NRP, the cantons report back to the federal level on an annual basis. Reports contain an overview of the achievement of the stated objectives, a detailed balance sheet, and an updated assessment of the sustainability of the implementation programme.

- In *Germany*, the *Länder* are obliged to report regularly to the federal level on the performance of the GRW, so that the *Bund* can comply with its duties of informing the two chambers of parliament. The reporting requirement of the *Länder* includes: submission of notifications of approval, reports on expenditure of funds and *ex post* reports on funded measures; reports on employment effects five years after funded investments with the scope to evaluate the sustainability of employment effects

[35] Bachtler and Mendez (2010) *op cit* p18.

[36] Jakoby, H. (2006) Evaluation as part of the regional policy life cycle: the example of North Rhine-Westphalia, *Regional Studies* 40(2).

(introduced in 2007); information on *Land*-level funding priorities and eligibility rules; and monthly reports on absorption of GRW funds.

- In *Canada*, ACOA reporting requirements are the primary means of performance assurance. Annual and 5-year performance reports are submitted by the President of ACOA documenting its operation. They document activities over the preceding year in relation to ACAO strategic priorities, including information disaggregated on a programme by programme basis. In addition to actual activities, the performance report identifies gaps, in financial markets, for example, and 'lessons learned' through operations and audits. Every five years, the Agency's president is required to submit to the Minister a comprehensive report that specifically evaluates the activities and the impact that these activities have had on regional disparities.

In policies with shared management systems, a key challenge is to ensure that different actors contribute consistent, timely and comparable data. Here, a balance may have to be struck between self-reporting on the part of recipients and support and scrutiny of reports by principals. The former approach creates lower administrative costs and strengthens ownership among beneficiaries but risks inconsistency or inaccuracy. Closer scrutiny and support can validate report findings but it can be costly and it can undermine partnership approaches.

- For instance, in the *United States* most of the performance outcome data for ARC projects is self reported - through its management information system, ARC.net - by the grantees even though validated later on the field by visiting a small percentage of projects. The ARC normally sends a field validation team to selected project sites two to three years after the final-project fiscal year to assess the accuracy of the annual reporting. However, there is a concern that the *ad-hoc* self-reporting by project managers appears to likely lead to overestimates of these gains, even if the local project manager is coached by ARC representatives to produce credible numbers.

3.8.2 Cohesion policy recommendations

Cohesion policy has a comprehensive reporting system. Quarterly or monthly progress reports are drawn up at priority, measure and project levels. From the 2000-06 programming period on, Annual Implementation Reports have been required by the Commission regulations. These are drawn up by Managing Authorities, drawing on information from monitoring systems, beneficiaries and implementing bodies. The production of the AIRs has been viewed as a good opportunity to exchange information and check the functioning of the monitoring system. In some cases, the AIRs were used as a basis for strategic discussions at Programme Monitoring Committee meetings and annual meetings with the Commission. However, these have tended to be formal documents, structured to meet regulatory requirements and reporting obligations. They tend to be descriptive, containing quantitative information on progress with implementation. Their utility as performance management instruments has been further limited by delays in their completion and their overall length.[37] The 2007-13 period has seen the introduction of strategic reporting, an important new dimension of the policy's governance architecture. The Member State strategic reports (2009 and 2012) and the Commission's synthesis (in 2010 and 2013) addressed to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions are precisely aimed at increasing transparency and accountability by involving the other European institutions in a dialogue on the policy's performance.

- From a performance management perspective, the strategic reporting mechanism has a number of potential benefits: it introduces a more structured high-level debate in the Council; it provides a more systematic effort to diffuse the results within the Member States; it provides a basis for a more comprehensive peer review process; and, it supports a closer alignment with the Europe 2020 strategy.

- However, some important limitations have been noted by some programme Managing Authorities. In many cases, the exercise is seen as a compliance exercise with limited or uncertain benefits in terms of strategic added value or policy impact. This highlights the need for: high quality and comparable monitoring data across the EU; reducing the scope and concentrating on strategic issues; a stronger focus on the analysis of added value of Cohesion policy compared to domestic policies; strong guidance from the Commission on what is expected from the strategic reports, including a standardised approach across the EU on the basis of more detailed guidance or a common set of jointly defined and simple core indicators to be used by all programmes; avoiding unnecessary duplication with more comprehensive domestic reporting processes or Lisbon reporting on NRPs at EU level.[38]

3.9 Evaluation

There are significant challenges to establishing evaluation as part of a model for measuring and improving performance. There is a widespread recognition that the evaluation of broader regional policy measures (including programme-based approaches) is especially challenging. In particular, there are difficulties in moving beyond process issues and outcomes to consider policy impacts and the implications for policy design.

3.9.1 Insights from case studies

- Although the ARC is seen as having a strong evaluation system in comparison to similar instruments in the *United States*, studies have not yet included counterfactual

[37] Bachtler, J., Polverari, L., Oraže, H., Clement, K., Gross, F., McMaster, I., Tödtling-Schönfofer, H. and Naylon, I. (2009) '*Ex post evaluation of the management and implementation of Cohesion policy, 2000-06 (ERDF),* Report to the European Commission, DG Regio, Brussels, August 2009, p35.

[38] Bachtler, J. and Mendez, C. (2010) 'The Reform of Cohesion Policy after 2013: More Concentration, Greater Performance and Better Governance?' *IQ-Net Thematic Paper* 26(2) p23.

techniques or taken into account displacement or selectivity effects of support. Reliance on qualitative interviews with beneficiaries is regarded as a weakness in developing evaluation as a useful instrument of performance management. Similarly, in *Canada,* ACOA evaluations are routinely undertaken internally through client satisfaction surveys. External evaluations, using broader criteria are less positive and the conclusion is that evaluation could be improved through systematic and regular external evaluations using more modern objective and quantitative methodologies that identify impact for the region as a whole.

Nevertheless, several countries are continuing to work on different methodologies to address this challenge, including piloting studies, case studies and 'counterfactual', placing particular emphasis on impact evaluation, identifying, measuring and aggregating different types of gross effects.

- A number of studies in relation to the impact of the GRW in *Germany* have recently been or are currently being undertaken by external experts for the Federal Ministry for Economics and Technology. In addition, a workshop has been held on GRW support for infrastructure. One recent study evaluated the effect of GRW business aid, and it found the GRW to be effective in stimulating private investment. It compared businesses that received aid with similar businesses that did not receive aid (via a 'matching study') and found that the development of assisted businesses was considerably stronger in terms of employment and earnings. A call for tender has been published for a further study, which will develop methods for monitoring and evaluating GRW support for infrastructure. Other studies have assessed the indicators, thresholds and data-years that could be used in designating GRW areas after 2013, and they have also identified options for coordinating policy fields that have an impact on spatial development.

- In contrast, assessing the outcomes of ongoing changes towards larger scale strategic planning and regional development in the *Japanese* regional planning system is still very difficult, because firstly, the changes are so recent, and secondly because the previous system had no measurable outcomes or evaluation processes. In terms of regional policies, such as cluster policy or specific discretionary central government funded projects, there are no formal assessments whatsoever. In the case of regional cluster policies, for instance, an informal evaluation and assessment programme operates. Cluster participants are asked to provide feedback and stakeholder meetings try to assess progress. In addition, government promotes exhibitions and personnel exchanges so as to foster knowledge transfer with other stakeholders, both within Japan and internationally. The problems with this informal system, however, are that there is limited quantitative evidence, there is no formal feedback mechanism, and there are no legal sanctions for poor performance.

- Among IFIs, evaluation is seen as a critical dimension for holding governments to account, not only for achieving impact but also for delivering value for money. Upon completion, all *EBRD* projects are self-evaluated, with a minimum of 60 percent being selected for a comprehensive evaluation by the independent Evaluation Department using a methodology that complements the initial appraisal. The ***World Bank*** has five different evaluation types to guide programme and project development: ex-ante project reviews, country assistance evaluations, sector and thematic reviews, process review and impact evaluations. Increasing emphasis is placed on quantitative, experimental impact evaluation that utilise a range of methods including interviews, focus groups, large-scale surveys and counterfactual analysis. Indeed, the World Bank is seen to play a leading role in pioneering innovative methodological approaches to address sensitive policy areas such as social policy.

3.9.2 Cohesion policy recommendations

Cohesion policy is one of the most intensively evaluated policies in Europe. Over successive programming periods, the Commission has introduced more sophisticated, rigorous and systematic approaches to evaluation of its policies and programmes.[39] A range of benefits can be identified. By stimulating a process of learning, identifying aspects of Cohesion policy that deliver added value and feeding this information back into the policy process, evaluation activities provide a means through which to improve the quality, relevance and impact of programming. The transparent provision of periodic and up-to-date information on the performance of programmes also contributes to ensuring the accountability, and, ultimately, legitimacy of EU expenditure. In fact, evaluation is seen as one of the clearest examples of policy learning between Cohesion policy practice and domestic policy systems. In several cases, Cohesion policy has been credited with growth in the status attached to evaluation, reflected in the number and quality of studies carried out and the expansion of overall evaluation capacity.[40] Despite this expansion, the ability of evaluation studies to produce definitive evidence on the effectiveness of the funds remains elusive. After over two decades of Cohesion policy, information on the “effects” of programmes is still limited and this makes it extremely difficult to learn about how an intervention works or does not work, or about how to draw lessons for the implementation of other programmes in other contexts.[41]

- A clear message from our research was the crucial role a strong base of programme information plays in determining the credibility and therefore utility of evaluations. As well as improving programme design, ex ante evaluations should be used for creating a comparison base / reference point for future strategic ex post analysis. These evaluations should go beyond mere logical analysis of the programming document

[39] Polverari L., Mendez C., Gross F, Bachtler J. (2007) ‘Making Sense of European Cohesion Policy: 2007-13 Ongoing Evaluation and Monitoring Arrangements’, *IQ-Net Thematic Paper* , 21(2) EPRC, University of Strathclyde, Glasgow.

[40] Bachtler J., Wren C. (2006) ‘Evaluation of European Union Cohesion Policy: Research Questions and Policy Challenges’, *Regional Studies* 40(2).

[41] Barca F. (2009) An Agenda for a Reformed Cohesion Policy A Place-Based Approach To Meeting European Union Challenges and Expectations, independent report prepared at the request of Danuta Hübner, Commissioner for Regional Policy.

structure. They should involve empirical study and be carefully designed, with the information needs of the future ex post in mind.

- Process evaluation is important in policies under shared management to assess how initial strategic objectives are shaped through implementation.

- However, there should also be a strong focus on impact evaluation. This serves to improve understanding of the causal link between policy and outcomes and thus strengthens the evidence base for the use of conditionalities. As with the case of the World Bank, Cohesion policy should continue to explore a range of quantitative impact evaluation methods: interviews, focus groups, large-scale surveys etc.

- Counterfactual methodologies are crucial for performance management as they increase knowledge of the causal links between policy interventions and impacts. Though challenging to conduct, comparing the impact of actions supported by Cohesion policy to similar interventions implemented over the same period without EU support provides vital insights into ‘what works’ and informs benchmarks and targets to assess performance.

- Institutional flux and frequent staff rotation in public administration can be a barrier to the accumulation of evaluation knowledge. The challenge is how to anchor at least some of the knowledge and expertise gained in evaluation processes even when the people directly involved move on. For this reason, public databases of all evaluation studies should be available as a source of information.

4. ASSURANCE MODELS: HOW IS THE PROPER USE OF FUNDING ENSURED?

Assurance is an increasingly crucial component of public policy systems. In a context of fiscal constraint there is a heavy emphasis on financial control but also on the identification and mitigation of risk. Assurance models are inevitably complex and challenging in multi-level or shared management systems. Developing an integrated regulatory framework, designing appropriate operational procedures for assurance, including auditing and reporting arrangements is an important but potentially sensitive task.

4.1 Scope of assurance models

One issue relates to the scope of assurance arrangements. What has to be assured? In terms of financial control, for public policy, the core objective is to assure the legitimacy of public action. This, in most cases, refers to *regularity* and *legality*. There is broad consensus on three main principles: any organisation accepting investor money should have a comprehensive internal control system; the system should be regularly monitored for effectiveness; and there should be public reporting with emphasis on ethics, risk, and related controls.

- In *Switzerland*, assurance requirements relate to the regularity, legality and economic viability of funding allocations. Regularity requirements refer to complete, true, clear and systematically arranged bookkeeping as specified by the Swiss Trusteeship Chamber; it also covers the correctness of accounting in accordance with the books and the existence of an internal audit system. Legality checks concern verifying the attribution of individual disbursements to guarantee and/or payment credits, the competence of the disposing agency, and the existence of legal safeguards of concrete expenditure patterns. This involves checking whether disbursements are in conformity with laws and regulations. The main focus is on auditing the legality of grants, notably regarding cost eligibility, compliance with human resources legislation and public procurement regulations. It is interesting to note that the Swiss assurance model extends to economic viability extends beyond the efficient use of funding to cover impact issues based on a comparison between impacts achieved and initial objectives. It is carried out via *ex post* performance checks on task fulfilment and grants, taking control procedures towards the realm of evaluation.[42]

Beyond this, the focus and scope of assurance increasingly encompasses *risk assessment*. IFI programmes and strategies (agreed with individual countries) place considerable importance on risk assessment and risk management plans.

- For example, *EBRD*'s Risk Management Department is responsible for supporting line managers who control and manage operational risk. Risk Management drafts proposals for discussion and review by the Operational Risk Management Group (ORMG). EBRD's operational risk framework includes: the categorisation of different loss type events to capture EBRD's exposure to operational risk; a group of key risk indicators to measure such risks; the identification of specific operational risks through an annual self-assessment exercise; internal loss data collection; and use of external loss data. Each risk (both inherent and post-control) is assessed for its impact, according to a defined value scale and the likelihood of occurrence, based on a frequency by time range.[43]

For national regional policies, an important question is what levels of risk are acceptable. These policies increasingly incorporate innovation-oriented actions and levels of risk are bound to rise. There is some concern that potentially innovative projects are deterred by intense assurance procedures. In most of the national cases, acceptable levels of irregularities (or 'error rates') have not been publically defined. However, there is awareness that risks are involved, particularly in the field of innovation.

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[42] Eidgenössische Finanzkontrolle (no date) *The Position and Activity of the Swiss Federal Audit Office (SFAO): An Overview*, Bern, p.11.

43 EBRD Website – 'Corporate Governance – Structure' Available from: http://www.ebrd.com/pages/about/principles/corporate/management.shtml

- In **Switzerland**, central administrations informed the cantons at a recent conference that the NRP involves risks, and that errors, which have not been committed deliberately and which are not repeated, are therefore acceptable.

- In the *United States*, the ARC includes specific criteria for 'high risk' grantees as part of its guidance for grant or project disbursements. It is currently responding to criticisms from its own audit office has historically done little tracking of the 'high risk' grants and did not follow through with 'lessons learned' to avoid future failings. There is relatively little difference in reporting and monitoring requirements across ARC programme areas, although bigger grants tend to have modestly more reporting and a greater chance to be selected for further scrutiny.

4.1.1 Cohesion policy recommendations

Effective identification and management of risks is increasingly considered as fundamental for strong policy administration. Identifying and responding to potential risks is key to effective performance management.

- For policies under shared management, such as Cohesion policy, risks inevitably arise from complex regulatory frameworks, the involvement of a large number of management authorities, implementing bodies and beneficiaries from different Member States. Some actors may be either unaware of the applicable rules or unsure about their correct interpretation. This can lead them to make incorrect or unjustified declarations.

- This emphasises the role of the Commission in pursuing an agenda of regulatory simplification, clarification of funding rules, eligibility and audit requirements and providing information, advice and training to implementing authorities and beneficiaries.

- It is important to note that risk management is an iterative process. It happens at the preventative stage prior to the launch of a programme or project. It is also an important part of ongoing management where emergent risks must be identified and addressed. Cohesion policy risk assessment could be applied according to types of activity and different Member State contexts. Member States and regions could identify specific operational risks when developing operational programmes and through an iterative self-assessment exercise as programmes are implemented. Departments within the EBRD identify their operational risk exposures and evaluate the mitigating controls that would help to reduce them. Managing authorities could also be required to report operational risk incident losses above a certain threshold (for EBRD the threshold is €5,000).

- Particular attention could be paid to due diligence, and risk management for major projects or for projects in particular sectors or institutional environments.

4.2 Audit

The division of audit responsibilities is a common challenge in shared policy management systems. Heavy auditing may encourage a short term focus on the delivery of annual outputs rather than the pursuit of more strategic long-term goals. Although audits can provide clarity and focus concerning policy objectives, they may find it difficult to take into account the complex and often informal relationships between different parties involved in multi-level policy systems. Lastly, it may result in the construction of a substantial 'audit infrastructure' with substantial administrative costs for auditors and those audited. For instance, *ARC* managers in the United States contend that resources needed to ensure favourable outcomes for the region need to be weighed against the trade-off of using those resources for financial oversight.

Thus, although significant work has been undertaken to improve financial management, control and audit in shared management systems, a number of challenges remain. These concern the increasing burden of financial control and audit activities; and difficulties in appropriately allocating tasks between levels. The main recent responses to these challenges relate to the development of an integrated framework for budgetary control; steps to enhance coordination between audit authorities at different levels; and, a stronger emphasis on the capacity and responsibilities of recipients of funding.

- For *IFI*s, there is increasing emphasis on improving the institutional capacity of the recipients of aid programmes and this includes public finance management. Related, the growing trend towards budget support in IFIs, by definition, uses the public financial management system of recipients. This necessitates the development of simplified and common regulatory frameworks, for instance on issues of budgeting; accounting; procurement; internal control; funds flow; financial reporting; and auditing arrangements. This implies the development of assurance models that combine senior-level oversight with the dissemination of assurance models at operational levels. For instance, the *World Bank*'s Quality Assurance Group (QUA), which focuses on improving accountability and enhancing real-time learning, operates at a number of different levels, utilising three different audit systems and interacting with different operational Bank units. The QAG shares assessments with task teams and line managers for follow-up and elevates issues that require additional attention to Senior Management for action.

- In federal countries, there are sophisticated frameworks in place for joint activities under the heading of assurance. In *Germany*, the GRW is an instrument that is jointly financed and managed by the *Bund* and the *Länder*, so the control of the proper use of the funding is shared by the two government levels. The actual implementation of the GRW with regard to the project level is the responsibility of the *Länder*. Hence, the control function is more pronounced at the *Land* level than at federal level. The *Länder* decide on the individual funding cases and control their legality in the first instance. They issue notifications of approval and verify the reports on expenditure submitted by the beneficiaries. The *Länder* actively check whether beneficiaries have complied with the rules attached to funding. After completion of the supported investment, each beneficiary is bound to present a report on expenditure, which is then checked according to *Land*-specific rules. However, the *Bund* also assumes a control function. The federal level checks the notifications of approval submitted by the *Länder*. If doubt about compliance exists, the *Land* is asked to provide further comment on the case in question. If the federal level comes to the conclusion that the *Land* has violated rules of compliance, it can claim the money back in accordance with Article 8(2) of the GRW law.

- In *Switzerland*, the federal level audit authority has the power to carry out independent audits of funding that has been delegated to the cantons. For joint tasks, financial audit is carried out in a coordinated approach by federal and cantonal audit offices. In the United States, responsibility for expenditures and oversight are shared by all levels of the ARC partnership. The Federal Co-Chair plays a key oversight role with ARC directors and grant coordinators in charge of approval and disbursement of payments to grantees. ARC has its own audit unit but also contracts external audits from the private sector.

- In unitary systems, the central level clearly plays a stronger role in assurance arrangements. In the *United Kingdom*, RDAs must have internal audit systems which comply with the objectives, standards and practices set out in central government Internal Audit Standards. The RDAs must also set up independent audit committees.

4.2.1 Cohesion policy recommendations

For Cohesion policy, the Member State is responsible for appointing a certification body to certify the statement of expenditure and the payment applications before their transmission to the Commission); and an auditing body (to oversee the efficient running of the management and monitoring system). The Commission verifies the control systems in place. Additionally, individual projects or OPs might be subject to audit by the European Court of Auditors. The burden of Cohesion policy audit has raised issues of administrative cost, especially in smaller programmes where the additional cost of audit may account for a relatively high percentage of the funding.[44] An additional concern is the effect of this administrative burden on programme design, project selection and financial flows. It may discourage administrators from allocating resources to untried types of project or to beneficiaries which have not previously dealt successfully with financial management. Similarly, it may slow down financial implementation. Thus, for Cohesion policy, there are strong arguments for:

[44] SWECO et. al. (2010) Regional governance in the context of globalisation: reviewing governance mechanisms & administrative costs Final Report to DG Regio p74.

- A clear chain of assurance and a single audit approach that allows the Commission to rely on previous controls performed by Member States.

- Proportionality and differentiation in control and audit requirements according to risks.[45]

4.3 Actions to be taken in response to problems: sanctions or support?

There is an ongoing debate on how compliance with financial management regulations can be strengthened. It is framed in terms of two alternative perspectives: enforcement or management.[46] Enforcement theorists characteristically stress a coercive strategy of monitoring and sanctions. A basic method of combating weaknesses in public financial management systems is through the use of sanctions. Donors or principals can correct irregular expenditure found by withdrawing it from payment claims, recovering any grant paid and debarring beneficiaries from future participation in programmes or projects. Alternatively, management theorists embrace a problem-solving approach based on capacity-building, rule interpretation, and transparency.

4.3.1 Lessons from case studies

- In *Germany*, the discovery of irregularities can prompt the responsible *Land* institutions to claim back the funds or adjust the conditions (e.g. extend the compliance period). In some cases, sanctions are used to deal with assurance problems. In this context, systems for disbursing funds can be used to strengthen assurance.

- In *Poland*, all financial transactions covered by a given tranche of funding under the regional contracts must be satisfactorily audited and accounted for before central government releases the next tranche. However, alternative approaches, based on problem-solving and capacity-building are also apparent.

- In *Switzerland*, discrepancies detected in the management of public finances are resolved based on dialogue between the audit authority and the audited body. The auditor can formally set out the shortcomings and also stipulate binding instructions. The concerned administrative unit has the right to appeal against the decision at the Federal Council.

Generally, the aim is to find the appropriate balance which satisfies the dual aims of ensuring legality and regularity but also improving systems and solving problems.

[45] Davies S, Gross F and Polverari L (2008) 'The Financial Management, Control and Audit of EU Cohesion Policy: Contrasting Views on Challenges, Idiosyncrasies and the Way Ahead', *IQ-Net* Thematic Paper, 23(2)

[46] Tallberg, J. (2002) 'Paths to Compliance: Enforcement, Management, and the European Union' *International Organization* 56, (3), Summer 2002, pp. 609 –643

- For instance, the *EBRD*'s Enforcement Policy and Procedures (EPPs) set out how it deals with allegations of prohibitive practices, including cancellation of financing, and/or debarment. However, the EPPs also provide for measures to help relevant entities address deficiencies in control or compliance.

- Similarly, the *World Bank* retains the right to claw back funding and to debar those involved in irregularities from future funding. A graduated approach to non-repayment is ordinarily used, beginning with reminders, and includes incentives and eventually sanctions. Sanctions are progressive; they start by withholding new loans and eventually proceed through delayed and suspended disbursements. The Bank issued Anti-Corruption Guidelines in 2006 that set out clear actions for the borrower and other loan recipients to prevent fraud and corruption. Actions include awareness-raising, prevention and reporting. Sanctions may be implemented for any borrower found to have violated the Guidelines, including a declaration of mis-procurement and the disbarring of firms. However, it also has several instruments designed to address weaknesses in public financial systems in recipient countries.

4.3.2 Cohesion policy recommendations

Cohesion policy approaches to financial irregularity should combine preventative and corrective aspects.

- On the one hand, a graduated approach to dealing with irregularities. As with the case of the *World Bank,* a series of stages, including warnings and reminders, support and advice should proceed to the use of sanctions.

- Nevertheless, ultimate enforcement of sanctions, including the suspension of payments, are crucial for credibility. The Commission should impose sanctions in cases of serious financial irregularities or systemic weaknesses despite political pressure not to do so.

5. ANNEXES

ANNEX 1: COMPARATIVE ANALYSIS OF WORLD BANK POLICY BASED LENDING, EBRD OPERATIONS AND COHESION POLICY

	World Bank's Policy based lending	*EBRD Operations*	*Cohesion Policy*
Context			
Scale	Policy-based Lending accounted for 40% of the Bank's lending commitments in 2009. In fiscal year 2009, the Bank committed US$18.35 billion (or €13.16 billion at an exchange rate of €1=$1.3948) to 67 DPOs.	In 2008 the EBRD approved 152 and supported 302 projects, totalling €12,889 million. EBRD commitments in 2008 amounted to €5.1 billion	Allocation to cohesion policy represents 35.7% of the total EU budget or €347.41 billion (current prices) for the period 2007-2013.
Rationale	Originally conceived to provide short-term financing for balance of payment support (in the aftermath of 1979 oil shock); the rationale for Bank's lending has overtime shifted to supporting complex social, institutional and structural reforms (over medium term) that are critical to sustainable development.	EBRD was established in the post Cold War period to facilitate the economic transition of Central and Eastern Europe economies.	The main rationale for cohesion policy is to reduce economic and social disparities among EU Member States and regions.
Legal Basis	Although the Bank's Articles of Agreement envisage the provision of project finance as the Bank's primary activity, policy based lending was introduced in 1980 under 'special circumstances' allowed in Article III of IBRD Articles and Article V of IDA Articles.	The legal basis for the EBRD's policy is established through its constitution, namely 'The Agreement establishing the European Bank for Reconstruction and Development'	Origins lie in the preamble to the Treaty of Rome (1957).
Overarching Objective(s)	To help borrowers achieve sustainable reductions in poverty through a programme of policy and institutional actions that promote growth and enhance the well-being and increase the incomes of poor people.	The overall objective of EBRD lending is to foster transition towards open and democratic market economies in its countries of operation	The main objectives of cohesion policy are: to tackle regional economic disparities (convergence); to support regional economic development and competitiveness; and to promote territorial cooperation
Funding Arrangements			
Sources of Policy Funding	World Bank funding is channelled through the IBRD and IDA. IBRD funding comes from capital markets through the issuance of bonds; borrower repayments and member subscriptions. IDA funding comes from donor government	EBRD lending is financed from borrowing funds on the international capital markets in the form of issuing bonds and other debt instruments. It does not utilise shareholders' capital for this purpose.	Cohesion policy is funded through the general budget of the EU. The general budget is financed from three main sources: customs duties; a share of the harmonised value added tax (VAT) base of each Member State; and a contribution from the Member States based

	World Bank's Policy based lending	*EBRD Operations*	*Cohesion Policy*
	contributions; transfers from IBRD's net income; grants from IFC; and borrowers' repayment of earlier IDA credits		on the size of their gross national income (GNI).
Funding instruments	Funds are allocated through low-interest loans via the IBRD and concessional loans and grants through the IDA	Main types of financing instruments used by EBRD are: equity investments, loans and guarantees	Transfer of resources (grants) from the Commission to EU regions
Allocation of Funding	Indicative country allocations are set out in the CAS; and are based on, *inter alia*, financing requirements, the sustainability of the country's debt, and absorptive capacity. For IBRD lending, a country's creditworthiness and the expected development impact of IBRD financing are important considerations. A Performance Based Allocation (PBA) system is used to allocate IDA resources. The main criteria for determining country allocations are: commitment to and ownership of a reform programme, its track record, population and per capita income.	Borrowers generally approach the EBRD to seek financing for their projects. It is EBRD policy to only invest in commercially viable projects. For smaller projects, EBRD makes credit available through financial intermediaries providing either loan financing, leasing facilities or equity. Although financing requirements are similar to EBRD policy, financial intermediaries make independent decisions about which enterprises they fund, based on their own requirements and investment limits.	The Commission allocates funds to Member States on the basis of the following criteria: eligible population, national wealth, regional wealth and unemployment rate. Each Member State then decides on the specific details of how the resources are divided up among the regions by taking into account their geographical eligibility and other criteria such as per capita income and unemployment rate. Funding allocation Is not based on considerations such as financial requirements, absorptive capacity or track record
Traceability of Funds	Bank lending takes the form of budget support – it is not possible to track the end use to which funds are put	The funds are put to a specified end use and it is a requirement that all eligible expenditure is supported by a clear audit trail	The funds are put to a specified end use and it is a requirement that all eligible expenditure is supported by a clear audit trail
Co-financing Arrangements	Bank only finances adequately funded programmes. During preparation, Bank staff needs to ascertain overall financing of programme from all sources	The EBRD usually provides, in the form of debt or equity, up to 35 percent of the long-term capital of a single private sector project. Additional funding by sponsors and other co-financiers is also required.	OPs and individual projects have to be co-financed. The Commission rigorously applies the principle of 'additionality'
Programme Design and Coordination			
Strategic Processes	A Country Assistance Strategy (CAS) provides an overall strategic context for individual Bank lending operations (DPOs and other lending) in a country over a specified period of time (typically, four years). It comprises: a country-owned vision; diagnosis or analytical underpinnings for the Bank's support; a results based framework; and, a selective programme of Bank's lending and non lending activities. CASs are expected to be fully aligned with a country's own development strategy and goals. In	Two types of strategic documents determine the types of investments the EBRD approves, namely Country and Sector Strategies. A Country Strategy (CS) assesses a country's stage of transition and its attractiveness to private sector investors, which in turn determines the level and pattern of demand for EBRD financing. CSs act as important strategic investment plans that assess a country's economic and political performance and define operational priorities. The EBRD's Sector Strategies (SS) guide its activities in sectors and provide operational frameworks for sector teams	The Community Strategic Guidelines set out the principles and priorities of cohesion policy. Each Member State prepares a National Strategic Reference Framework (NSRF), coherent with the Strategic Guidelines. The NSRF defines the strategy chosen by the Member State and proposes a list of operational programmes (OPs) that it plans to implement.

	World Bank's Policy based lending	*EBRD Operations*	*Cohesion Policy*
	recent years, they have become more selective, focused and results orientated		
Coordination and Collaboration	CAS is developed by Bank officials in consultation with recipient government, and local stakeholders (e.g. civil society, private sector); and in collaboration with other development partners. Programme implementation is coordinated by Bank staff working in country offices[47]. Approach to collaboration varies across countries. Some CASs are fully joint, with joint upstream analysis and diagnostic work, joint activities, and joint results. Other collaborative CASs involve a joint process of analysis and diagnosis; but activities that are coordinated, not carried out jointly. The Bank's Board does not approve the CAS; it only approves individual DPOs.	CSs are updated annually and new strategies are produced every two years in negotiation with the national government The EBRD also works in partnership with other institutions, such as domestic and foreign institutions and other IFIs, to increase the availability of financing and to improve the investment climate. Co-financiers are fundamental to EBRD projects as EBRD financing needs to be matched by funding from other sources. A key part of this is loan syndications, which are responsible for arranging co-financing with commercial banks and other IFIs directly, and directly or indirectly with export credit agencies	The NSRFs and OPs are prepared by national / regional authorities in consultation with national/ regional stakeholders. The NSRF is 'owned' by the Member State; the Commission validates certain parts of the NSRF that require a decision. The Commission negotiates and approves the OPs. The Member States and their regions manage the programmes, implement them by selecting projects, control and assess them. OPs are delivered through a participative and collaborative approach. A Programme Monitoring Committee is set-up to provide strategic steer, make programming decisions and to monitor progress.
Programme orientation	Individual DPOs follow from the CAS; and are based on a consideration of a number of factors such as, developmental impact, Bank's comparative advantage and activities of other partners. The details of individual operations are set out in a 'Program Document' which is prepared by the Bank. The Program Document describes country's participatory arrangements for the operation; the main analytical work used; operation description and policy areas; specific results, including measurable indicators for monitoring and evaluation).	EBRD does not provide policy-based support. It is a project-based institution i.e. it provides funding on a project by project basis	The OP presents the overall objectives and priorities of the Member State / region; as well as a blueprint for the delivery of the programme. The Operational Programme is developed by the Managing Authority in consultation with stakeholders and partners.
Programme Structure	DPOs can be structured as single tranche operations; multiple tranche operations; or a programmatic series of single tranche operations. Recent years have seen an increasing use of programmatic approach	Not applicable for reasons stated above	Multi-annual programmes covering a seven year period

[47] Borrower is responsible for overall implementation and monitoring and evaluation

	World Bank's Policy based lending	*EBRD Operations*	*Cohesion Policy*
Performance Management			
Use of Conditionality	The Bank makes the funds available to the borrower conditional upon: maintenance of an adequate macroeconomic policy framework; satisfactory implementation of the overall programme; compliance with critical policy and institutional actions (referred to as conditionality). More focused and streamlined conditions essentially comprising critical actions deemed necessary for programme success. Emphasis on good practice principles such as reinforcement of ownership, harmonization, customisation, criticality, and transparency and predictability. The use of conditionality in sensitive policy areas has declined and nowadays it focuses on complex medium-term institutional reforms; strong emphasis on public sector/governance	Conditions are placed on EBRD loans through various covenants in the loan agreement, which cover three areas, namely credit, environmental/social issues and transition impact. Loan covenants are legal requirements for a client to undertake specific actions as a condition of the loan.	Funds are granted to the Member State / region under the condition that they will be used accordingly to what is stated in the OP approved by the Commission. At a project level, funds are approved and disbursed subject to fulfilment of conditions relating to eligibility of expenditure and beneficiaries; publicity and procurement requirements, environmental standards etc.; achievement of stated outputs and results
Monitoring	Bank staff review implementation progress to verify fulfilment of conditions and compliance with legal covenants. The Bank uses monitoring indicators with baselines, targets, and expected results	The operation team from the Banking Department monitors the project's performance against EBRD's expectations and legal requirements. Regular monitoring reports (MRs) are prepared twice-yearly for private sector and yearly for state sector operations, which feed back into the project's implementation. EBRD projects as well as its portfolio of projects must maintain a minimum standard of transition performance.	The Commission monitors each OP alongside the Member State/ region. Managing Authorities are required to submit an Annual Implementation Report to the Commission for each OP.
Incentives	The Bank's lending is becoming increasingly selective in favour of better performing countries	The EBRD does not allocate any specific concessional resources on the basis of performance EBRD only funds projects which cannot obtain funding through alternative means (additionality requirement) which gives it considerable leverage over borrowers. Another incentive for clients to work with the EBRD is the implicit stamp of approval their project receives by being endorsed by the EBRD	Cohesion policy is criticised for lacking in incentives
Sanctions	There are no sanctions involved in DPOs as conditions must be met before funds are released.	A default can be called and the loan cancelled prematurely when a project breaches a loan covenant.	De-commitment of funds not spent within a specified period
Evaluation	The Bank employs a range of evaluative processes at different organisational levels and at different points over a programme/project's lifespan: Project reviews; country assistance evaluation;	Ex-post evaluation is done both through self-evaluation reports of the operation team, as well as the EvD, which is independent of the EBRD's banking operations	It is a regulatory requirement to conduct ex-ante and ex-post evaluations of OPs. Additionally, Managing Authorities can carry out thematic

	World Bank's Policy based lending	*EBRD Operations*	*Cohesion Policy*
	sector and thematic reviews; process reviews; and, impact evaluations		evaluations. Individual projects may or may not be subject to evaluations.
Quality Assurance and Control	The Quality Assurance Group (QAG) is responsible for quality assessment of the Bank's lending operations. An Inspection Panel (an impartial fact-finding body, independent of Bank Management) investigates any 'Request for Inspection' relating to a potential violation by the Bank of its policies and procedures WBG Internal Auditing Department examines the adequacy and functioning of the Bank's governance, risk management and control processes	The Audit Committee of the Board reviews the recommendations and once a year EvD, utilising a self-assessment by management of the degree of follow-up, reviews implementation of evaluation recommendations and the working of the system in general. The EBRD's Internal Audit Department (IAD) provides independent, objective assurance and consulting services designed to add value and improve the EBRD's operations. The EBRD's Office of the Chief Compliance Officer (OCCO) is responsible for: investigating allegations of fraud and corruption both internal as well as external to the EBRD; identifying and handling of reputational risks to the EBRD; ensuring that the EBRD operates to the highest ethical standards and investigating allegations of staff misconduct. EBRD's Risk Management Department is responsible for supporting line managers who control and manage operational risk.	The Member State is responsible for appointing a certification body to certify the statement of expenditure and the payment applications before their transmission to the Commission); and an auditing body (to oversee the efficient running of the management and monitoring system). The Commission verifies the control systems in place. Additionally, individual projects or OPs might be subject to audit by the European Court of Auditors

ANNEX 2: COMPARATIVE ANALYSIS OF EUROPEAN CASE STUDIES

	Germany	*Poland*	*United Kingdom*	*Switzerland*
Context				
Scale	The total has fallen progressively in recent years, but appears to have stabilised at around €600-650 million per annum	Total funding for ERDF Regional Operational Programmes, on which contracts are based, in 2007-13 is over €16 billion.	The scale of 'Single Pot' funding disbursed through the RDAs grew for a number of years after their launch as their responsibilities increased, but budgets have been cut over several successive years, culminating in the abolition of the RDAs in 2010. The contribution of UK Government Departments to the 'Single Pot' was c. £2,300 million in 2007-08. Over the period 2002-07, RDA spending represented approximately 0.7 percent of identifiable public expenditure in the regions.	The Regional Development Fund is endowed with €160 million for 2008-15.
Rationale	GRW is an instrument for both equity and growth. It is an equity instrument because it is limited to disadvantaged regions, and it is a growth instrument because it funds investment and not consumption.	To support regional development, organisational rationale to strengthen national/regional coordination and improve the coordination of sectoral and regional development interventions.	The channelling of 'Single Pot' funding though the RDAs represented a central facet of the previous Labour government's regionalisation agenda, and pursued the twin agenda of equity and efficiency – equity by funding being weighted towards regions facing the biggest development challenges, and efficiency, as regions pursued locally-led economic development strategies.	Combination of competitiveness objectives (regional innovation and added-value creation) with more traditional, convergence-oriented elements (safeguarding of decentralised settlement patterns and reduction of regional disparities).
Legal Basis	The tasks of the GRW are defined in Article 91a of the German Constitution[48] and in the federal law on the GRW, 'Improvement of the regional economic structure' ('*Verbesserung der regionalen Wirtschaftsstruktur*')	Article 5, paragraph 1 of the Act of 6 December 2006 on the principles of development policy (most recently amended in Journal of Laws 2009, No. 84, Art. 712).	RDAs outside London were given legal status by the Regional Development Agencies Act 1998; the wider approach to regional policy was laid out in the 2003 consultation document A Modern Regional Policy for the United	The federal Constitution states that the Confederation can support areas under threat of economic downturn (Art. 103 on structural policies). The main objectives and priorities of the NRP are defined in the 2006 Federal Law on

[48] Deutscher Bundestag (2010) *op. cit.*

	Germany	*Poland*	*United Kingdom*	*Switzerland*
			Kingdom.	Regional Policy.
Overarching Objective(s)	To reduce the locational disadvantages of structurally weak regions, thus facilitating their participation in broader economic development processes and reducing overall developmental disparities.	Supporting the competitiveness of regions; building territorial cohesion and preventing the marginalisation of problem areas; Creating the conditions for efficient, effective and partnership-based implementation.	To improve the economic performance of all English regions and reduce the gap in economic growth rates between regions.	The overriding aim is to enhance the competitiveness of regions - in promoting their assets in the fields of innovation and entrepreneurship - in order to stabilise and improve the labour market situation.
Funding Arrangements				
Sources of Policy Funding	Federal government and individual *Länder* provide funding for the GRW on a 50:50 basis	Total ERDF funding for the Regional Operational Programmes 2007-13 is over €16 billion.	The RDAs are funded by a 'Single Pot' from five central government departments: Department for Business, Innovation and Skills (BIS); Department for Communities and Local Government (CLG); Department for Culture, Media and Sport; Department for Environment, Food and Rural Affairs; and UK Trade & Investment.	The Regional Development Fund is endowed via tax income and interest earnings, repayments and guarantees from loans.
Funding instruments	Resources are direct aid for businesses in the form of non-refundable investment grants (*Investitionszuschuss*)	Transfer of resources (grants) from the Commission to regions via Polish central government.	A broad range of instruments is used, including strategic capital investment, investment in employment and skills, the provision of business information and advice, and the delivery of grants, loans and equity funding (now suspended).	Grants, loans and territorially-based tax allowances.
Allocation of Funding	6:1 distribution between new and old Länder; definition of eligible areas (A-, C- and D-areas) on the basis of four indicators (unemployment, wage level, employment forecast and infrastructure indicator)	Equalisation criteria (number of inhabitants: 80 percent; regions with per capita GNP below 80 percent of the national average: 10 percent; population living in districts with an unemployment rate above 150% of the national average for the last three years: 10 percent).	Funding is allocated using a formula that takes into account various measures of need and opportunity but has a pro-equity weighting (the North East of England has the highest per capita budget).	Global grants were allocated based on the appraisal of cantonal programmes by the federal level, a weighting and ranking process, coordination talks with federal partners and negotiations with the cantons.
Traceability of Funds	-	-	-	-
Co-financing Arrangements	Between 10 and 50 percent of the project value can be provided through GRW funds; this depends on eligible area and firm size	ROPs and individual projects have to be co-financed.	-	The principle of 'cantonal participation' requires co-financing contributions of 50 percent to implementation programmes. This can be used flexibly by the cantons based on global grants delegations.

	Germany	*Poland*	*United Kingdom*	*Switzerland*
Programme Design and Coordination				
Strategic Processes	GRW is co-administered by federal and Land-level governance structures; financing and common framework planning are shared responsibilities. Decisions are taken by the GRW Coordination Committee, made up of federal and Land-level Ministers.	The Community Strategic Guidelines set out the principles and priorities of cohesion policy. Each Member State prepares a National Strategic Reference Framework (NSRF), coherent with the Strategic Guidelines. The NSRF defines the strategy chosen by the Member State and proposes a list of operational programmes (OPs) that it plans to implement.	Central government issues statutory and non-statutory guidance to the RDAs on the formulation of Regional Economic Strategies, which are reviewed in full every three years. There is also an annual Corporate Planning process, which determines the RDAs budgets annually.	The NRP is conceived as a 'joint task' and a two-stage approach is applied: Conditions for support are outlined in broad terms in regulatory and (multi-annual) framework documents and are further specified via programme agreements with the cantons.
Coordination and Collaboration	See above	Overall strategic coordination by Ministry of Regional Development. ROPs (and the contracts on which they are based) supported by EU-type coordination structures: national and regional monitoring and steering committees, conferences and negotiations between programme partners from national and regional levels.	The RDAs activities were overseen by a Sponsorship Framework, enforced through the Corporate Planning process. Measures were stipulated centrally, but the number of measures, and related targets, were agreed/negotiated as part of the Corporate Planning process and the Ministerial sign-off of Corporate Plans, which took place every three years.	Coordination between the Confederation and the cantons covers problem analysis, programme development, the division of implementation tasks, controlling, reporting, monitoring and evaluation.
Programme orientation	-	ROPs tied to the European Commission's guidance on ERDF priorities and agreed in close cooperation with the Ministry for Regional Development. infrastructure, remains a significant priority. But Business support, RTD increasing.	The RDAs can choose to prioritise their spending in different areas, broadly categorised into the following areas: regeneration through physical infrastructure; business development and competitiveness; and activities related to people and skills.	First programme generation in place for 2008-11 based on existing cantonal economic development objectives and strategies (i.e. selected initiatives and projects that correspond to NRP criteria).
Programme Structure	Within the jointly agreed federal GRW Coordination Framework, each Land possesses wide scope for action. The Framework defines a minimum set of rules and conditions; within these, each Land can further detail funding conditions.	Multi-annual programmes covering a seven year period.	Multi-annual Regional Economic Strategies (now suspended).	Implementation programmes were elaborated around a 'Territorial Innovation Programme of the Canton', justifying the innovative character of the strategy and establishing links to systemic dynamics with respect to regional economic centres. A SWOT and spatial analysis applying a functional approach were also required.
Performance Management				
Use of Conditionality	Basic conditionalities are set out by the GRW Coordination Framework. Länder can further	Funds granted to region under the condition that they will be used	Reputational - conditionalities have not been employed – instead, the	Conditionalities relate to programme priorities, applying content-related and

	Germany	*Poland*	*United Kingdom*	*Switzerland*
	develop these in their legislation. Some conditions attached to the funding must be fulfilled after the funding has been granted. For instance, employment effects must still be visible five years after the funding decision. Other conditions relate to amortisation rules in infrastructure investments.	accordingly to what is stated in the OP. Supported by signing of regional contracts. Funding, in the form of ERDF payments and grants from the central state budget, is released from central government in quarterly tranches. Ministry of Regional Development also provided an extensive list of programme level and thematic indicators for ROPs. At project level, conditionalities are built into the system of project generation and selection. Prospective beneficiaries under the ROP fill in a project fiche, outlining the characteristics of the project and the steps for its realisation	framework and reporting requirements (allied with the evaluation and appraisal system – see below) provided a strong incentive to perform well, as well as regular opportunities to monitor progress and identify successes, challenges and risks.	methodological criteria, and to criteria for different intervention types (grants, tax allowances). Also, annual reporting is a pre-condition for the allocation of the subsequent annual funding tranche.
Monitoring	The Federal Office of Economics and Export Control keeps records of funding cases; data is collected at the responsible Land-level bodies.	Regional government monitors each ROP alongside Commission. Managing Authorities are required to submit an Annual Implementation Report to the Commission for each OP.	Monitoring of performance took place annually through annual performance reporting (as part of the RDA's Annual Report and Accounts) to BIS and then to the UK Parliament.	Important focus on the monitoring of the multi-annual programme and the cantonal implementation programmes based on a model of 'integrated performance and impact management'. Controlling, reporting and monitoring instruments are being deployed in an unprecedented way with a joint monitoring instrument for all cantons.
Incentives	-	performance reserve fund for the ROPs to reward those regions with the best financial performance, plans for new reserve in reformed territorial contract.	As budget allocations to the RDAs are formula-driven and reflect the economic situation of the region, there are few financial incentives or sanctions in operation. To a certain extent, reputational incentives are used to ensure the performance of RDAs.	-
Sanctions	The Land-level institutions in charge can claim back the funds or adjust the conditions.	De-commitment of funds not spent within a specified period	-	The programme agreements contain specific information on adaptation modalities, consequences of non-compliance, and mediation procedures. Funding that has not been committed by the end of 2011 needs to be paid back to the federal level.
Evaluation	Evaluations are typically commissioned by	It is a regulatory requirement to conduct	Evaluation takes place at regional	Evaluation plays a crucial role in the

	Germany	*Poland*	*United Kingdom*	*Switzerland*
	the Federal Ministry of Economics. A matching approach compares the performance of firms in receipt of GRW funding with other comparable non-eligible firms. Recently, a major evaluation looked at the business-support side of the GRW.	ex-ante and ex-post evaluations of ROPs. Polish national and regional authorities increasingly active in ongoing evaluation.	level (commissioned by the individual RDAs) and at national level (commissioned by BIS). There is a strong emphasis on impact evaluation.	overall NRP programming cycle: After four years, a mid-term review of cantonal implementation programmes is carried out at the federal level based on the cantonal reports. The Federal Council is responsible for the final evaluation of the programme after eight years and for reporting to the Parliament.
Quality Assurance and Control	The Courts of Auditors of the Länder check the implementation of GRW funds (assessing the legality of notifications of approval, checking the settlement of the funding, checking reports on expenditure). In addition, the Länder courts assess the efficiency of funding implementation arrangements and carry out on-the-spot checks. The results of these audits can be communicated to the Federal Court of Auditors, which may in turn inform the Federal Ministry of Economics and Technology with regard to particular cases.	Multi-level assurance system for regional policy, driven largely by arrangements for the management and implementation of Cohesion policy. Assurance responsibilities are divided into two independent processes: external control carried out by audit authorities at national and regional levels, and control and audit carried out internally by regional governments (see Annex). As ERDF financing flows through the contracts, they are also subject to financial audit and control from the European Commission.	RDAs formally accountable through their Chairperson to BIS and its Secretary of State, and they must submit annual reports and audited financial accounts. The RDA Chief Executives are personally accountable for the effective and efficient management of public money to Parliament (through BIS, their sponsor Department).	Control and audit arrangements are set out in the programme agreements concluded between the Confederation and the cantons. They generally state that audit bodies of both levels can realise on-site inspections to check the existence, completeness and accuracy of data provided by the canton. Checking modalities are agreed in advance by the Federal and Cantonal Audit Offices. If a joint approach is impossible, the federal office can carry out on-sight controls alone, but the cantonal office always needs to be invited to the final meeting. Audit reports are submitted to all involved parties.

ANNEX 3: COMPARATIVE ANALYSIS OF NON-EUROPEAN CASES

	Canada (ACAO)	Japan	US (ARC)
Scale	Enterprise Development Program ($174.3 million planned spending 2010-11, 46% of budget); Community Development ($160.4 million planned spending 2010-11, 42%); Policy, Advocacy and Coordination ($13.7million in 2010-11, 3%); and Internal Services ($40.4 million for the 2010-11 year, 9%).	No data.	ARC funding 1965 to 2009 cumulative total of $9.2 billion in federal funding for the ADHS (roads) and $3.5 billion federal funding for Area Development. In 2009, the ARC received $439.9 million for the AHDS and $75 million for area development
Rationale	To address spatially unequal regional economic performance in Atlantic Canada Area.	To respond to the long term economic, demographic and environmental changes and shifted the emphasis from the construction of top-down strategies to those built on the wide-area region-centred plans proposed by blocs of prefectures grouped into regions.	To assist the region in meeting its special problems, to promote its economic development, and to establish a framework for joint federal and state efforts toward providing the basic facilities essential to its growth and attacking its common problems and meeting its common needs on a coordinated and concerted regional basis
Legal Basis	Atlantic Canada Opportunity Agency (ACOA) Act was first passed in 1985 (ACOA was then subsequently established in 1987) and has been augmented with 4 supplements since then.	The Comprehensive National Development Act was revised with the enactment of the National Spatial Planning Act of 2005 which initiated the reform of the whole National Spatial Planning System and its relationship to the development of National Land Use Plans.	1965 Appalachian Regional Development Act (ARDA),
Overarching Objective(s)	ACOA purpose to increase opportunity for economic development in Atlantic Canada and to enhance the growth of earned incomes and employment opportunities in that region.". Objectives: establish SMEs; develop entrepreneurial talent ; support business associations, conferences, studies, consultations and market research; develop business opportunity data banks and network; improve communication and cooperation among businesses; promote scholarship related to business and investment.	Promoting endogenous growth, with a focus on the provision of 'softer' business support, including through the promotion of clusters.	Provide a regional development forum; provide grants that leverage federal, state, and private resources; generate a diversified regional economy; serve as a focal point and coordinating unit for Appalachian programs; make the region more competitive; improve workforce skills of the; adapt and apply new technologies; business development; coordination of economic development; development of the Appalachian Development Highway System.
Funding Arrangements			
Sources of Policy Funding	Federal government budget.	Combination of national and prefecture sources, often flexible, ad hoc arrangements.	Annual requests for federal funding from the. State and local governments (and some non-profit organizations) also contribute through co-finding (see below)
Funding instruments	ACOA can assist businesses to locate and/or develop in Atlantic Canada, making and guaranteeing loans to individuals for that purpose	Local grants, transfers from central government ministries.	Construction contracts to complete the AHDS, grants and projects for the construction of basic non-highway infrastructure and related facilities. Grants to groups

	Canada (ACAO)	*Japan*	*US (ARC)*
	as well as awarding grants and other contributions.		to provide healthcare, training programs, and local capacity building. Basic funding for research assistance and financial support for local development districts. Modest revolving loan support for SMEs.
Allocation of Funding	Funding levels reflect historic allocations, pre-dating the formation of ACOA, along with responses to funding plans and requests, like any other federal government department. Annual budgetary requests are supported by the annual Plans and Priorities. From the Plans and Priorities, the budget is assessed as part of Canadaian budgetary process, Program and region priorities generally guide the allocations to the regional offices, though per capita allocations are common. Distribution between enterprise development and community development is determined in the regional offices. At the 'bottom' level, individual enterprises or communities make application for funding, including as a response to project calls.	For central subsidies, competitive process for local authorities. For regional blocs, ad hoc pooling of resources.	Coordinated effort of all ARC-state transportation planners jointly deciding the highest priority projects. Also, ARC funding for Area Development, typically used for smaller grants related to specific projects. 30% directly to distressed counties 70% allocated to the states based on a formula that weighs factors such as population, land area, educational attainment, and per-capita income.
Traceability of Funds	The reporting requirements are the primary means of performance assurances. Canadian Office of the Auditor General (OAG) has the responsibility to report to Parliament on ACOA performance. ACOA maintains a searchable Project Information website that identifies all ACOA funded projects back to 1995. Transparency ensures a level of accountability as project information is available 60 days following client acceptance of written offer.	National and local audit.	Internal ARC procedures assuring that grants are properly awarded and monitored. ARC maintains an independent unit that audits procedures and expenditures. External auditors from the private sector produce financial statements.
Co-financing Arrangements	Business Development Program has range of funding arrangements. ACOA offers unsecured, interest-free loans towards eligible costs. Loan have varied levels of assistance, repayable on a time schedule tailored to the circumstances. Contributions to non-commercial organisations non-repayable.	Combination of national and prefecture sources, often flexible, ad hoc arrangements.	ARC has matching requirements for its projects in its quest to leverage other sources of funding. Area Development projects: at least a 50% match, falling to 20% for projects in “distressed counties”. The source of these matching funds: state and local governments (and some non-profit organizations). Federal government and the 13 member states share equally the Commission’s operating expenses.
Programme Design and Coordination			
Strategic Processes	Federal government provides the broad policy framework and the budget, and develops and refines policy objectives with input from provincial	Wide Area Regional Plans (WARPs) are being developed for eight regional blocs of prefectures, amounting to 45 of Japan’s 47 prefectures.	Five-year strategic plans incorporate input from private citizens, local governments, its regional local development districts (LDDs), state governments, with

	Canada (ACAO)	Japan	US (ARC)
	governments, local businesses and communities, through ACAO local and regional offices.		some input from federal agencies.
Coordination and Collaboration	See above.	Flexible: no formal rules on the level of access to central government on the part of local areas and local authorities collaborate on an ad hoc basis. emergence of WARPs points to the commitment of central government to new forms of regional plans. new governance organisations have also been set up, one for each regional bloc grouping, and these are known as Wide Area Regional Councils WARCs, and these are made up of government offices, prefecture governors' offices, mayors' offices, and business representatives	Explicit and detailed guidelines provided in at Congress level and associated ARC Code. Bottom-up input in setting policy directions through the priorities put forward by each of the state governments. Governor's plan is augmented by annual "strategy statements." Projects for ARC approval are included in these statements. State plans incorporate input from stakeholders including the LDDs. Flexibility for year-to-year changes.
Programme orientation	Three main programme areas: enterprise development, community development, policy advocacy and coordination.	WARPS will cover broad spatial and economic development.	Increase job opportunities and per capita income; strengthen capacity to compete in the global economy; develop and improve infrastructure
Programme Structure	Multi-annual programmes and sub-programmes.	No data.	Multi-annual programmes covering a five year period, can be adapted annually.
Performance Management			
Use of Conditionality	Reporting requirements are the primary instrument of conditionality, annual to ACOA president and 5-year to Minister. Ex-ante conditionalities set out in eligibility criteria. Environmental and ethical criteria included.	Targets and criteria attached to central government transfers.	ARC is a collegial organization that does not have the authority to insist on formal conditions of reform or changes in governance. Has conditionalities for management of construction grants, the need to meet ARC strategies and objectives, the need to follow applicable federal guidelines for projects, and the need for project reporting. Implicit conditionality: funding is targeted to economically distressed counties.
Monitoring	Close monitoring of programme by local and regional agents of ACOA. disaggregated by type and compared with performance targets and reported annually.	For central subsidies, interim monitoring or assessments are possible. Not usual or obligatory, but central government can enforce these if it feels this is required. Targets can be adjusted or revised in exceptional cases. Detailed manuals with assessment criteria available to aid the assessment process. Central government provides data and criteria and example reference cases, but local authorities and municipalities	ARC grant oversight is provided by the program coordinators who are in charge of authorising disbursements and of monitoring progress and final reporting.

	Canada (ACAO)	*Japan*	*US (ARC)*
		also have their own information and data.	
Incentives	Benchmarking - Comparisons with the Canadian benchmark are provided for a number of Indicators in 5 yearly ACAO reports to the Canadian parliament.	For central government subsidies, local authorities compete ex ante between themselves in terms of the quality, innovativeness and costing of their project proposals.	ARC generally does not employ explicit incentives or sanctions for poor performance.
Sanctions	In the event of failure to comply, or business failures, it is not clear that there are consequences for the client, other than the withholding of any outstanding funds. In general prevention would be preferred to sanctions.	No sanction, subsidy amounts not dependent on the outcomes of the ex post assessment	Implicit reputational sanctions Serious threat of sanctions for poor financial management or poor project reporting.
Evaluation	ACOA conducts its own internal evaluations of the relevance, success and cost effectiveness of its programs and initiatives, including through client satisfaction surveys. Perceived need for improved through systematic and regular external evaluations using more modern objective and quantitative methodologies that identify impact for the region as a whole.	Peer review evaluation system for local government projects. Ad hoc and informal process organised by local authorities. Reputation effects very important in Japanese local and regional government, and competition allied with publicity can change performance.	Strong evaluation tradition but challenges in developing objective, robust results. More quantitative statistical approaches could be used.
Quality Assurance and Control	Follows federal government requirements, and those set out in the ACOA Act. Reporting and transparency crucial. Audits, within ACOA and by the Office of the Auditor General of Canada, provide additional detail, checks and balances. In terms of project performance, a high level of assurance is provided by intensive monitoring and mentoring, as well as in setting goals and objectives that are achievable. Assurance processes are closely tied to the stated objectives of programs and requirements and less so to the overall performance of the local and regional economies.	National and local audit authorities.	Through multi-level ARC governance structure, and the independent audit process provided by the Office of the Inspector General.