

**Civil Society working group on EU financial support
European Active Citizenship Group**

**Response to the public consultation on the review of the
European financial regulation**

Brussels, 18 December 2009

This paper is the result of the collective work of civil society members of the European Active Citizenship established as part of the structured dialogue with DG EAC.

From this a working group was created in September 2009 to focus on EU financial support to civil society organisations.¹ Since September the working group has met twice to look at the review of the European financial regulation (FR). After an electronic consultation this response has been endorsed by the group.

The paper includes answers to the 11 questions in the public consultation and an additional issue raised by the group. All the members of the working group are well acquainted with European grants and are recipient of an operating grant from the Europe for Citizens Programme.

The work of the group draws on the “Striking the Balance” report² produced in 2005 by a coalition of NGOs and on an independent consultation organised by Euclid Network in August this year.³

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¹ List of Members Appendix 1

² [Http://www.euclidnetwork.eu/data/files/striking_a_balance_final.pdf](http://www.euclidnetwork.eu/data/files/striking_a_balance_final.pdf)

³ http://www.euclidnetwork.eu/data/files/consultation_on_the_european_financial_regulation_review_by_euclid_network.pdf

Introduction

In the opening speech for the second mandate at the European Parliament (3rd September 2009), the President of the European Commission, José Manuel Barroso, repeatedly referred to the central role played by civil society⁴ in tackling the challenges faced by the European Union.⁵

The role of civil society is also acknowledged in the Lisbon Treaty. In Article 11 it states that: “*The institutions shall, by appropriate means, give citizens and representative associations the opportunity to make known and publicly exchange their views in all areas of Union action.*”

Civil society has a unique role in Europe, enhancing, promoting and monitoring the quality of life of individuals, groups and society at large. It is a source of social cohesion and solidarity, engaging citizens both through value based campaigns and the provision of essential services such as education and healthcare.

Civil society has been at the forefront of campaigning for human rights, equal opportunities, environmental protection and international development with remarkable success achieved in Europe, and worldwide.

The role of civil society in developing innovative solutions to tackle poverty and social injustice, and as a source of social innovation (e.g. the fair trade label and public services) has been increasingly recognized by the European institutions.⁶

Civil society can be an efficient and effective partner in developing and implementing the EU’s objectives. Its organisations are trusted by the general

⁴ Civil society is formally organised as associations, charities, cooperatives, mutuals, NGOs, foundations and social enterprises ranging from small to multinational organisations. It comprises, in fact, the entire not-for-profit sector. Despite their diversity, all organisations share a mission focused on public good beyond private gains. Being not-for-profits, they can make a surplus at the end of the year, but must reinvest this in their mission and can’t be redistributed directly or indirectly. Their boards are normally elected by members/beneficiaries and being a trustee is an unpaid job. Organisations have a certain number of volunteers and attract contributions in kind. The latter two are unique characteristics of civil society.

⁵ José Manuel Barroso, President of the European Commission in *Political Guidelines for the Next Commission* (Brussels, 3rd September 2009)

⁶ *Reinvent Europe through Innovation* by DG Enterprise (see http://ec.europa.eu/enterprise/policies/innovation/files/panel_report_en.pdf); Patrizia Toia MEP’s report on social economy (A6-0015/2009); *Getting to the end of the tunnel: creating the right environment for the Social Economy* by EESC (see http://www.eesc.europa.eu/groups/3/categories/soceco/booklets/EN_Web.pdf).

public,⁷ they have developed unique expertise and networks, and their staff are moved by a passion for the cause, which means they can mobilise great resources, especially on a voluntary basis. They also tend to have lower operational costs than similar commercial organisations, because individuals work for the social mission rather than pure profit and they do not need to distribute any surplus.

However, being non-profit means that civil society organisations need to raise the funds to undertake their activities. The EU recognises this value, and as a result has been an important and significant contributor of funding through grants.

Unfortunately the Financial Regulation (FR) adopted in 2002, with a view to addressing the public demand for more stringent control in the management of EU funding, has also proved an onerous and frustrating experience for much of civil society: the high administrative burden, lack of coherence between and complexity of the FR and Implementing Rules undermine the sustainability of organisations and are an obstacle to innovation and effective project delivery.

The expertise of civil society and its added value are not acknowledged in the FR. Civil society organisations are treated as commercial organisations limiting a more productive partnership between them and the EU.

As Jacques Delors recently stated: “L’avantage de la société civile est sa plasticité, son ouverture et sa sensibilité au monde.”⁸

A crucial change to the EU financial culture would be to accept a reasonable level of shared risk to support and grow civil society across Europe. This would increase trust, and stimulate innovation and a genuine culture of partnership.

The public consultation on the next FR is therefore an extremely welcome and necessary initiative. This report demonstrates that the value of European funding can be increased without creating additional costs, by improving the FR and clarifying the Implementing Rules.

An improved FR could contribute to fostering the financial sustainability that civil society needs in order to be more effective in challenging times and yield a better return on investment, while improving the European Commission’s own efficiency and effectiveness, and promoting a culture of social investment.

⁷ The Trust Barometer launched at the World Economic Forum in Davos in January 2009 has provided evidence that NGOs are the most trusted organizations by citizens amongst all sectors (See <http://www.edelman.co.uk/files/trust-barometer-2009.pdf>)

⁸ See <http://www.euractiv.com/en/opinion/delors-critical-lisbon-treaty/article-187924>

List of priorities

This is the list of priorities in the changes in the new text of the FR based on the view of the working group. Every priority is linked to the respective question as listed in the public consultation of the EC.

Rating of priorities

1. Non-profit rule (Question 4)
2. Co-financing and in kind contributions (Question 2)
3. Lump sums/flat rates and contribution to indirect costs (Question 3)
4. Bank guarantee (Question 9)
5. Operating grants (Question 6)
6. Pre-financing (Question 8)
7. Application procedure (Question 11)
8. Low value grants (Question 5)
9. Cascading grants (Question 7)
10. Level of thresholds (Question 10)
11. Calls (Question 1)
12. Exchange rate

Answers to the questions of the public consultation of EC DG Budget⁹

Question 1: Are you significantly informed about upcoming calls for proposals in a timely manner? What improvements would you suggest?

Problem

The main issues to arise from the current system are caused by of a lack of centralised information directed at civil society organisations.

Despite the calls being widely published, the lack of a single and easily accessible directory can cause confusion amongst applicants about where to find information. A further problem emerges for organisations which lack familiarity with the current system e.g. first time applicants or new organisations. These organisations are often not aware of calls that might be suitable for them or where to find them. This also becomes an issue of organisational capacity. A small organisation might not be able to justify allocating the time to searching or waiting till an appropriate call is published. On the receiving end of this, the Commission may at times get proposals from applicants who are not knocking at the "right door", which results in a waste of time both for them and for the Commission.

The language can also present an obstacle because of jargon, and translations which are not always accurate (or even available).

Due to the tight deadlines of some calls, combined with the lack of a notification about upcoming calls, a situation arises where organisations hastily prepare applications, and do not deliver projects to the best possible standards that they might, had the applicants had more time. Once a project has been awarded a grant, it is very difficult to amend the program.

Testimony

"It is a nightmare trying to find out about the current calls for proposals in the EU's massive website. It is not easy trying to browse through all the departments trying to find out this information and in most cases if one does, it is only a few days left to closing deadline. The guidance always tend to be complicated and full of technical words/jargon and cross references to even more technical papers.

⁹ http://ec.europa.eu/budget/library/consultations/FRconsult2009/consultation_paper_en.pdf

Over the last two years we have been searching for opportunities that link with our strategic plan. We have attended workshops in this regard but have yet to find out the best way to get the information about the open calls. I understand that one way is to keep visiting the website but in most cases we end up lost in the EU website.”

Perez Ochieng, SACOMA

Proposed Solution

The first step to rectifying this situation would be to create a centralised database / directory spanning all DGs. This system could include calls which, although not yet open are forthcoming, including the main purpose of the grant and the profile of targeted organisations, as well as indicative amounts. This will allow suitable organisations to be aware of forthcoming calls, prepare their applications with ample time and forestall any claims of being unforeseen or unfairness when they do close. If calls were on the database, and there was a system of key words / subcategories / DGs, organisations could sign up for email notifications, much like the current system in place for announcements of public consultations.

The database currently used by EuropeAid¹⁰ is a good example and could be a used as a model for a database covering all DGs.

DG EAC has also introduced a system of programme guide which are very useful for civil society. These guides which are published at the launch of a multi-annual programme, (e.g. Youth programme, Europe for citizens) give easy to read information on the objectives of the programme, the calendar for the publication of calls for proposals, and indications on the evaluation criteria that will be used to select proposals. Again this is a good practice which could be adopted by other DGs.

¹⁰ <https://webgate.ec.europa.eu/europeaid/online-services/index.cfm?do=publi.welcome>

Question 2: Should the rules be more flexible on co-financing requirements taking into account the type of actions and project managers? How could in-kind contributions best be dealt with, while adhering to the non profit principle?

Problem

The aforementioned question covers two major issues for organisations. These are co-financing and in-kind contributions. For ease of understanding they are dealt with in turn.

Whilst acknowledging the requirement by the EC of co-financing as a mechanism to ensure beneficiaries' commitment there are a number of issues arising from its current structure.

1. The double ceiling

Grants are expressed both as a maximum amount and as a maximum percentage and defined in the grant agreement as a proportion of eligible costs, but:

- It is rare that the costs actually incurred end up being the same as those estimated in the project proposal;
- In the current grant agreements, the percentage applied is calculated at the time of the signature on the basis of the amounts of the grant requested and the eligible costs. Most often, this ends up being lower than the maximum percentage allowed by the call for proposals (for example 54.78 % instead of 60 %); legally speaking, it does not correspond to any actual "will" of the parties, but is only the result of a calculation; it is to be noted that the IR does not require this calculation, but only that the maximum rate of funding is mentioned;
- It does not encourage cost effectiveness; beneficiaries who achieve the results of the project at a lower cost and/or despite receiving less external co-financing than originally foreseen (and having more volunteers to do the projects for example) will have their grant cut to match the percentage defined in the grant agreement.

2. Level of co-financing

The working group believes that there should be more transparency in the proportion chosen by the EU and the rationale behind it.

There should also be greater flexibility on the level of co-funding when it comes to supporting national/local organisations which do not have easy access to funding. Not all civil society organisations across Europe are in the same position when it comes to co-funded projects. Civil society organisations from

wealthier nations and those that are well established tend to have easier access to funds. The requested level of co-financing can therefore become a factor of geographic discrimination.

Since the '90s calls for applications have become more prescriptive; they look more like calls for tenders and leave less room for creativity and innovation in civil society. The high level of co-financing is therefore inappropriate.

The current financial crisis also offers an example of how the prevailing economic situation of Member States can cause problems for organisations when it comes to co-financing. Indeed, civil society organisations have reported substantial cuts in their budget this year, while at the same time they are witnessing an increase in demand for their services (e.g. food banks, shelters).

NOTE it has been noted that it would be more appropriate to use the concept of match-funding rather than co-financing

3. In-kind contributions

The issue of in-kind contributions is of major concern to many prospective applicants, being frequently cited as a barrier to applying. Broadly speaking in-kind contributions come in two forms:

- **Voluntary and pro-bono work**
- **Goods and services given by third parties for free**

These are the elements that make civil society unique. Volunteering and contributions in kind are an added value that only the not-for-profit sector can leverage. Excluding these two contributions as eligible costs is a missed opportunity to tap into the unique potential of the sector: specifically, their capacity to mobilise groups of volunteers to work in support of European values and foster donations in-kind to ensure the implementation of project objectives.

The present regulation (Article 172) says that the Authorising Officer can allow for the recognition of volunteers' work. However, practice shows officials are extremely reluctant to engage in this path. "In-kind" contributions are at present not considered an eligible cost.

Testimony

"Due to the financial crisis income in 2008 was less than foreseen, and therefore expenditure was €334,270 less than predicted. As the original co-financing rate was 5.17%; the Commission applied this ratio to the reduced amount of expenditure, to give the EPC a final award of €132 325, instead of €149 606, a reduction of 11.5%. If the Commission had kept the grant at €149

606, the co-financing rate by the Commission would only have increased by a tiny margin: from 5.17 to 5.85 per cent.

We feel that we have been penalised twice: first by the financial crisis and secondly by the Commission applying the co-financing rate pro rata”

Elizabeth Bisland, European Policy Centre

“Most applications require the co-funding to be in cash. This undermines the nature of the not-for-profit sector and the importance of volunteer work in an organization, including ours. We have volunteers and interns whose work we can not factor in the budget. Our organization does also own the office, which for us is a tremendous investment in the sustainability of the organization, but that does not get appreciated in the evaluation and does not count as a contribution.”

Partners Albania, Center for Change and Conflict Management

Proposed Solution

1. Double ceiling

The status of the agreement on co-financing needs to be addressed. If it is reduced through no fault of the delivery partner, then the Authorising Officer should have the discretion to maintain the EU contribution depending on their understanding of the cause of the shortfall and its effect on the project achieving its objectives. Solutions could include the production of a legal form if the partner organisation folds and the situation should be decided on a case by case basis. Member states and other donors, for instance the Office of the Third Sector in the UK, define the ceiling as a total amount and not a percentage.

2. Level of Co-financing

The generally held view is that the need for co-financing should be judged on a case by case basis and allow for more flexibility. The only way of remedying the situation is by:

- Geographical discrimination: some Member states have no tradition of financially supporting civil society organisations. Some MS are more affected by the financial crisis
- Sectorial discrimination: EU funds are increasingly won by larger organisations that are more financially stable to the detriment of smaller and more local organisations.

Considering the factors above and the economic crisis there is a need for more flexibility in co-financing requirements. The initiative of the European

Commission to reduce the minimum co-funding threshold to 5% is therefore welcomed. This flexibility should also include the option to suppress the co-financing requirement and allow for a 100% grant.

Given the highly prescriptive nature of calls for proposals, the possibility for **spontaneous applications** should be reintroduced in a limited number of cases - i.e. projects submitted by civil society without a call for applications. The latter not only creates opportunities for innovation but would be an effective tool to quickly respond to unforeseen circumstances and emergencies.

In addition to this, a database of co-financers and financial partners should be set up to include information at national and regional level.

3. In-kind contributions

To mark the start of the European year of volunteering in 2011, the new financial regulation should make it compulsory for authorising officers to recognise the contribution of volunteers including expertise given on a pro bono basis and sponsorship in kind (goods and services) as co-financing.

The present wording of Art. 172.2 IR should be amended as follows “the OA responsible shall accept co-financing in kind unless he/she justifies why it’s not considered necessary or appropriate”

In order to identify the best model for calculation of the financial value of such in kind contribution¹¹, an advisory group should be established with the objective of making an operational proposal to DG Budget. The group should include European networks of volunteer organisations and civil society representatives.

An appropriate recognition of contributions in kind could solve the problem of co-financing because it would acknowledge resources that civil society is capable of mobilizing for projects:

¹¹ The UN handbook on measuring volunteering, which has been adopted by the International Labour Organisation (ILO), explains how volunteers’ time is quantifiable. There are also examples that could be drawn from the European social fund of how scales have been used to evaluate volunteers’ contribution.

Question 3: Should the use of lump sums and flat rates become the norm rather than the exception? Should the rules allow for costs to be covered on the basis of expected outputs? If yes, can you provide concrete examples?

The two questions will be answered in turn and a specific issue has been added:

Should the use of lump sums and flat rates become the norm rather than the exception?

The answer of the group is negative. Even if the group welcomes the simplification of the work done by the Commission when introducing the system of lump sums, the systems has shortfalls:

- While the system of lump sums and flat rates is easier to administer for the EC, it forces applicants to tailor and downgrade projects to fit within these specific targets and structure of funding.
- Flat rates that have been used are too low and do not sufficiently compensate for the real costs being occurred by an organisation
- Flat rates are based on assumptions vis-à-vis the overall project design and impede on civil society creativity in the execution of a project. For instance, the rates used impose arbitrary ceilings on certain types of project expenditure (e.g. staff costs), while not on others (e.g. travel), implying that certain costs are more valid than others. Consequently applicants are encouraged to increase expenditure unnecessarily in certain areas in order for them to be able to justify their required level of expenditure in others.

The group therefore recommends:

- Maintaining the option for organisations to choose between submitting a budget using a lump sum calculation or one based on real costs.
- Raising the ceiling to market standards. Flat rates must be appropriate, and more flexibility has to be given to organisations in spending such funds. More emphasis should be given to the return on the investment and not just the financial accounting.
- Basing flat rates and lump sums on outputs and not budget. Moreover, they must include outcomes, and civil society organisations must be allowed some degree of flexibility in managing them given that they don't cover the all the costs.

Should the rules allow for costs to be covered on the basis of expected outputs?

In our understanding this is currently the case, at least in theory.

The problem with the proposed system to cover costs based on expected outputs is that it does not recognise that outputs are a means to achieving outcomes. Therefore a balance must be found in terms of focusing on both outputs (i.e. products) and outcomes (i.e. impact) together, because only focusing on outputs would remove the innovative nature of many applications, as the focus would inevitably shift towards safe, predictable and easily guaranteed outputs.

The two obvious challenges with covering costs based on outcomes are that they are not immediately realised, and they also depend on external factors outside of the implementers' control. Therefore developing a suitable, equitable methodology for assessing outputs and outcomes is required.

Contribution to Indirect Costs

This issue has been raised as a priority and the working group found it appropriate to address it in this session.

The issue with the current system relates to the level of the cap to cover indirect costs. The current 7% cap to cover indirect costs is set too low to allow organisations to cover their overhead costs. Not even commercial organisations can run so efficiently. This results in overheads being cross-subsidised from other parts of their budgets or even different projects. This also does not fit in with transparent practices, as organisations in effect hide real, incurred costs.

Testimony

“The 7% cap on indirect expenses for implementing an EU grant does not allow, in the majority of cases, for NPOs to recover full overhead costs on the project. As a result, it negatively affects the financial sustainability of NPOs; prompts them towards less transparent practices of allocating overheads; and prevents NPOs with smaller operational budgets to apply for EU grants. We recommend that the EC should allow for higher indirect cost ratios on a broader basis than the current practice.”

The 7% cap on the indirect (or administrative) expenses for implementing an EU project is lower than the actual overhead ratio for many NPOs, especially those which are smaller and medium-sized. Since there is no way to

compensate for these costs (they cannot be charged to the project) it results in an inevitable deficit for the project that the NPO undertakes. In our opinion, it is extremely counter-productive to have a financing scheme with a built-in loss for NPOs. For instance, the administrative expenses of the European Center for Not-for-Profit Law (ECNL) in 2007-2008 equalled on average 20% of the operating budget. During this time, ECNL implemented an EU project financed by EIDHR, and since it could only allocate 7% of the project related administrative costs to the project, it had suffered 13 cents loss on every one euro spent on (or 13% of the total cost of) the project. As a result, our board decided that the organization should not apply for EIDHR funding despite the fact that it could greatly contribute to the objectives of the EIDHR in several regions.

In our view, an overhead rate anywhere between 10 - 30% can be considered as normal, depending on the situation; in fact, a professional NPO needs 22 proper systems for accountability and monitoring of its projects, which in themselves contribute to the administrative expenses and come at a cost. We know of several other NPOs which have had the same problem; some of them overcame the problem through a less transparent allocation of its overhead costs, which runs counter to the EC's efforts to increase transparency and accountability. A rule that produces a loss for NPOs undermines the organisations' financial sustainability and/or integrity, and does not contribute to the well-being of the NPO sector as a whole.

The Implementing Rules of the Financial Regulation already contain a provision that allows exceeding the 7% ceiling "by a reasoned decision of the Commission" [Art. 181.(3)]. However, this provision lacks any further instructions or guidance as to how it should be carried out and is hardly implemented in practice; in fact, the large majority of projects under the current instruments limit administrative expenses chargeable to the project to 7%. We recommend that a) the generally applicable indirect cost ratio be set higher; and b) that the Implementing Rules elaborate on the procedures to determine when and how a different ratio can be applied."

Nilda Bullain, European Center for Not-for-Profit Law.

Solution

There are two possible solutions.

1. One is to raise the flat rate to a more realistic level, or range. **A rate of 15-20%** could still stimulate organisations to become more efficient, whilst covering costs and fostering transparency. This is the average cost of overheads incurred by an organisation when delivering a project.

2. Another solution could be the **full cost recovery** method as used in the UK.¹² In addition to this, organisations which receive an operational grant should be allowed to apply for indirect costs for further projects.

¹² See www.fullcostrecovery.org.uk

Question 4: Should the rules strictly adhere to the non-profit principle or should there be room for some flexibility in this matter? Do you have examples of good practices from other public authorities?

Problem

The non-profit principle is a major problem facing civil society organisations (in particular those receiving operating grants) and should be addressed as a matter of priority in the new financial regulation.

In order to do so, the group recommends the European Commission clearly differentiates between operating grants and project funding.

The crux of the problem is that the rule fails to take account of the fundamental nature of organisations involved in applications. They are not organisations set up with shareholders or profit goals at their core.

1. Operating Grants

Operating grants are available to an organisation which pursues an aim of general European interest. The grant goes towards running costs and can range from a few percent to being the core source of an organisation's funding.

At present the non-profit principle impacts negatively on civil society organisations for the following reasons:

- The rule acts as a disincentive for organisations to look for extra funding as this would automatically be deducted from EC grants.
- The rules undermine the capacity of organisations to maintain or constitute reserves. This affects their financial sustainability and goes against the objective of the EU to build or support sustainable organisations. It is also worth noting that some national laws (e.g. Belgium) impose the creation of reserves to guarantee the wage for a certain number of months for each member of the staff. These reserves are also essential to cover unexpected and unbudgeted for changes in an organisation (e.g. delayed payments by the EC or non renewal of an operating grant). Reserves are also requested by banks to provide financial guarantees.

2. Project grants

Organisations are not allowed to make a surplus with project grants, which is reasonable, however, they shouldn't subsidize the costs of undertaking a project funded by the EC.

Organisations receiving an operating grant can't claim the overheads in applications for project grants. This limitation doesn't take into account that every new project includes its own overheads and it is a disincentive for undertaking more projects because organisations have to subsidize the overheads.

Furthermore, the non-profit rule and the co-financing rule need to be looked at together when considering this issue.

The EU deems an NGO to have made a 'profit' after accounting for the combined partners' and the EU's contributions. The EU's objective is maximising the leverage of its own funds; the issue is not really about making a profit when comparing the project costs to the EU's own contribution. Making a profit against the EU's contribution would be a very unusual scenario.

While a case can be made for the non-profit rule, the EU in effect offers a 'loss-making' rule even after partner contributions:

- On average, we understand that only 10% of applications are successful. Applying for grants is an increasingly complex process, particularly where translations are required. Hence significant losses are made by civil society when applying for grants.

Some project related costs do not qualify even though they've been incurred as a result of the project. For example, if a category of cost is more than 10% higher than the grant budget any expenditure over the 10% is disallowed, no matter what the reason was for the variance. Note, this is the case when the total expenditure was within budget and tasks were properly carried out. An example of this is when work is switched between the organisation's staff and sub-contractors for the benefit of the project.

Testimony

"The non-profit constraint is counter-productive. With core costs being so central to an organisation's operations, especially for small and new organisations that have not yet developed a strong administrative base, the strict limits on building up any reserves are very prohibitive to an organisation's long term sustainability. A more appropriate system would enable (and should encourage) the build up of reserves within the boundaries of good practice, i.e. 3-6 months' running costs, enabling grantee organisations to have a more sustainable future and securing the donors' investment".

Proposed Solution

1 Operating grants

The working group considered different solutions as ranked below:

A) The optimal solution would be to exclude operating grants given to organisations pursuing a European general interest from the scope of the non profit rule: the list of 109.3 FR, excluding some grants from the scope of the non profit rule should be extended to "d) operating grants to organisations pursuing a European general interest", (provided that it has confirmed the non distribution of surplus, even indirectly capping salaries and bonuses as is done in the UK).

It's also necessary to distinguish between "profit" that can be distributed amongst shareholders and which is not related to non-profit organisations, and "surplus" which can be generated by civil society organisations and is reinvested in the organisation as a contribution to the mission or stored in the reserves.

B) An acceptable solution would be to allow a certain level of surplus - *de minimis rule* - or to build reserves up to 3-6 months as in Germany. In the actual text of the FR political parties are allowed to carry over a surplus to the following year which can be used for its mission up to the end of the first quarter (art 109 FR).

C) The last resort would be to carry over the surplus with a break even over 5 years.

2 Project grants

In the case of project grants, if the funding of a project is based on deliverables and these deliverables are achieved having spent less than the project budget, but more than the EU contribution, then the NGO should be allowed to retain the surplus, as long as its objectives do not counter those of the EU and the statutes do forbid distribution. There may need to be restrictions on it being put towards salary increases or bonuses. The rule should be that if a project is based on cost recovery then only cost incurred should be recovered.

In some Member States' equivalent to the FR, there is already a stipulation that a civil society organisation can make a surplus, but this must be fed into a

Reserve Fund that can be accessed at a later date if needed to cover future deficits. Examples of this are as follows:

Czech Republic

ACT No. 248/1995 Coll. of 28th September 1995 on Public Benefit Corporations and on the change and amendment of some laws PART ONE, CHAPTER I, BASIC PROVISIONS, Article 2

c) the profit of which may not be used for the benefit of its Founders, members of its bodies or employees and must serve to render the generally beneficial services for which the Public Benefit Corporation was established.

CHAPTER V, BUSINESS MANAGEMENT OF THE PUBLIC BENEFIT CORPORATION, Article 17

3) The net profit as reported at the end of the fiscal year shall be transferred by the Public Benefit Corporation to the Reserve Fund in its full amount. The Reserve Fund shall be first used to cover any losses reported in future fiscal years.

Latvia

LAW ON NON-PROFIT ORGANIZATIONS, 17 December 1991, as amended 5 November 1993 (unofficial translation) CHAPTER II. Basic Principles of Operation of Non-Profit Organizations Article 4. Reserve Fund.

Non-profit organizations shall transfer the assets exceeding their expenses into the reserve fund that shall be transferred to the next economic year without imposition of the profit tax. Such profit may not be withdrawn or paid to the participants, it may be used only for purposes provided for in the Articles of Incorporation. In the event of liquidation of any non-profit organization, fixed assets or other property purchased for assets of its reserve fund may not be divided among its participants.

Question 5: What, in your view, would be the appropriate amount for low and very low value grants?

Low and very low value grants offer the opportunity to take risks giving room for innovation and would work as a seed fund for start-ups and grass-root organisations. Therefore the working group recommends a threshold of 150'000 € for the low value and 20'000 € for very low value.

Naturally this is rough figure as the value depends on the country where the project is implemented i.e. the costs in France are not the same as in Uganda.

Question 6: How could the rules on operating grants be more flexible? In which way? What are your views on the duration of framework partnership agreements?

Problem

A major part of this issue relates to the non-profit constraint, which has been discussed in the answer to question 4. The building up of reserves and operating costs are so intrinsically linked that they need to be addressed together. The other problems are:

1. Organisations awarded an operational grant can't apply for indirect costs in further applications for project grants, even if they receive only a small operating grant as a percentage of their total expenditure. New projects increase indirect costs beyond the overheads covered by an operational grant.
2. Beneficiaries of operating grants are not like project promoters. Their specificity should be recognised and their grants should be handled in a different way. The operating grant supports the normal day-to-day work of organisations which are considered key interlocutors for the EC because of their mission and regular activities. Currently the applications resemble those made for a project grant and demands far too great a level of detail. Creating budgets to a level of detail which includes how many people will attend a conference to be held in 12 months time, from which country and how they will attend, is at best inappropriate and never accurate.
3. Timing for signatures is too spread out over the year putting organisations at risk. The decision of the EC often comes several months into the start of the financial year, not to mention the pre-financing. This creates a very difficult situation for organisations in terms of cash flow: while they are still waiting for the final payment of the previous year's grant, they have to wait 4 to 6 months to receive the first payment of the current year's grant. This is also linked with the first issue: if the level of detail required was more acceptable, it would be possible to send an application much earlier during the previous year.
4. Operating grants should not automatically be based on the logic of progressive increase of co-financing requirement. Some organisations that have been established on the basis of European public interest cannot, by their very nature, become independent of EU funding nor fundraise at national level or through private donors.

Testimony

The rules of Operating Grants present two main problems. They limit the possibility to cover indirect costs of partners. SOLIDAR has received an Operating Grant from DG Education and Culture to implement projects together with national and local partners. The Operating Grant covers indirect costs of SOLIDAR secretariat but not the indirect costs of partners. This limits their ability to contribute. Moreover, they are penalized because they can't include indirect costs in other project applications (for instance with DG EuropAid or EMPL).

The rules of Operating Grant also do not cover all indirect costs of organisations with a diversified portfolio (activities in different fields). Not all initiatives of SOLIDAR and its members are part of the work plan to which DG EAC Operating Grant contributes. Take for instance “capacity building of member organisations on disaster preparedness” and “developing a EU-wide rapid response mechanism for humanitarian aid”: SOLIDAR members have to find funding elsewhere for such activities. ECHO provides financial support for this type of EU network and capacity building only in the form of covering indirect costs, but is not accessible for SOLIDAR.

Maurice Claassens, SOLIDAR

Solution

1. Beneficiaries of operating grants must be allowed to claim indirect costs for projects which aren't included in the action plan submitted for the operating grant.
2. The process should be more pragmatic and based on agreeing objectives rather than micro-managing spending. The level of detail required from applicants for operational grants needs to be reduced. A structured partnership needs to be developed, starting with a database of beneficiaries. (See the answer to question 11).
3. The results of the applications must be communicated by the end of the previous year and signature of the contract must be done by the beginning of the financial year (February at the latest).
4. On the issue of progressive increase in co-financing requirements we would recommend deleting article 113.2
5. Framework agreements: they are welcomed as long as they allow organisations long term planning and include annual action plans. They could

be extended to 5 years in specific cases as is the case with contracts for commercial organisations.

Question 7: Can you give concrete examples and types of actions where the strict limitation on cascading grants became an obstacle for achieving the goal of your action?

Problem

The current regulation is seen as too restrictive in terms of the level of sub-grants that can be further distributed. The current amount designated for reallocation is generally considered too low. It does not take into account local connections and links organisations have with each other which could deliver the project in a much more beneficial way, whilst still working in tandem with the organisation that received the grant. The current system does allow for some projects to emerge through the redistribution of funds, and due to restrictions the scope of these projects can be too narrow and the impact can be minimal.

This problem is particularly acute when a grant is awarded to a network. Networks, by their very nature, will have access to a wide range of partners in similar fields, and the limits to sharing of knowledge and capacity can be detrimental to the efficiency of a project. The provision can also actually negate some of the effects the project has. If a project delivers training, and the trained group or individual then want to use the knowledge gained, it would be logical for them to do this within the scope of the project. However, this is often not possible or at least the outreach is restricted.

Testimony

“The global 100k threshold can impede on project design, especially if it is applied without taking into account the total budget volume. For the time being the amount of a proposal is not related to the threshold i.e. when working on a 4 MEUR proposal, the rules provide for the same threshold as with a total budget of 300.000.

We would suggest a link between the maximum amount of sub grants possible and the total budget available per projects.”

Concord

Proposed Solution

As alluded to in the previous quote the solution to this problem is linking the maximum amount of sub grants with the total budget per project. This simplification allows more scope for partners to be involved and in whatever arena is deemed appropriate within the projects aims. Although there is an understanding that the current situation aims to act as a safeguard to the

distribution of grants there should be enough checks in place in other parts of the application and deliverance of grants that could allow sub granting within the scope of the rules.

Member States frequently use grants to outsource to third parties (both for-profit and not-for-profit organisations), especially in international development.

Question 8: From your experience, what alternative solutions could be proposed for pre-financing payments while safeguarding tax payers' money?

Proposed Solution

The solution comes in a series of steps, the objective of which is to maximise the number of applications from organisations that can deliver the project objectives and are financially robust.

Firstly there should be a proper 'pre-application' process for grants to better ascertain the quality of potential applicants outside of project timetables. Organisations can ascertain whether they are eligible to apply for grants from any part of the EC prior to their completing the whole applications (many civil society organisations incur the costs of applications only to be rejected at the eligibility stage). The benefits of this from the EU's perspective are: That they can give the job of reviewing the company's documentation to experts who understand what they are reading no matter which national legislation it falls under, or in which language it was produced.

Eligibility documentation should include:

- a. The organisation's up to date published accounts
- b. The director's biographies
- c. The members, their financial strength and their structure
- d. The organisation's history
- e. The organisation's objectives and confirmation that they do not conflict with those of the EU

The process can continue until the EU is happy to take a view on the organisation's suitability (there is no project timetable limitation)

It also has other benefits:

- f. It stops the process of multiple EU departments having to vet the same documentation multiple times, hence improving efficiency
- g. It creates a database where the onus is on the organisation to update it, but allows project histories to be recorded (including audit issues) further increasing EU efficiency and effectiveness.
- h. It would reduce the timetable length of calls for Proposals

This process could be used to give CSOs "credit limits" i.e. the maximum pre-financing for which they are eligible. This is normal best practice in the commercial sector and is well understood. The EU can then demonstrate that they have a widely accepted and recognised process of limiting risk.

Pre-financing should be offered to NGOs with credit limits. The key is to make the process work for the EU and the grant recipient. It should include an agreed schedule of payments for agreed periods or phases of work. Close to the end of each phase the organisation should report, in writing, to the Authorising

Officer on progress, results and expenditure to date. The report should include financial support such as copies of invoices or payroll slips.

The directors should sign the report stating that it is a true, full and fair representation of progress and expenditure.

The Authorising Officer should have the option of calling a meeting, or having an interim audit undertaken, but can only withhold the payment of the next phase if they have proof of inappropriate behaviour or expenditure. Concern or an impending audit should not be an adequate reason.

The Authorising Officer should be required to review the reports, but not be required to certify the interim reports as 'correct' prior to paying the next instalment.

This reporting process should help the EU to ensure better results from projects compared to a full interaction at the beginning and end of the process.

The requirement to pay interest on pre-financing should be removed. It is an unnecessary complication for relatively small amounts of money that acts as an incentive for organisations to put money into non-interest bearing accounts.

If an organisation cannot earn a credit limit, then they must pre-finance themselves but in stages, recovering funds on a periodic, or delivery based mechanism. The reporting mechanism would be the same as pre-financing, but in arrears. Authorising Officers would be aware that these counterparties would represent a higher risk and should be more prepared to check reports. The application should prove the ability to pre-finance.

Question 9: What mechanism, other than pre-financing guarantee, could be explored while ensuring adequate protection of community funds?

Problem

This is another key issue. Primarily because it is not considered an appropriate instrument for what it is supposed to achieve. A guarantee from a bank's perspective is very similar to a loan, it uses their reserves and they have to charge for it. They need some certainty that they will not lose money, usually in the form of security. If civil society organisations have low assets and reserves (see answer to question 2) then it is difficult for the bank to secure against those assets and they may not give the guarantee. If an organisation could obtain a guarantee it could probably obtain a loan and would apply for EC funding.

As a result the request for a guarantee is discriminatory in favour of large well funded organisations, even if they do not have the best skill base for the project, and certain economies where the mechanism is well understood e.g. Belgium.

This use of bank guarantees as a method to ensure the financial stability of an organisation also results in a situation where the reason for giving the grant is sometimes forgotten i.e. funding a project that would otherwise be financially unviable.

A bank may look at future performance rather than assets for assurance. However, performance is often reliant on the EU being happy with the work done and paying the grant. In effect the bank is being asked to underwrite the quality of the work done by the organisation from the perspective of the EU - the very people wanting protection. Thus the paradox: "one of the reasons for supporting civil society organisations is so that they can undertake activities that would not normally be financially viable and yet at the same time, the organisations are expected to demonstrate financial viability in order to meet the requirements" for obtaining a bank guarantee.

Thirdly, the full value of the guarantee normally stays in place until released (project acceptance by the EU). This is usually well after the organisation has spent all the funds relating to the project. As a result a guarantee is often worse for the organisation than a loan when they return to the bank for further funds or guarantees. They also have to pay for the guarantee until it is released.

In summary, a guarantee is a totally inappropriate instrument for the purpose intended. It gives the EU security, while limiting NGOs ability to apply for grants and damaging them financially.

As a concept it is not sound and universally applicable, and as such becomes discriminatory to applicants.

Testimony

“The EU requires the implementing partner to obtain a bank guarantee for that particular year to safeguard the EU’s financial interests. Under the terms of a bank guarantee, the implementing partner would be required to deposit an amount of money equal to the budget for that particular year in a separate bank account, which the bank would hold as a guarantee of performance. Similar to the co-financing requirement, this provision limits participation in EU-funded programs to organizations with insignificant cash reserves that have the financial resources to put forth such as guarantee.

Rather than include such prohibitive requirements, we would encourage the EU to consider alternatives to protecting their financial investment in the project, perhaps by checking applicant references in managing programs of similar size and scope for other international donors, or by performing some sort of prequalification process that would the EU to assess the project management and accounting systems of perspective applicants”

Robert Hurd, National Democratic Institute for International Affairs.

“That too often small NGOs cannot answer calls for tender/for proposals, not because there is a lack of technical or financial expertise, in managing projects -even big and complex -, but because the financial guarantees requested by the Commission, would be a too big burden for the organisation, taking into account its financial account and total turnover.

It would be therefore very useful to introduce in FR some new clauses that offer more flexibility to small NGOs in this regard. Or at least clauses that focus more on the evaluation of “who” is requesting the funds, and suggest some options.”

Cristina Fancello, Generation Europe Foundation

Proposed Solution

A complete revision of the nature of the pre-financing guarantee is called for. The main priority would be discarding the bank guarantee.

As a result the EU mindset should find another solution which is fit for purpose, even if it marginally increases the EU’s financial risk. In reality the financial risk should be more than offset by the increased choice of proposals.

It is important to describe risk. It should be noted that every action has associated risks and that there are multiple risks. Financial failure is one, but poor implementation of agreed actions leads to exactly the same effect - failure to attain objectives while expenditure has been suffered. Changing environments and the undertaking of agreed but no longer relevant actions is another risk and one that is arguably the result of the Financial Regulation itself.

Using multiple organisations for actions creates a 'portfolio effect' spreading risk, both against financial failure but also against failure of performance. Increasing the choice of applicants and methods of achieving the project objectives also decreases risk.

One option would be a system similar to that employed currently by the UN, a **comfort letter**.¹³ This is a document signed by an accountant declaring that an organisation has the appropriate financial systems in place to receive a grant. This proposal could be speeded up with a harmonisation of auditing standards.

In case the Commission has doubts on the financial capacity, it could give the funds more progressively in **split payments**. In fact, this is allowed by the FR but in practice AO tend to request the financial guarantee.

Another complementary solution would be to have a **database** of organisations which are eligible and financially viable (see answer to question 11) or a **prequalification process** as proposed in the testimony.

Finally, a solution for small NGOs, which have neither shareholders nor capital, would be an opt-out clause for the (20%) pre-payments which are often stressful and a strain on them because they necessitate bank guarantees. The conditions could be established through the database recommendations above.

¹³ http://www.un.org/democracyfund/Docs/ANNEX%20VIII_CSOP_3rdR.doc

Question 10: Based on your experience, do you think current thresholds are still adequate or should they be increased, and why?

The working group did not discuss this issue. (article 129)

Question 11: How could the application procedure for both grants and contracts be further improved?

Problem

The sheer number of documents that applicants need to fill in is not only a major administrative burden for applicants who commit to the process, but it can put off prospective applicants. Many documents require a precise level of planning that often does not reflect the reality of the situation.

The Call for Proposal requires a full application including eligibility documentation, concept outline, detailed project plan, co-financing details and proof of co-financing, including full budgets.

Many organisations commit to co-financing for projects that are unsuccessful, but in the meantime reject other organisations' requests (these requests are often for EU Calls for Proposals which, as a result, the applicant cannot respond to).

However, the Commission reviews in stages and a significant proportion fail at the first review (eligibility) from which there is no recovery in costs for the applicant. The EU process can often take months, with rejections being issued at various stages.

The cost of filling in such documents can be huge and the effects are especially felt in small organisations, new Member States and post conflict zones. It can also cause problems for those organisations where a significant proportion of staff is volunteers. These often lack the expertise, understanding or the time to commit to the application process.

The aforementioned point also links in with the issue of the language used in the documents. Often considered long and convoluted, it can act as a disincentive for prospective applicants. Another issue arises in terms of time - not only the time it takes to fill in application forms, but also the time it takes for decisions to be made. In a volatile economic climate, the prevailing state of affairs may change so quickly that information is rendered redundant and outdated.

Another problem arises with frequent applicants. The repetition of information is highly burdensome in terms of bureaucracy and also highlights the issue of record retention. Currently, the time period for record retention is too long, expensive and unrealistic.

It should also be noted that CSOs are closer to the actual situation than most EU officials. A fact that many EU officials lamented and felt that the Financial Regulation, in requiring them to create prescriptive annualised Calls for

Proposals the facilitated easy and transparent comparative assessment, had reduced the impact of many projects.

Testimony

“Application procedures are unnecessarily complex: ...Submit on line (form may not be compatible) but accompany with two hardcopies, a summary in French and English, signed partnership declarations and special extract from accounts for certain finance levels all by precise date... Decision making is slow with decisions frequently taking 6 months and subject to delays which can mean projects have to be redrawn or withdrawn, with decisions on significant changes also taking a long time”

Tamara Flanagan, Community Service Volunteers

Proposed Solution

There is a need for **simplification** of the procedures. A **label** or **passport system** that would store the key details and mean that only immediately relevant information need be submitted. It would also go a long way to improving the current situation. There is already something similar known as PANDOR. Alternatively the system could be based on the information already provided in the register of interest representatives. A shift towards fully online applications would reduce the physical paperwork.

Harmonization of the procedures across DGs and Agencies is vital and should start with the interpretation of the FR going right down to accounting system.

A system of **applications in stages** would be beneficial as it would allow applicants to state their initial ideas and, if desired, proceed with a full application.

Firstly create a database of approved applicants as described in question 9.

Secondly create a series of steps:

1. The first being a concept paper with an outline budget.
2. This should then be followed by a full project description and more detailed budget.
3. Lastly the proof of co-financing is required.

The result of this is that significant expenditure is only incurred if there is a good chance of success and contributors are only approached for formal co-financing commitments when there is a reasonable chance of success.

Finally, proportionality must be taken into account. For instance, additional audits should be required to take place within a given timeframe at the end of the project and a pending audit should not be used as a justification to withhold payment.

The FR should leave some room to the AO for grants given occasionally on a discretionary basis for specific purposes, especially in the interests of promoting innovation or in the case of an emergency as in the case of ECHO.

It worth noting here a previously mentioned point in answer to question 2 - the need to reintroduce spontaneous application as an instrument to promote innovation and quick responses to unforeseen events and emergencies.

Other issues raised by the working group but not addressed in the public consultation

Exchange Rates

Problem

As grants are delivered in Euros a considerable problem arises for those organisations applying from outside the Eurozone. Whilst the FR stipulates that not only must the exchange rate must be calculated using the InforEuro¹⁴ rate but there is also no allowance for the fluctuating exchange rate from the time of application to the time of distribution of the grant.

This can be a major problem for countries where the exchange rate fluctuates significantly. If losses or surpluses occur this can cause added stress for an organisation if you take into account the non-profit constraint and it can penalise organisations through lower than expected grants.

Fixing exchange rates at the start of a project does not fit conceptually with pre-funding.

In multi-currency projects fixing expenditure by currency creates unnecessary inflexibility, or an excessive cost of flexibility.

InforEuro gives an average exchange rate for the month which does not include intermediaries' spreads or account for high fluctuation in the month. Hence, in terms of exchanging currencies it can only be a guide, not a real basis for accounting the costs.

Testimony

“Our Association is located in Hungary, which is a country outside the euro-zone. When receiving and accounting operating grants, we have to solve the problems arising from the fluctuations in the exchange rate. In the current economic circumstances the exchange rates are always changing; one day there are only 260 HUF to the Euro, and a few weeks later it may go up to 320 HUF. The time elapsing between handing in, decision-making and actually receiving the grant is very long (up to 1.5 years) and no sound forecasting of the values is possible.

When handing in the application, we make our estimate in HUF how much money to apply for, and we convert this amount into euros with the exchange

¹⁴ <http://ec.europa.eu/budget/inforeuro/index.cfm?Language=en>

rate valid at that time. By the time the decision is reached, this figure may have changed considerably. During the actual utilization of the grant the exchange rate does not remain steady either.

Finally, when writing the final report and creating the balance sheet there is yet another exchange rate which applies.

Therefore, the risks involved are extremely high, leaving us and other non-Euro zone applicants vulnerable to the unpredictable changes which may ultimately hinder the realization of our work programme and everyday activities.”

Gabor Farkas, Future of Europe Association

Solution

The Commission should carry the risk of the exchange rate changing. If money is spent as budgeted for in the local currency but translates into a higher Euro amount the Commission should pay this.

It should be accepted that changing exchange rates are a way of life and that the best rate that be can achieved at a point in time (proven by 3 quotes) is the correct rate to use.

Under or overspending in any one currency is a risky activity which is an unavoidable inconvenience and should be accepted by the EC.

When currencies are exchanged (e.g over €5,000), 3 quotes should be obtained, with at least one from another intermediary rather than a clearing bank (they have high spreads).

_Appendix 1

Members of the Working Group

Position	Name	Organisation	Country	Type	Email
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