

Special Report

## The European Institute of Innovation and Technology must modify its delivery mechanisms and elements of its design to achieve the expected impact



EUROPEAN  
COURT  
OF AUDITORS

EUROPEAN COURT OF AUDITORS  
12, rue Alcide De Gasperi  
1615 Luxembourg  
LUXEMBOURG

Tel. +352 4398-1

Email: [eca-info@eca.europa.eu](mailto:eca-info@eca.europa.eu)  
Internet: <http://eca.europa.eu>

Twitter: @EUAuditorsECA  
YouTube: EUAuditorsECA

More information on the European Union is available on the internet (<http://europa.eu>).

Luxembourg: Publications Office of the European Union, 2016

Print	ISBN 978-92-872-4224-2	ISSN 1831-0834	doi:10.2865/1032	QJ-AB-16-003-EN-C
PDF	ISBN 978-92-872-4269-3	ISSN 1977-5679	doi:10.2865/606788	QJ-AB-16-003-EN-N
EPUB	ISBN 978-92-872-4267-9	ISSN 1977-5679	doi:10.2865/77336	QJ-AB-16-003-EN-E

© European Union, 2016

Reproduction is authorised provided the source is acknowledged.

For any use or reproduction of the image in box 1 on p. 10, permission must be sought directly from the copyright holder.

**Special Report****The European Institute of Innovation and Technology must modify its delivery mechanisms and elements of its design to achieve the expected impact**

(pursuant to Article 287(4), second subparagraph, TFEU)

The ECA's special reports set out the results of its performance and compliance audits of specific budgetary areas or management topics. The ECA selects and designs these audit tasks to be of maximum impact by considering the risks to performance or compliance, the level of income or spending involved, forthcoming developments and political and public interest.

This performance audit was produced by Audit Chamber IV — headed by ECA Member Milan Martin Cvikl — which specialises in auditing revenue, research and internal policies, financial and economic governance and the European Union's institutions and bodies. The audit was led by ECA Member Alex Brenninkmeijer, supported by the Head of his private office, Antonius Moonen, Raphael Debets, Attaché, and Michael Schuppan, Trainee; Paul Stafford, Principal Manager; Maria Echanove, Head of Task; Alexandre Hugé, Eddy Struyvelt and Juan Vazquez Rivera, auditors.



*From left to right: R. Debets, A. Hugé, M. Schuppan, A. Brenninkmeijer, P. Stafford, M. Echanove, A. Moonen.*

## Paragraph

### **Glossary and abbreviations**

I-IX **Executive summary**

1-13 **Introduction**

1-2 **Europe is lagging behind in innovation**

3-6 **Shift in EU policy focus towards innovation**

7-13 **The European Institute of Innovation and Technology**

7-8 **The EIT's mission and objective**

9-13 **How does it work?**

14-18 **Audit scope and approach**

19-103 **Observations**

19-23 **The EIT is based on a valid rationale**

24-68 **Some key elements have not been appropriately designed**

25-26 **The knowledge triangle is not adequately reflected at Commission level**

27-33 **EIT funding based on complementary activities a poorly defined concept**

34-37 **The claimed leverage effect is undemonstrated and implausible**

38-39 **KICs are unlikely to reach financial sustainability**

40 **The EIT Foundation (EITF) failed to attract additional funds**

41-50 **The annual grant agreement process does not adequately encourage KIC innovation activities**

- 51-54 **The existing key performance indicators are not suited for effective monitoring**
- 55-57 **Business participation could be improved**
- 58-62 **The EIT model does not sufficiently set targets to support existing SMEs**
- 63-64 **There are not enough concrete synergies and complementarities**
- 65-68 **Some EIT elements are well appreciated: focus on the market, long-term perspective, autonomy of the KICs and the co-location centres**
- 69-95 **The implementation of the EIT model needs to improve**
- 69 **The EIT is not yet fully autonomous**
- 70-72 **The EIT has not fulfilled its role as an impact investor**
- 73 **The competitive funding mechanism undervalues performance**
- 74-79 **There are significant administrative and audit burdens on KIC partners**
- 80-84 **The EIT is under-resourced and has in the past been poorly managed**
- 85-86 **The EIT financial support is concentrated**
- 87-88 **The KICs lack transparency**
- 89-95 **The KICs have stimulated an innovation network and entrepreneurial culture but with little evidence of tangible results or impact to date**
- 96-103 **The future**
- 97-98 **Financial sustainability principles have been introduced**
- 99-100 **The definition of KIC complementary activities has been revised**
- 101 **More meaningful key performance indicators will be developed**
- 102 **The EIT is trying to involve more countries**
- 103 **New framework partnership agreements are currently being discussed**

104-111 **Conclusions and recommendations**

105 **Rationale**

106-107 **Design**

108-109 **Implementation and impact**

**Annex I — Regional co-location centres across Europe**

**Annex II — Objectives of the EIT**

**Reply of the Commission**

**Basic research:** Basic research is experimental or theoretical work undertaken primarily to acquire new knowledge of the underlying foundation of phenomena and observable facts, without any particular application or use in view.

**Business incubator:** A business incubator is an organisation designed to support the successful establishment and further development of enterprises. It often offers access to physical business infrastructure, individually tailored business support services and networking opportunities.

**Co-location centre:** Set up and managed by the KIC, a co-location centre is a geographical hub for the practical integration of the knowledge triangle. Co-location centres provide office space where innovators can physically meet and work together.

**DG Education and Culture:** The Directorate-General for Education and Culture of the European Commission is the executive branch of the European Union responsible for policy on education, culture, youth, languages and sport. DG Education and Culture is the supervisory body of the EIT.

**DG Internal Market, Industry, Entrepreneurship and SMEs:** The Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs of the European Commission has the mission to promote a growth-friendly framework for EU enterprises. DG Internal Market, Industry, Entrepreneurship and SMEs is responsible for a number of actions to improve the business environment, notably for SMEs, and to support the development of a strong and sustainable industrial base able to compete globally.

**DG Research and Innovation:** The Directorate-General for Research and Innovation of the European Commission is responsible for the European Union's research and innovation policy and the coordination of related activities. It funds innovative activities through the framework programmes, the current one being Horizon 2020.

**ECA:** The European Court of Auditors.

**EIT:** The European Institute of Innovation and Technology.

**Europe 2020:** Europe 2020 is the EU's growth strategy for the coming years and aims to make the EU a smart, sustainable and inclusive economy.

**FP7:** The seventh framework programme for research, technological development and demonstration activities was the European Union's main instrument for supporting research and innovation over the 2007-2013 period. The EIT was not part of FP7.

**H2020:** Horizon 2020 is the successor to FP7. With an original budget of 77 billion euro over the 2014-2020 period, its main objective is to ensure the EU produces world-class science, removes barriers to innovation and makes it easier for the public and private sectors to work together in delivering innovation. The EIT is part of H2020.

**Impact:** Long-term socioeconomic consequences that can be observed after a certain period following the completion of an intervention, which may affect either direct addressees of the intervention or indirect addressees falling outside the boundary of the intervention.

## Glossary and abbreviations

**KIC:** A knowledge and innovation community is a highly autonomous partnership of leading higher education institutions, research organisations, companies and other stakeholders in the innovation process that tackles societal challenges through the development of products, services and processes and by nurturing innovative, entrepreneurial people.

**Knowledge triangle:** The contribution of higher education to jobs and growth can be enhanced through close, effective links between education, research, and innovation — the three sides of the knowledge triangle.

**KPIs:** Key performance indicators are used to measure the factors which are crucial for the success of an organisation.

**Result:** Immediate changes that arise for direct addressees at the end of the participation in an intervention.

I Weak links between the worlds of education, science and business is often cited as one of the main reasons why the EU is falling short in innovation performance compared to its competitors. Created in 2008, the European Institute of Innovation and Technology (EIT) has the ambitious objective of overcoming this barrier. The EIT's mission is to reinforce the EU's innovation capacity 'by promoting synergies and cooperation among ... higher education, research and innovation of the highest standards, including by fostering entrepreneurship'.

II With an original budget of 3 billion euro over the 2008-2020 period, the EIT has a prominent role to play in the Europe 2020 strategy for smart, sustainable and inclusive growth. Covering the entire innovation cycle at EU level, from laboratory to market, the EIT aims to bring the best creative and innovative partners from academia, research and business to work together on major societal challenges such as climate change, energy efficiency, digital innovation, health and raw materials.

III The EIT is not a research centre and does not directly contribute to financing individual projects. Instead, it provides grants to the knowledge and innovation communities (KICs). Selected on a competitive basis, the KICs are autonomous partnerships of existing businesses, research institutes and universities. They mainly carry out: (1) training and education activities; (2) collaborative innovation-driven research; and (3) innovative business creation and development.

IV We examined whether the EIT is an effective tool to foster innovation in the EU. We considered whether the EIT's rationale and design address the needs of the innovation communities and assessed the implementation and monitoring of the EIT's activities. We conclude that, despite a valid *raison d'être*, the EIT's complex operational framework and management problems have impeded its overall effectiveness.

V The main reasons for setting up the EIT are well founded and generally supported by its stakeholders: weak links between business, research institutes and higher education, little success in bringing research outcomes to market and a lack of entrepreneurial culture were arguments to justify its creation to address these specific issues. Thanks to the EIT, the three KICs launched in 2010 have brought more than 500 partners together across disciplines, countries and sectors. KICs are autonomous, an EIT feature particularly valued by the KIC partners. Through the EIT, the KICs have offered new opportunities to carry out innovative activities and have promoted an entrepreneurial culture.

### VI

However, the audit has identified several weaknesses in key concepts and operational processes, as detailed below.

- (a) The funding model of the EIT includes the concept of KIC complementary activities, which are not funded by the EIT. There is little or no added value to this funding condition, which unnecessarily complicates the monitoring and reporting of the EIT's financial contribution.
- (b) The practical arrangements between the EIT and the KICs, such as the procedures for EIT grants to the KICs, are ill suited given the nature of the innovation activities the EIT aims to support.
- (c) The financial sustainability of the KICs is doubtful. Businesses are not involved enough in the KIC activities even though their participation was a prerequisite for the EIT to be successful. EIT funding is concentrated within a few countries and a limited number of KIC partners.
- (d) The performance indicators and the monitoring and reporting processes do not provide an informative picture of results and impacts.

### VII

Seven years after its inception, the EIT is not yet fully operationally independent from the European Commission. This has hampered its decision-making. The EIT is not the impact-driven institute envisaged. The performance of the KICs is not sufficiently taken into account when the final payment of the grant is processed. The EIT rarely rejected costs based on the lack of performance prior to 2015.

### VIII

The impact of the remedial actions undertaken by the Commission and the EIT in 2015 remains to be seen. The following conclusions and recommendations are pertinent and need to be followed up.

### IX

If the EIT wants to become the groundbreaking innovative institute it was originally conceived to be, significant legislative and operational adjustments are required to better foster the EU's innovation potential. We recommend the following.

- (1) The Commission should propose an amended EIT legal basis to the European Parliament and the Council, revising the EIT's funding model.
- (2) The EIT grant agreement (a) should cover a longer period than the calendar year and (b) should be signed before the start of the activities.
- (3) The EIT should refocus its approach to delivering impact. To that end, it should seek greater autonomy and make use of the flexibility in the legal basis of Horizon 2020. In particular, it should adopt specific rules tailored to the needs of the KIC partners. The EIT should resolve its staffing issues to enable it to continuously monitor KICs' performance.
- (4) The EIT should develop impact-based analysis. The EIT should also streamline its monitoring and reporting processes.

## Europe is lagging behind in innovation

### 01

Commission research has shown that the EU lacks an innovation culture where good ideas can be easily transformed into new products and services. It has failed to convert its excellence in basic research to market-driven innovation.

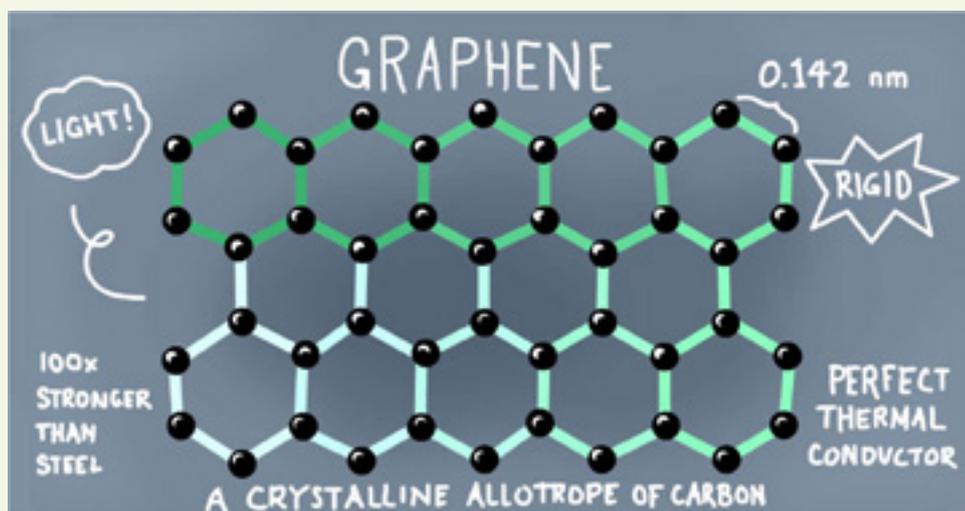
**Box 1** gives an example of this failure, which has been termed the 'European paradox'<sup>1</sup>.

1 Theory developed in the Green Paper on innovation, European Commission, 1995.

### Box 1

#### The European paradox — the example of graphene

Graphene is a structure material based on carbon which was discovered in 2004 by Andre Geim, a physics professor at the University of Manchester. Because of its many extraordinary properties (it is lighter than steel but nevertheless stronger and holds high heat and electricity conduction capacity), graphene has enormous potential for wide-ranging applications from high-performance electronic devices to energy storage.



Source: <http://www.sketchport.com>, ©Magicalhobo, 2014. Licensed under CC-BY.

Since its discovery, more than 11 000 graphene-related patents and patent applications have been filed worldwide. But the United Kingdom has accounted for less than 1 % of these, with Asian organisations taking out nearly two thirds according to Cambridge IP, a UK-based technology strategy company.

Source: Sarah Gordon 'Red tape and cost lie behind Europe's poor patent performance', *Financial Times*, December 2014.

## 02

To tackle this problem, the EU is striving to become a knowledge-based economy centred on an ambitious research and innovation agenda. The European Union strategy is 'to create an innovation-friendly environment that makes it easier for great ideas to be turned into products and services that will bring ... economy growth and jobs'<sup>2</sup>. **Box 2** defines innovation, which is indeed a key driver of economic growth and job creation.

2 Innovation union, a Europe 2020 Initiative ([http://ec.europa.eu/research/innovation-union/index\\_en.cfm](http://ec.europa.eu/research/innovation-union/index_en.cfm)).

### Box 2

#### The definition of innovation

An **innovation** is the implementation of a new or significantly improved product (good or service) or process, a new marketing method or a new organisational method in business practices, workplace organisation or external relations. The minimum requirement for an innovation is that the product, process, marketing method or organisational method must be new to the firm, or significantly improved.

**Innovation activities** are all scientific, technological, organisational, financial and commercial steps which actually, or are intended to, lead to the implementation of innovations. Innovation activities also include R & D that is not directly related to the development of a specific innovation.

Source: OECD/European Communities, *Oslo manual — Guidelines for collecting and interpreting innovation data*, 2005.

## Shift in EU policy focus towards innovation

## 03

Europe's inability to turn inventions into saleable goods and services has led the EU to rethink its research policies. EU public policies traditionally concentrated on basic research<sup>3</sup>, which is driven more by curiosity than by any potential market application. The underlying assumption was that basic research would spur applied research, which would in turn lead to innovation and commercialisation. However, these policies often neglected the absorption capacity of the market and the need for innovation support required by the private sector.

3 The major beneficiaries under the previous European R & D framework programmes were researchers outside the business sector (*Interim evaluation of the seventh framework programme – report of the expert group*, 12 November 2012).

## 04

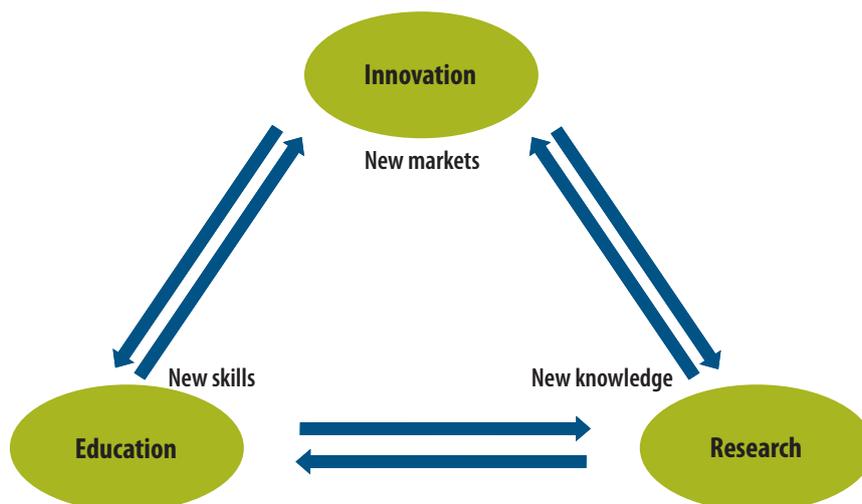
The European Commission has put greater emphasis on the end of the innovation cycle with the aim of bringing research results to the market. Unlike its predecessors, Horizon 2020 (the current framework programme for research and innovation) explicitly funds innovation. New EU public instruments such as public–private partnerships (e.g. JTIs<sup>4</sup>), loan and guarantee schemes (e.g. the RSFF<sup>5</sup>) and venture capital (e.g. the GIF<sup>6</sup>) have been introduced to strengthen EU innovation and to further encourage business participation in innovation activities<sup>7</sup>.

## 05

However, these innovative EU initiatives took little account of the links between the main stakeholders involved in the ‘knowledge triangle’— the interaction between research, education and innovation (see **Figure 1**). Economic growth is founded on a broader, well-functioning ‘knowledge and innovation system’ in which productive interactions between all innovative actors is crucial. A better understanding of these relationships within the knowledge triangle has encouraged the development of a new public scheme designed to support the whole innovation ecosystem.

- 4 Joint technology initiatives were introduced to better address the needs of industry in dedicated fields of research. They are independent EU bodies with the participation of industry and, in some instances, of Member States.
- 5 The Risk Sharing Finance Facility was launched to improve access to debt financing for research performers, especially for higher risk investment in research, technological development and innovation.
- 6 The High Growth and Innovative SMEs Facility under the competitiveness and innovation programme provides risk capital for innovative SMEs and SMEs with high growth potential.
- 7 The low commitment of business to expenditure on R & D is often cited as one reason why the EU is underperforming. According to Eurostat, the R & D conducted within the business enterprise sector was equivalent to 1.30% of the EU-28’s GDP in 2012, compared with 2.49% in Japan (2010 data) and 1.83% in the United States (2011 data).

Figure 1 The knowledge triangle



Source: ECA.

## Introduction

### 06

The Commission presented 'a broad-based innovation strategy for the EU, aimed at translating investments in knowledge into products and services' and proposed the creation of a specific body to 'act as a pole of attraction for the best minds, ideas and companies from around the world'<sup>8</sup>. The EIT came into being in 2008.

#### Initial logo of the EIT



## The European Institute of Innovation and Technology

### The EIT's mission and objective

### 07

The EIT aims to bridge the gap between the research-focused universities and market-oriented companies. The EIT's concept of an integrated approach to the knowledge triangle is a unique way for an EU public scheme to promote innovation and entrepreneurship. Moreover, the EIT has the explicit objective of clearly focusing on tangible results and concrete benefits to society by 'converting outputs from research into high-value products and services'<sup>9</sup>.

### 08

With a budget of over 300 million euro for the 2008-2013 period and 2.7 billion euro originally planned for 2014-2020, the EIT has a prominent role to play in the Europe 2020 strategy 'to contribute to sustainable European economic growth and competitiveness by reinforcing the innovation capacity of the Member States and the Union in order to address major challenges faced by European society. It shall do this by promoting synergies and cooperation among, and integrating, higher education, research and innovation of the highest standards, including by fostering entrepreneurship'<sup>10</sup>. The EIT has now been incorporated into the current framework programme for research and innovation, Horizon 2020<sup>11</sup>.

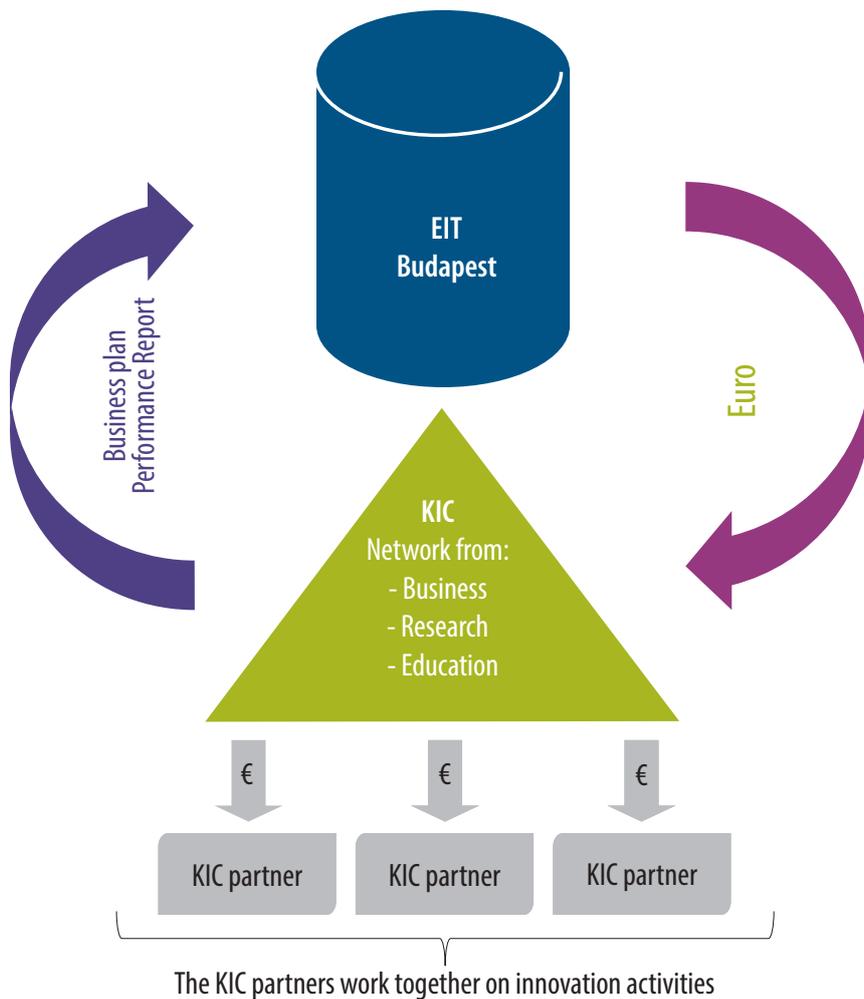
- 8 COM(2005) 24 final of 2 February 2005 'Working together for growth and jobs: a new start for the Lisbon strategy'.
- 9 Decision No 1312/2013 of the European Parliament and Council of 11 December 2013 on the strategic innovation agenda of the EIT the contribution of the EIT to a more innovative Europe (OJ L 347, 20.12.2013, p. 892).
- 10 Article 3 of Regulation (EU) No 1292/2013 of the European Parliament and of the Council of 11 December 2013 amending Regulation (EC) No 294/2008 establishing the European Institute of Innovation and Technology (OJ L 347, 20.12.2013, p. 174).
- 11 Horizon 2020 was established by Regulation No 1291/2013 of the European Parliament and the Council of 11 December 2013 (OJ L 347, 20.12.2013, p. 104). It is FP7's successor programme and will run from 2014 to 2020 with a budget of 77 billion euro.

How does it work?

09

Under the supervision of the European Commission’s DG Education and Culture, the EIT operates as a decentralised EU body. Its headquarters are located in Budapest. The EIT is not a research centre and does not directly contribute to financing individual projects. Instead it provides grants to the KICs, structured partnerships of existing businesses, research institutes and universities (the KIC partners). The KICs are at the core of the EIT’s activities and are the principal means by which the EIT is expected to deliver its objectives (see **Figure 2** for an overview of the model of the EIT).

Figure 2 Overview of the EIT model



Source: ECA.

10

The KICs should ensure that the EIT’s vision and policies are translated into effective actions. The KICs are selected by means of a competitive call based on priority topics with high societal impact. Five KICs have been selected by the EIT for financial support — see **Figure 3**. Each KIC is represented by an autonomous organisation, the KIC legal entity, to conclude the contractual agreements with the EIT.

Figure 3

The five KICs selected and funded by the EIT

KIC	Mission	Numbers of KIC partners	
EIT Digital	To drive European leadership in ICT innovation for economic growth and quality of life	115	Launched in 2010
Climate-KIC	To create opportunities for innovators to address climate change and shape the world’s economy	209	
KIC InnoEnergy	To become the leading engine for innovation and entrepreneurship in sustainable energy	242	
EIT Health	To accelerate entrepreneurship and innovation in healthy living and active ageing, providing Europe’s top talents with new opportunities and resources for the benefit of all citizens	209	Launched in 2015
EIT Raw Materials	To boost the competitiveness, growth and attractiveness of the European raw materials sector via radical innovation and entrepreneurship	115	

Source: ECA/EIT.

### 11

The EIT grant agreement specifies the maximum annual financial contribution and defines the portfolio of activities to be undertaken by the KIC for the calendar year the grant is signed. The planned portfolio of all KIC activities must be included in a KIC business plan, annexed to the grant agreement. These KIC activities can be subdivided into four main action lines:

- (i) education,
- (ii) innovation projects,
- (iii) entrepreneurship, and
- (iv) management and other KIC operating costs.

### 12

Under the education action line, the EIT funds education and training activities at master's and doctoral level, focusing on the delivery of entrepreneurship and innovation skills. Under the second action line, innovation-driven projects are carried out by a consortium of KIC partners selected through an internal competitive call organised and managed by the KIC legal entity. The aim is to bridge the innovation gap between research and the market by funding projects connected to business development activities<sup>12</sup>. The entrepreneurship action line aims to foster business creation through incubators and to accelerate business development via financial and technical support for the growth of start-ups. One of its principal objectives is to reduce the 'time-to-market' for new businesses through demonstration actions, facilitating experience labs and market studies.

### 13

The fourth action line covers costs related to the management of the KIC and its co-location centres. Each KIC has regional co-location centres across the EU (see **Annex I**). They are physical meeting and collaboration spaces, conceived to deliver innovation locally.

12 The focus on business applications is the main difference with traditional collaborative research projects such as those proposed through FP7 competitive calls.

## 14

The aim of the Court's audit was to assess whether the EIT is an effective tool to foster innovation in the EU. In particular, the rationale, design and implementation of the EIT were examined to assess whether this new instrument is on the right path to achieve its general objective of boosting EU innovation by integrating the knowledge triangle.

## 15

The audit was carried out between December 2014 and June 2015 and covered KIC and EIT activities from 2010 to 2014. The EIT undertook several initiatives in 2015 which are described in paragraphs 96 to 103. We met representatives of the following:

- DG Education and Culture of the European Commission,
- the EIT's headquarters,
- the three KIC legal entities,
- seven KIC partners, and
- five co-location centres<sup>13</sup>.

## 16

The KIC partners were selected based on the amount of EIT funding they have received. A second criterion was used to ensure that the sampled KIC partners covered all KICs launched in 2010 and all types of organisation representing the three sides of the knowledge triangle (i.e. universities, research institutes and businesses). On a sample basis, KIC activities funded by the EIT were also reviewed.

## 17

The audit approach was complemented by:

- a web-based survey to collect the views of the KIC partners<sup>14</sup>;
- a quantitative analysis of the costs reported of the KICs covering the 2010-2014 period;
- a review of the academic literature on innovation and EIT; and
- an analysis of the initiatives taken by the EIT and the Commission during and since our audit.

## 18

Prior to the audit, a panel of key stakeholders was organised to better understand the main challenges the EIT has to face. Data and conclusions from the Court's annual audit of the EIT's financial accounts have also been used as a source of information.

13 Located in Grenoble (KIC InnoEnergy), London (Climate-KIC and EIT Digital) and Stockholm (EIT Digital and KIC InnoEnergy).

14 The KICs only provided valid email addresses for 298 KIC partners (out of 546), of which 113 answered the survey fully, representing a response rate of 38%.

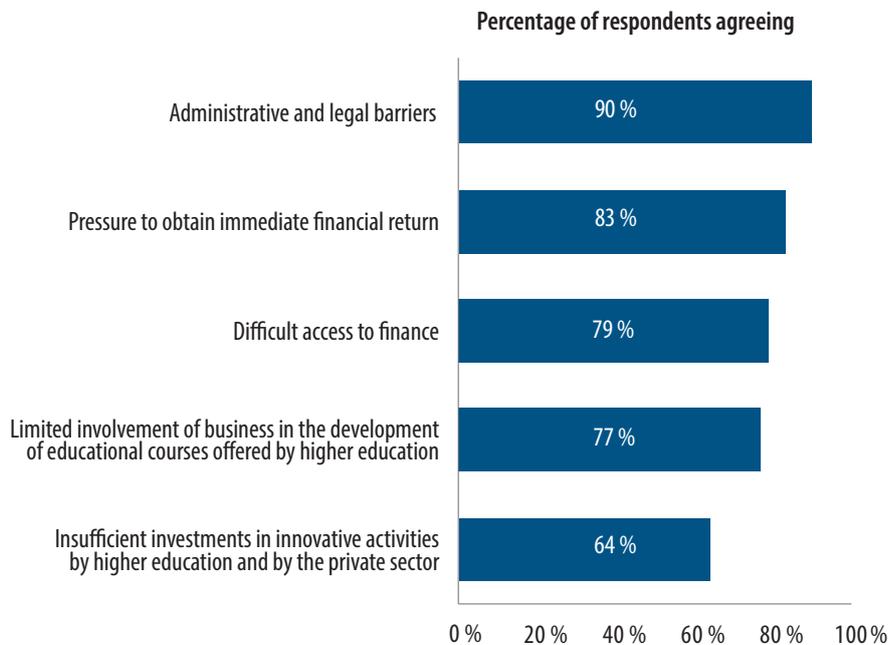
## The EIT is based on a valid rationale

### 19

The stakeholders and the majority of the KIC partners who responded to the survey are of the opinion that the main barriers to innovation are, by order of importance for the respondents to the survey (see **Figure 4**):

Figure 4

### Main barriers to innovation according to respondents



Source: ECA.

### 20

Other barriers to innovation in the EU were reported to be: too many different public funding mechanisms with their own rules which weaken the overall efficiency of public support schemes; too much fragmentation of the research effort across the EU leading to costly duplication; a lack of common strategies and/or synergies in the EU programmes with other EU, national and local programmes which support innovation; the existence of different legal systems at the national level, restricting cross-border innovation; lack of an effective EU internal market, which increases the difficulty of commercialising new products/services in other EU countries.

21

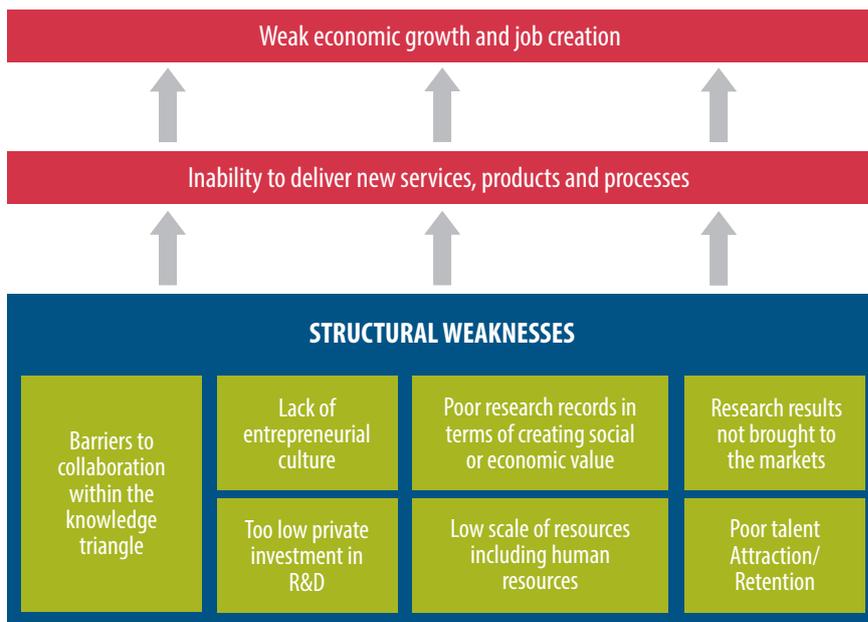
Almost 80% of the survey respondents agreed that public schemes supporting innovation are not sufficiently geared towards market applications. This view was also confirmed during the interviews. According to 66% of the respondents to the survey, the objectives of the EIT are relevant to addressing the main barriers impeding innovation in the EU — see **Annex II** for the EIT’s objectives. All those consulted confirmed the reasons and the need to set up a new EU instrument (the EIT) which differed from the existing ones.

22

The market failures the EIT aims to address (see **Figure 5**) are the structural weaknesses that hamper innovation and consequently constitute an obstacle to economic growth and job creation. There is insufficient development of an entrepreneurial culture. The lack of commercialisation of the results and the low level of cooperation between the research-focused universities and market-oriented companies are often cited as main reasons for the EU falling short in innovation performance. Higher education has not focused sufficiently on fostering innovators and entrepreneurs. There is a need for higher education to embed innovation and entrepreneurial skills into educational programmes.

Figure 5

The market failures the EIT aims to address



Source: ECA.

## Observations

### 23

Thus the EIT aims to give priority to the transfer of its higher education, research and innovation activities to the business context and their commercial application. However, whilst the EIT concept is based on a valid rationale, it has yet to have the desired effect.

### Some key elements have not been appropriately designed

### 24

The EIT was originally conceived to be an innovative public scheme. The EIT model introduced specific features which are not found in any other EU instrument fostering innovation. For example, its ability to support the entire innovation ecosystem from education to start-up through innovation-driven projects run by multiple KIC partners is unique. The autonomy given to the KICs is another characteristic of the EIT's model particularly appreciated by its partners. However, some key elements of the EIT model have not been appropriately designed to ensure that it is an effective and groundbreaking public scheme.

### The knowledge triangle is not adequately reflected at Commission level

### 25

The initial drive to establish the EIT was based on the assumption that the weakest link in the integration of the knowledge triangle was between the higher education sector and the business community. The EIT was therefore placed under the responsibility of DG Education and Culture, which has a large amount of experience with educational programmes. DG Education and Culture has thus taken the lead role within the Commission, for example as its observer on the EIT Governing Board.

### 26

The innovation and entrepreneurship action lines which now take up the majority of EIT funding need to have expertise directly available<sup>15</sup>. To do this, the EIT should have regular access to the expertise of DG Research and Innovation and DG Internal Market, Industry, Entrepreneurship and SMEs. DG Research and Innovation has valuable experience in managing research and innovation projects and DG Internal Market, Industry, Entrepreneurship and SMEs has expertise in new business creation. However, these DGs have no units responsible for EIT matters, and the Court found little evidence of their active involvement.

15 Over the 2010-2014 period, the innovation projects action line accounted for 42% of EIT-funded activities costs, 22% of entrepreneurship costs, 14% of education costs and 22% of other costs (see paragraphs 11 to 13). It should be noted that there is a significant misalignment in methodologies among KICs when measuring other costs which are mainly made up of administrative and overhead costs.

**EIT funding based on complementary activities a poorly defined concept**

**27**

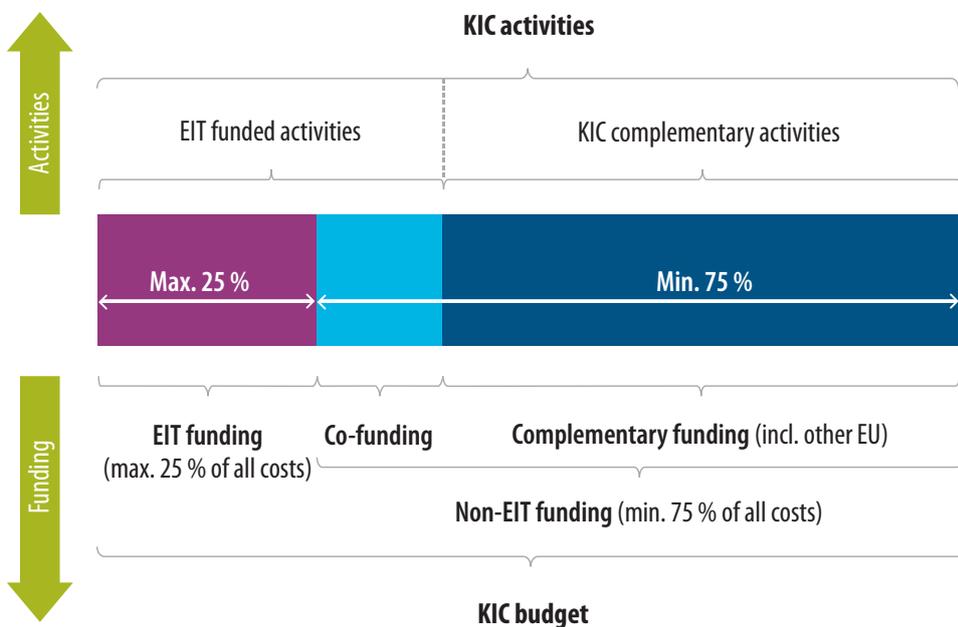
The innovation activities carried out by the KIC partners have been split into two categories:

- (a) activities funded up to 100 % by the EIT; and
- (b) KIC complementary activities which are not funded by the EIT.

The distinction between these two types of activities is fundamental to the EIT’s funding model as it determines the ceiling of the EIT’s contribution. EIT funding may only cover a maximum of 25 % of a KIC’s overall costs (i.e. the sum of the costs of activities funded by the EIT and of those not funded by the EIT — this complex model is set out in **Figure 6**).

**Figure 6**

**EIT funding model**



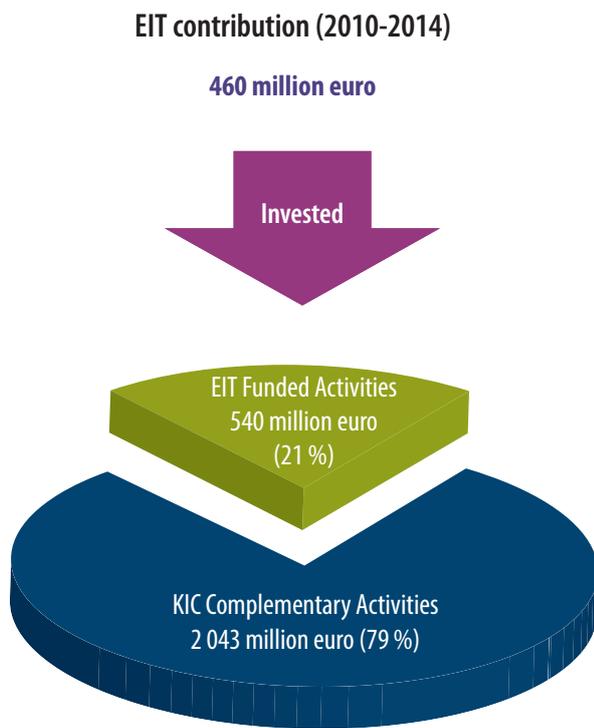
Source: ECA.

28

Over the 2010-2014 period the EIT contributed 460 million euro to the three KICs. This has helped to fund innovation activities of 540 million euro. KIC complementary activities have been declared for 2 043 million euro (of which 10 % were funded by EU programmes other than EIT such as FP7 collaborative projects, ERC funding schemes, JTI projects etc., and 23 % by other national or regional public schemes) — see **Figure 7**.

Figure 7

**EIT contribution to the KICs activities over the 2010-2014 period**



Source: EIT.

### 29

The KIC complementary activities were poorly defined. This lack of clear definition led to operational difficulties for the KIC partners who had a different understanding from the EIT of what could be reported as KIC complementary activities and how to report them. This issue was raised by one KIC in 2012 in its performance report: ‘pending definition of complementary funding is causing problems in full engagement of some partners, and full declaration of the complementary sourcing they are really bringing’.

### 30

The KIC complementary activities were not legally defined until the 2014 grant agreements were signed between the KICs and the EIT, at the start of the fourth year of KIC operations. However, even this definition was of little help as the complementary activities are merely described as ‘activities ... carried out by ... KIC partners ... primarily focused on activities [the KIC has to carry out to fulfil its mission]’. The 2014 EIT guidance document *Principles for financing, monitoring and evaluating KIC activities* specified that such activities must have ‘a clear link with a least one [activity funded by the EIT] and not be financed from the EIT contribution’. It also stated that the costs of these activities must be ‘proportionate to the cost of [the activity funded by the EIT] and/or to the expected impact in furthering the mission of a KIC’.

### 31

The proportionality principle was introduced in 2014 by the EIT to address and prevent the occurrence of inflated KIC complementary activities. Nevertheless, assessing whether the ‘proportionality’ criterion is respected for a specific KIC complementary activity remains challenging as no further guidance has been issued and the EIT did not put in place any specific mechanism to systemically test proportionality. As a result, no cost has been rejected by the EIT on the grounds of being ‘disproportionate’ during its review of the KIC complementary activities for the 2010-2014 period.

### 32

Prior to the 2016 business plan cycle, the criteria of ‘having a clear link’ and ‘being proportionate’ were subject to different interpretations. This has led to uncertainties between KIC partners, the EIT and those checking cost statements<sup>16</sup> as to whether the associated costs should be accepted or not in the calculation of the maximum EIT contribution (see **Box 3** for an example). This is prejudicial for the KIC partners as rejected costs lead to a decrease in the EIT’s financial contribution.

<sup>16</sup> Checks and audits are performed by the EIT, private external auditors and ECA.

## Box 3

**Example of a KIC complementary activity with a less than 'clear link' to an EIT-funded activity**

A KIC partner reported in 2013 one KIC complementary activity valued at 188 million euro. According to the financial reporting, this activity was linked to an EIT-funded innovation project of 4.5 million euro — the implied cost ratio is 42:1. The amount of this KIC complementary activity would be enough to support the whole 2013 EIT contribution to the KIC concerned. To justify the link, a short document was provided explaining that the partner is involved in many KIC activities including educational and business creation programmes.

However, there is no convincing evidence of a 'clear link' between the purpose of the 188 million euro in incurred costs and the innovation project valued at 4.5 million euro undertaken by other KIC partners.

**33**

The measuring and reporting of KIC complementary activities are not essential to the achievements of the EIT's objectives; only the activities funded by the EIT 'are the activities that make a KIC a KIC'<sup>17</sup>. The purpose of the grant is to finance EIT-funded activities, not 25 % of the KIC overall's costs. Excluding the KIC complementary activities as a funding condition would not affect the outcome; the KICs would still carry out the EIT-funded activities.

**The claimed leverage effect is undemonstrated and implausible****34**

The inclusion of the KIC complementary activities in the EIT's funding model is used to demonstrate its leverage effect. Horizon 2020 states that 'the EIT approach to funding will be firmly based on a strong leverage effect ...' The 2013 EIT annual report states 'Leverage factor of 4: more than 80 % of the KIC's overall budget comes from external sources and for every euro invested from the EU budget, a higher investment is triggered from other sources.' The Commission reported in 2013 as a performance indicator the 'enhanced leverage effect of the EIT on private and other public financial sources'.

17 'FAQ about KICs' — EIT (2010).

## 35

The claimed EIT leverage effect of four is based on the assumption that all KIC complementary activities declared by the KIC partners are additional, i.e. triggered by the EIT's intervention. This is an unrealistic hypothesis, because the EIT has permitted the KICs to declare the KIC complementary activities retroactively — costs from a past KIC complementary activity can be declared in the current reporting year of the associated activity funded by the EIT.

## 36

These retroactive KIC complementary activities are not additional as they were undertaken by the KIC partners without the EIT support (see **Box 4** for an example). The retroactive KIC complementary activities account for 450 million euro (22 %) of the overall KIC complementary activities declared over the 2010-2014 period.

### Box 4

#### A financial leverage effect cannot stem from a retroactive activity

The costs incurred of a previous EU collaborative project running from 2010 to 2013 can be declared by a KIC partner as a KIC complementary activity to an EIT-funded activity occurring in 2014. But the decision to undertake the FP7 project in 2010 was independent of the 2014 EIT's approval to fund the associated activity, thus there is no leverage effect in this specific case.

## 37

Furthermore, the KIC partners mainly contribute to the KICs' budgets 'in kind' and not in cash. The inherent risk is thus high that the KIC partners are doing what they would have been doing anyway (deadweight) and declaring the costs as a KIC complementary activity's contribution to the EIT. The KIC partners and the three KIC legal entities interviewed during the course of this audit confirmed that most of the KIC complementary activities are not additional — they would have been carried out without the existence of the EIT. Our review of each KIC complementary activity greater than 2 million euro showed this to be the case.

### Box 5

#### Example of non-additional KIC complementary activities

KIC partners have reported as a KIC complementary activity the cost of non-EIT students attending courses in which EIT students also participate. These costs are not additional as the courses are part of the standard educational programme of the university.

## KICs are unlikely to reach financial sustainability

### 38

KICs are to develop strategies to become financially sustainable<sup>18</sup>, although this objective in the long term is not compatible with the expected lifespan of a KIC (7 to 15 years) as described in the EIT's founding regulation<sup>19</sup>. Due to this legislative incoherence, it is commonly understood<sup>20</sup> that the EIT's financial contribution should end, in principle, after a maximum period of 15 years, but that the KICs should live on.

### 39

KIC partners and the three KIC legal entities interviewed stated that the KICs are unlikely to become financially independent after 15 years. Over the 2010-2014 period, only one KIC declared any income (400 000 euro), while the EIT injected over 460 million euro into the KICs. Two thirds of the respondents to the ECA's survey do not think that in the long term the KICs are likely to become financially independent.

## The EIT Foundation (EITF) failed to attract additional funds

### 40

The EIT's 2010 annual report announced the creation of the EITF, which 'will be used as a vehicle to attract and channel funding for EIT activities which fall outside the scope of its regular funding ... In this way, the foundation will play a crucial role in both safeguarding the EIT's financial sustainability and autonomy, as well as enhancing its social outreach.' The foundation never attracted any significant funds and was closed down in 2014.

## The annual grant agreement process does not adequately encourage KIC innovation activities

### 41

The KIC business plan, annexed to the grant agreement, is a comprehensive document setting out the selection, description and management of the KIC's portfolio of planned activities for the calendar year. The EIT issues guidelines to clarify the requirements of the business plan in terms of structure, content and level of detail.

18 Article 6(2) of the amended EIT founding regulation states: 'KICs shall have substantial overall autonomy to define their internal organisation and composition, as well as their precise agenda and working methods. In particular, KICs shall ... develop strategies for financial sustainability.'

19 Article 7b of the amended EIT founding regulation states: '... a KIC shall normally have a time-frame of seven to fifteen years.'

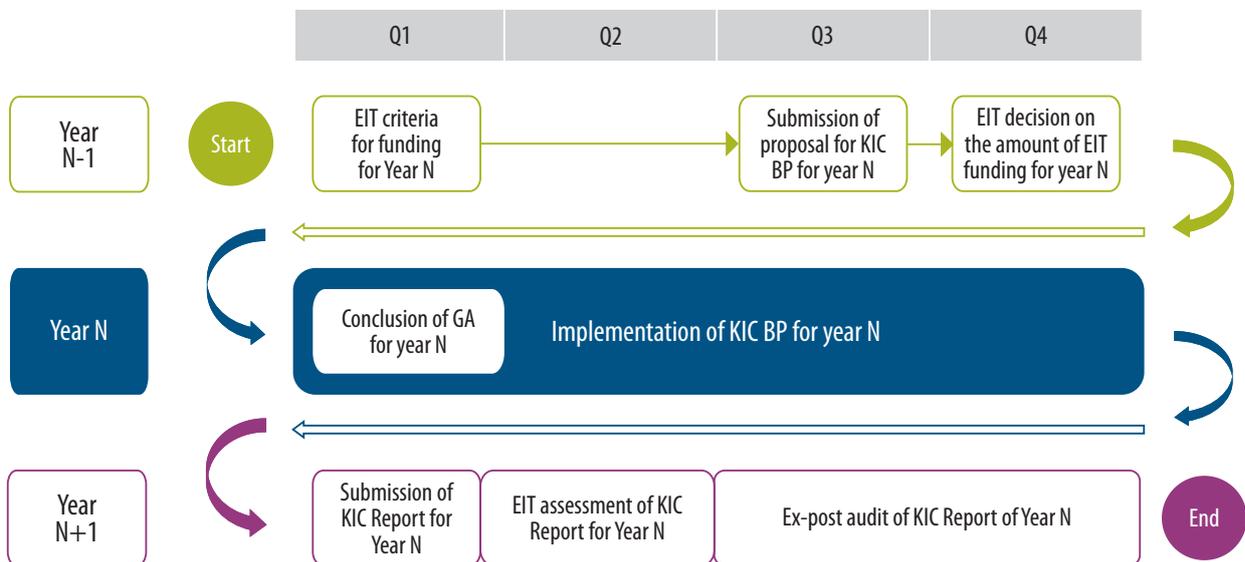
20 This was explicitly communicated by the EIT to the KICs in 2015.

42

The business plan of a KIC is more like an annual work programme with a strong emphasis on the short term. The draft business plan for the coming year must be submitted to the EIT at the latest at the end of September of the year N-1 — see **Figure 8** for the timeline of the grant agreement and related business plan. In order for the KIC to meet this deadline, KIC partners must identify and cost all innovation activities they wish to carry out in the following year by the end of the second quarter. The KIC partners therefore have to anticipate at least 6 months in advance the exact innovation activities they will carry out in the following calendar year. Under the innovation project action lines, an additional period of 3 months is needed to launch a competitive call for project proposals. Nevertheless, the KICs can amend the business plans during the year in order to include new innovation projects, which is formalised by way of an amendment to the annual grant agreement.

Figure 8

**Timeline of the grant agreement, related KIC business plan and assessment of KIC performance report**



Source: EIT, Principles for financing, monitoring and evaluating KIC activities.

## 43

The strategy of a KIC should be 'based on joint mid- to long-term innovation planning to achieve the EIT challenges ...'<sup>21</sup>. Nevertheless, the grant agreement signed between the EIT and the KIC legal entity only determines the EIT financial contribution for 1 calendar year. The EIT funding is thus only secured to cover costs declared on an annual basis. Future funding depends on the availability of the EIT budget, which is subject to the effect of the introduction of EFSI — see **Box 6** — and on the results of the competitive funding between KICs<sup>22</sup>.

## 44

Whilst the Court supports competitive funding, there is a problem of timing. As the competitive funding allocation is decided by the EIT Governing Board in its December meeting, the results of the competitive funding are not known before the end of the year. This creates uncertainty for the KIC partners, as some projects are put on hold until it is clear whether the funding will be available or not.

21 Regulation (EC) No 294/2008 of the European Parliament and of the Council of 11 March 2008 establishing the European Institute of Innovation and Technology (OJ L 97, 9.4.2008, p. 1).

22 Part of the annual grant is decided on a competitive basis between KICs. 40% of the total 2015 EIT contribution to the KICs has been allocated that way. This share should increase over the years.

## Box 6

### The European Fund for Strategic Investments<sup>23</sup> and its impact on the EIT budget

In November 2014, the European Commission launched an investment plan for Europe in order to relaunch growth and investment in the EU. It proposed to create the European Fund for Strategic Investments (EFSI), set up within the EIB and jointly funded by the EU and the EIB.

The EFSI regulation reduced the EU contribution to the EIT by 12%, from 2 711 to 2 383 million euro over the 7-year period from 2014 to 2020. The EIT budget for 2016 will be reduced from 336 million (as initially foreseen in Horizon 2020) to as low as 285 million euro (– 15%). This will lead to fewer EIT-funded innovation activities. In combination with the competitive funding, this creates additional uncertainty for the KICs, who have to select projects and draft their business plans without having any clear idea about the funding available for the following year(s).

KICs may indirectly benefit from the EFSI funds, which will compensate for some of the decrease in the EIT budget.

23 Opinion No 4/2015 concerning the proposal for a regulation of the European Parliament and of the Council on the European Fund for Strategic Investments and amending Regulations (EU) No 1291/2013 and (EU) No 1316/2013 (<http://eca.europa.eu>).

## Observations

### 45

This short-term vision in terms of operational and financial planning does not match the time horizon of the innovation activities the KICs are undertaking. All the KIC partners the ECA visited cited the principle of annuality as a major handicap to fostering innovation in the long run.

### 46

The education action line is mainly composed of master's and doctoral programmes. These education programmes have an expected time frame of, respectively, 2 and 4 years. It is therefore risky for the higher education KIC partners to sign a multiannual contract with EIT students because there is legal uncertainty over the funding they will receive in future years. This is particularly a problem for public organisations (mainly universities and research institutes), which have to apply strict financial rules under their respective national legislation.

### 47

The annual grant process is also a major obstacle to planning and coordinating multiannual innovation projects under the innovation action lines. Some KICs have set up specific activities dedicated to longer-term projects with, in principle, financing guaranteed over their lifetime (with an interim evaluation process to ascertain that the funded project is viable and likely to generate commercial impact — a negative interim evaluation would stop the financing of the venture). However, because the EIT financial contribution is only fixed for 1 year, the financial risks related to future years are borne by the KIC partners. Some KIC projects might have to be discontinued or abandoned due to a lack of funding.

### 48

In contrast, EU grants for collaborative research projects are signed for a multiannual period, for example, grants under the Marie Skłodowska-Curie programme offer secured funding to researchers for periods longer than 12 months.

### 49

On average, over the 2011-2014 period, the grant agreements were signed 3 months after the start of the calendar year. The signatures of the 2015 grant agreements were delayed until June 2015. The activities undertaken by the KICs after 1 January are not covered by a legal contract until the new annual grant agreement is signed. Late signature causes a hiatus in the innovation process as some KIC partners do not want to take the legal and financial risks of committing resources until the grant agreement is signed.

## 50

The late signature of the annual grant agreements also delays the payment by the EIT of the pre-financing to the KICs, which should take place within 30 days of the entry into force of the grant agreement. Only then can the KICs distribute the money to the individual partners. All expenses made before then must therefore be met by the partners themselves. All costs exceeding the amount of the pre-financing (up to 50%) received will only be reimbursed by the EIT through the final payment made in the second half of the following year.

### The existing key performance indicators are not suited for effective monitoring

## 51

According to the SIA<sup>24</sup>, the EIT should 'establish, in cooperation with the Commission and the KICs, a comprehensive system to monitor: the EIT's contribution to Horizon 2020; the EIT's impact via its own and KIC activities; and KIC results.' This system is not yet in place.

## 52

The EIT's core KPIs (see **Box 7**) are not clearly defined and have not been consistent over time (definition of graduates, the concept of technology transfer and knowledge adoption, the notion of ideas incubated, etc.). **Box 8** shows an example of the unclear definition of KPIs. This complicates performance reporting, especially when the definitions of the KPIs change in the middle of the calendar year, requiring retroactive adaptation.

24 Decision No 1312/2013.

### Box 7

#### KPIs

There are three types of KPI.

- (1) **EIT core KPIs.** There are six EIT core KPIs: attractiveness of educational programmes; number of new graduates; number of business ideas incubated; number of start-ups or spin-offs created; knowledge transfer/adoption; and new or improved products/services/processes launched into the market. Progress against these KPIs is measured for the purposes of the competitive funding.
- (2) **EIT-specific KPIs** measure EIT's own activities, monitoring its operational performance using indicators such as due dates for grant agreement completion, report acceptance and payment execution, percentage of processes formalised and level of satisfaction with EIT.
- (3) **KIC-specific KPIs** are developed by the KICs themselves.

Box 8

**Unclear KPI definition of start-ups created**

For a start-up to be recognised, the KIC needs to provide ‘proof (e.g. letter of intent or an order form/invoice) demonstrating that this start-up has won its first customer or the existence of a potential first customer or other document demonstrating that the start-up has commenced commercial operations.’ Because of the vagueness of the criteria (what is a ‘potential first customer’?), the KICs interpret this rule in different ways.

**53**

It is difficult to compare the three KICs through these core KPIs. Considerations such as the size of the start-up, the duration of the course, etc. are not taken into account in the core KPIs. Moreover, the KICs operate in different sectors, with different levels of maturity, making it more or less difficult to create start-ups, incubate business ideas, etc. Mere quantitative analysis does not take into account the different environments in which the three KICs operate. Progress in developing KIC-specific KPIs is limited.

**54**

Several shortcomings which were identified by an external evaluation in 2011 have not yet been remedied. The core indicators continue to focus on input or output rather than on results or impacts, and on absolute values rather than on the increase in activity as a consequence of the KICs<sup>25</sup> (see also paragraph 99).

**Business participation could be improved**

**55**

The business community should be strongly involved at the strategic and operational levels for the EIT to be a success. This would ensure that the KICs’ activities are driven by market needs and further steered in directions useful to the economy and society<sup>26</sup>. In 2006, the Commissioner for Education, Training and Culture emphasised the importance of the business community in the proposal: ‘Businesses will be core partners at the Institute’s strategic and operational levels. Companies will be directly involved in research and education activities, thereby helping to nurture an entrepreneurial mind-set among graduates and researchers’<sup>27</sup>. Businesses thus have a crucial role to play in bridging the gap between research and innovation.

- 25 Paragraph 6.31 Monitoring progress and outcomes, *External evaluation of the European Institute of Innovation and Technology- Framework Contract on evaluation and related services* (EAC 03/06), May 2011.
- 26 COM(2006) 77 final of 22 February 2006 ‘Implementing the renewed partnership for growth and jobs — Developing a knowledge flagship: the European Institute of Technology’.
- 27 ‘The Commission details its plan for a European Institute of Technology’, European Commission press release (IP/06/751), 8 June 2006.

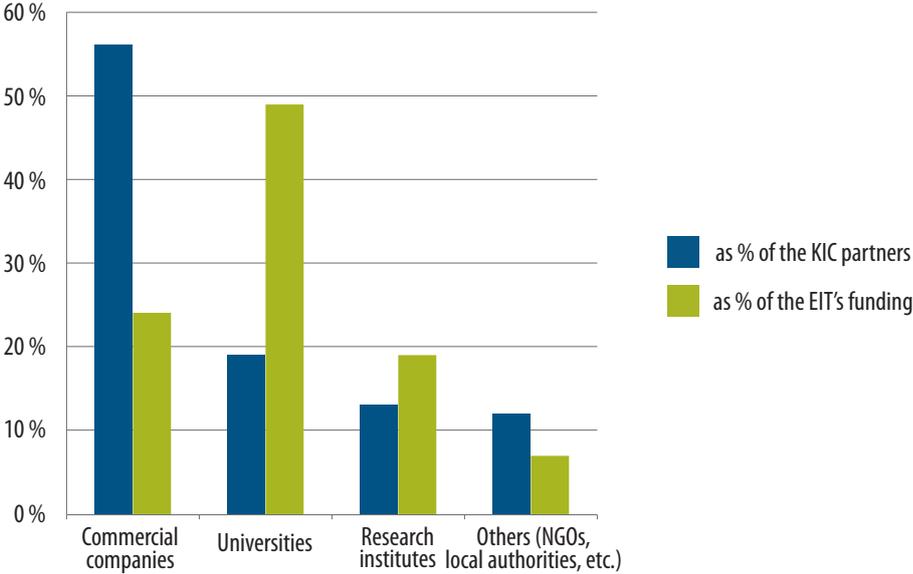
Observations

56

Despite the importance of business organisations, they have only received 24 % of the EIT’s financial support (see **Figure 9**), whilst making up 56 % of the KIC partners. Although the level of financial contribution is not the only indicator of participation<sup>28</sup>, the involvement of the business community in the EIT and KICs could be improved. Over the 2010-2014 period, only two of the top 40 beneficiaries by EIT funding are businesses.

28 Businesses also have non-financial grounds to join the KICs, such as a way to have access to talented students coming out of the EIT-labelled education programmes).

Figure 9 Split by organisation type over the 2010-2014 period



Source: EIT.

### 57

Business stakeholders have expressed their concern that the KICs' agendas are mainly driven by the needs of higher education, while universities interviewed in the course of this audit regret that the business community is not sufficiently involved in the development of educational courses. In the first 3 years, collaborative projects undertaken by KICs were abandoned or did not lead to tangible results because they did not sufficiently focus on a market application. One cause of this was the selection of topics for the projects to be funded by the EIT, which was mainly guided by the needs of higher education rather than the business community. KICs have since remedied this by ensuring that a project to be funded by the EIT should lead to a potential market application and thereby generate future revenues.

### **The EIT model does not sufficiently set targets to support existing SMEs**

### 58

SMEs are typically more agile and better than large-scale organisations at developing and applying new technologies. Many EU policies recognise the important role of SMEs. Although Horizon 2020 has a specific objective of allocating at least 20% of its budget to SMEs, the EIT has not set any target in this context.

### 59

Whereas the respondents to the survey ranked 'promoting and supporting SMEs' participation in innovation activities' as the third most important objective the EIT should achieve in order to foster innovation in the EU, the EIT did not implement specific measures beyond those of other EU schemes to better support existing SMEs. While start-up and newly created business are supported through the business incubators of the KICs, existing SMEs with high growth potential have greater difficulty in taking full advantage of the support offered by the EIT. In particular, the participation of SMEs in the innovation-driven project action line is very limited.

## 60

Moreover, all KIC partners interviewed stated that the grant payment cycle is an obstacle because it does not meet the financial needs of SMEs. The payment cycle of the KIC is a significant constraint for financially weaker partners, such as SMEs which do not have the financial capacity to cover the funding gap (see paragraph 50).

## 61

The data gathered by the EIT is piecemeal because SME reporting is not mandatory. However, over the 2010-2014 period, SMEs received less than 5 % of the EIT's financial support<sup>29</sup>.

## 62

Because SMEs are indirect recipients and are not accounted for, the wider picture may not be so bleak. Survey respondents stated that the KIC partnerships have created an environment in which start-ups, spin-offs and SMEs can grow. KICs do provide support to start-ups/SMEs, especially via their business incubators. However, creating better conditions to favour SMEs by setting clear strategies and objectives can only increase the SMEs' participation in the KICs — see **Box 9** for examples of criticisms of the lack of effective EIT support for SMEs.

<sup>29</sup> Data on SMEs is only available for one KIC.

### Box 9

#### Examples of criticisms of SMEs' participation

'[The] EIT has continuously lacked a clear message towards SMEs ...'

'SMEs are critical for innovation in the EU and they should be involved, but now the focus is on start-ups and the heavy bureaucracy and inefficient communications are only for large companies.'

'SMEs are not sufficiently represented in KIC governance, preventing their constraints and interests from being taken into account.'

Source: Audit survey.

### **There are not enough concrete synergies and complementarities**

#### **63**

Until the business plans of 2016, there were few effective incentives for a KIC to seek synergies with another KIC. Competitive funding between KICs provides a stimulus for a KIC to perform better. However, it discourages cooperation between them because any benefits would be shared with a funding rival. Although some scientific topics may be common to different KICs, in particular between KIC InnoEnergy and KIC Climate, there is no evidence of concrete output resulting from inter-KIC collaboration over the period under review (2010-2014).

#### **64**

The plethora of EU research and innovation programmes makes the creation of synergies between them difficult. Interaction between KICs and other EU initiatives is growing but needs to be further developed.

### **Some EIT elements are well appreciated: focus on the market, long-term perspective, autonomy of the KICs and the co-location centres**

#### **65**

A key difference from other existing research and innovation public schemes is the main objective of the EIT to focus on the market. The main objective of the EIT, 'to transfer higher education, research and innovation knowledge into a business context and their commercial application', has been ranked by the respondents to the survey as the most important objective the EIT should strive to achieve.

#### **66**

The long-term perspective of the EIT's financial support for the KIC partnership is a unique feature appreciated by the beneficiaries. In principle, the EIT instrument allows mid- to long-term planning of innovation activities which no other public scheme can offer. However the use by EIT of annual grants has undermined this at KIC partner level (see also paragraphs 42 to 45).

**67**

As stipulated in the EIT's legal basis, the KICs 'shall have substantial overall autonomy to define their internal organisation and composition, as well as their precise agenda and working methods'. This level of autonomy is valued by the KIC partners. It has facilitated the bottom-up approach sought by the innovation community. In contrast with traditional public schemes, where research and innovation topics are developed using a top-down approach dictated by budget requirements, the KIC concept allows more flexibility in the selection of the activities, a feature particularly welcomed by the partners.

**68**

Co-location centres (see *Annex I*) constitute another specificity of the EIT model the KIC partners have appreciated. A co-location centre is where the integration of the innovation triangle can take place. Articulated around thematic or regional areas, the co-location centres lead projects, develop ideas, bring regional partners together and design strategies. They coordinate and execute partners' administrative tasks related to the KIC and offer a common space for discussing partners' concerns. In some cases, they also offer working premises for the start-ups.

### The implementation of the EIT model needs to improve

#### The EIT is not yet fully autonomous

**69**

The EIT has not yet obtained its own full autonomy. This delay is longer than usual: other EU bodies such as the JTI (also created in 2008) took no more than 3 years to obtain full financial autonomy. According to DG Education and Culture, this was due to 'the limited leadership and managerial abilities of the EIT management'<sup>30</sup>. The high turnover in senior management has been a continuing cause of this (see paragraph 84).

30 Annual activity report of DG Education and Culture 2013.

**The EIT has not fulfilled its role as an impact investor**

**70**

The EIT is often presented as an ‘entrepreneurial-driven innovation impact investment institute’. The legal basis of H2020 states ‘the EIT ... takes a results-oriented approach.’ In its 2012-2014 triennial work programme, the EIT highlighted its objective to become an ‘engaged impact investor’.

**71**

Although conceived and presented as an impact-oriented institute, the EIT mostly focuses on compliance with the rules and on its own budgetary absorption. In September 2014, several EIT board members emphasised the need to reorient the EIT towards being an impact-driven institute. The EIT rarely rejected costs based on lack of performance prior to 2015.

**72**

Until 2015, the assessment of the annual performance of the KICs by the EIT had little or no impact on the level of the final grant payment. The annual assessments often report that several objectives set in the planning stage are not or only partially met, but the final amount of the grant was nevertheless paid (see **Box 10**).

**Box 10**

**Example of a lack of performance of a KIC**

The assessment of the business plan of a KIC in 2013, carried out by the EIT project officers with the help of external experts, stated that ‘when it comes to the key highlights mentioned in the 2013 business plan, Climate-KIC achieved only moderate progress ... Concerning the 18 strategic objectives specified in the 2013 BP, Climate-KIC has managed to fully meet eight of them, while seven of them have been addressed only partially and three of them have not been met so far’.

### **The competitive funding mechanism undervalues performance**

#### **73**

Competitive funding should be geared to rewarding performance. 40% of the total grant to the KICs for 2015 was allocated via a competitive process, based on an assessment of three pillars: (1) the past — performance in 2013; (2) the future — the 2015 business plan; and (3) implementation of the KIC multiannual strategy, via an EIT Governing Board hearing. Each of the three pillars had equal weighting. As the third pillar is both forward and backward looking, past performance and plans for the future receive, in reality, equal weighting. The EIT's competitive funding thus only partially rewards performance.

### **There are significant administrative and audit burdens on KIC partners**

#### **74**

The EIT largely copied its operational framework and processes from traditional EU research programmes, although it was not legally bound to do so. Whereas most EU programmes fund single projects, the EIT funds a portfolio of activities through the KICs. However, the related processes have not been adjusted to take into account this fundamental difference. For example, using the same threshold of 325 000 euro is likely to trigger the need for more certificates because activities (as opposed to single projects) will often exceed it (see paragraph 79).

#### **75**

The costs declared by the KIC partners are subject to many financial checks under this operational framework. Several KIC partners interviewed or surveyed by the Court complained that they sometimes need to provide the same information more than once.

#### **76**

The yearly reporting of the KIC complementary activities, both in the business plans and in the financial reports submitted by the KICs, is EIT-specific and adds a considerable burden with limited added value (see paragraph 33). The yearly statements submitted by the KICs include a detailed breakdown of the KIC complementary activities costs. The audit certificates obtained on KIC complementary activities in 2015 covered the 2010-2014 period.

### 77

Checks on the costs reported by the KIC partners are required by the legal framework applicable to all EU bodies (agencies and joint undertakings) awarding grants. These checks are carried out both before (*ex ante*) and after (*ex post*) the KICs receive the final grant payment from the EIT.

### 78

*Ex ante* checks include the certification of the cost statements by an independent auditor contracted by the KIC partner and some desk checks carried out by the financial officers in the EIT. *Ex post* checks are carried out by a private audit firm contracted by the EIT which checks a sample of KIC partners on the spot. The Court carries out an annual audit on the basis of which it issues an opinion on the reliability of the EIT annual accounts and the legality and regularity of the transactions underlying these accounts. It issued qualified opinions on the transactions underlying the EIT's 2012 and 2013 accounts on the basis of a material level of error. The 2014 accounts were not qualified.

### 79

Both the legal provisions and the material level of error found by the Court confirm the need for effective financial checks. However, there are various options which would increase the efficiency of the check and reporting requirements, such as:

- using a simpler funding model through a greater use of lump-sum payments and fixed rates;
- requiring a financial certificate by an independent auditor on selected costs by single KIC partner based upon an appropriate threshold for each activity (see paragraph 74); and
- increasing the threshold, currently set at 325 000 euro, triggering the need for certification of the cost statements.

## The EIT is under-resourced and has in the past been poorly managed

### 80

The EIT's headquarters had between 40 and 50 staff over the 2011-2014 period. The number of project officers compared to the grant budget is much lower than for most other EU research grant programmes (the budget managed per staff member under FP7 in the themes of ICT, Energy and Environment<sup>31</sup> varied from 12.5 to 20.4 million euro<sup>32</sup>). The EIT has one dedicated project officer for each KIC, whose annual budget may be up to 400 million euro. In addition there are three cross-KIC officers responsible for the action lines of education, innovation and entrepreneurship.

### 81

As they do not always have sufficient technical knowledge in the related domains, the EIT outsources part of the assessment of projects to external experts. For the assessment of the 2013 performance reports, the EIT had no senior official in charge of innovation. The in-house capacity of the EIT to assess the operational performance of the KICs is therefore limited.

### 82

Despite the large increase in the budget from 309 million euro (2008-2013) to 2.7 billion euro (2014-2020) and the fact that the number of KICs has grown from three to five as from late 2014, no significant increase in the number of posts is provided for. There is a risk that the EIT will not have sufficient capacity to deal with the expanded workload.

### 83

The high staff turnover and many vacancies at the EIT has been a problem: 25 of the 40 staff members who were working with the EIT at the end of 2011 left within 3 years and 30% of the posts were vacant at the end of 2013 (see **Figure 10**). This fell to 16% in 2015. However, staff turnover remains high at 17% in 2015. Several vacant posts are in the unit responsible for the technical and financial assessment of the KIC's reports. The salary package the EIT can offer is lower than that of most other EU bodies, which is a factor contributing to the high staff turnover and vacancy rate<sup>33</sup>.

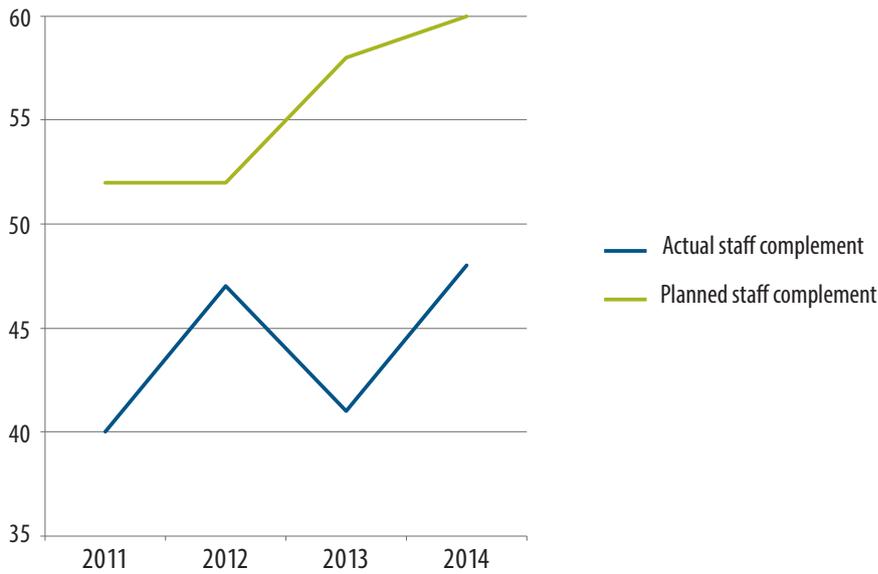
31 The three themes linked to the three first KICs launched by the EIT.

32 Special Report No 2/2013, 'Has the Commission ensured efficient implementation of the seventh framework programme for research?' (<http://eca.europa.eu>).

33 The remuneration of the staff of EU institutions, agencies and other EU bodies is multiplied by a correction coefficient depending on cost of living in the place of employment. For Hungary this coefficient was set at 71.4% for 2014-15, which means that agents working for the EIT earn almost 30% less than their colleagues employed in Brussels.

Figure 10

Actual vs planned EIT staff complement



Source: EIT.

84

Since its creation the EIT has been managed by five different Executive Directors/ Acting Directors (see **Table 1**). Two of these left after less than a year in office. Three high-ranking EIT staff were dismissed in 2013. As at 1 January 2015, one Head of Unit post was vacant and another had been occupied ad interim since 2013. The rapid turnover at senior management level is disruptive and impairs leadership and strategic continuity.

Table 1

Executive Director of the EIT

Executive Director	Start of mandate	End of mandate	Duration of mandate
1st Director Resources of DG Education and Culture ( <i>ad interim</i> )	April 2008	October 2009	1.5 years
2nd Director	1.11.2009	31.8.2010	10 months
3rd Director	1.9.2010	30.6.2011	10 months
4th Director	1.7.2011	31.7.2014	3 years
5th Acting Director	1.8.2014	Ongoing	Ongoing

Source: EIT.

The EIT financial support is concentrated

85

In each KIC the bulk of the EIT financial contribution is concentrated in a core of KIC partners: the top 10 partners received between 49 % and 65 % of the EIT’s financial support to each KIC (see **Table 2**). In KIC InnoEnergy, the top 10 partners account for almost two thirds of the EIT’s contribution, with the rest spread between the other 220 KIC partners. In addition to the significant role played by the universities in all action lines, this concentration can be explained by the dominant role of the core KIC partners, which have been heavily involved since the inception of the KICs. At the other end of the scale, most KIC partners received less than 500 000 euro over the 2010-2014 period, and between 20 % and 58 % of them received less than 100 000 euro over that period.

Table 2

Distribution among KIC partners of the EIT’s financial contribution

2010–2014	Climate-KIC	KIC InnoEnergy	EIT Digital
Top 10 beneficiaries as a % of EIT total funding	55 %	65 %	49 %
Number of KIC partners active in EIT funded activities	205	230	114
Number of active KIC partners receiving less than 500 000 EUR in %	76 %	85 %	52 %
Number of active KIC partners receiving less than 100 000 EUR	83	133	23
Number of active KIC partners receiving less than 100 000 EUR in %	40 %	58 %	20 %

Source: EIT.

86

The EIT financial contribution is highly concentrated in five countries (73 %) while only two countries of the EU 12<sup>34</sup> have received an EIT financial support (6 %) (see **Table 3**). A two-speed Europe risks being further engrained, with EIT expenditure concentrated in countries with developed research infrastructure (see also paragraph 102).

34 The EU 12 refers to the 12 countries having joined the EU between 2004 and 2007.

Table 3

EIT’s financial contribution for each KIC split by countries (2010-2014)

in % of total EIT contribution	Climate-KIC	KIC InnoEnergy	EIT Digital	ALL EIT <sup>1</sup>
Top five countries	88 %	85 %	79 %	73 % <sup>2</sup>
EU 12	4 %	10 %	2 %	6 % <sup>3</sup>
Others	8 %	5 %	19 %	21 %

- 1 The top 5 countries differ from one KIC to another explaining why the aggregated top 5 is lower than the individual KIC.
- 2 The top five countries receiving EIT support are the Netherlands (24 %), Germany (15 %), France (13 %), Sweden (12 %) and United Kingdom (9 %).
- 3 Poland (4 %) and Hungary (2 %) are the two EU 12 countries benefitting from the EIT financial support.

Source: EIT.

## The KICs lack transparency

### 87

This concentration of EIT financial support among a limited number of partners should be monitored to ensure that it is not the result of an unfair allocation of public funding within the KIC — see **Box 11**. In some cases, a partner is a member of the committee that reviews proposals and selects the projects. This risks creating a conflict of interest and generating a lack of trust in the KIC. Moreover, although in general the selection process is well documented, when the partners submit their proposals they do not always know to whom the grants are eventually allocated. Almost half of the respondents to the survey do not believe that the selection of the activities to be funded by EIT within the KIC is fair and transparent.

### 88

Despite the existence of many communication channels, some KIC partners have little knowledge of the progress and specific results of projects for which they did not take the lead. In some joint projects, each partner executes its part, but is not aware of further developments. This lack of communication can hamper the dissemination of knowledge.

#### Box 11

### Concerns over the concentration of EIT financial support and the lack of transparency

Some KIC partners have expressed their concerns by stating that: 'there are a couple of influential partners and they distribute the funds among themselves. The processes to select proposals for activities are highly [opaque]' and 'in theory the EIT is a good idea, but in practice it just serves to fund initial ... partners which are mainly large organisations ... Moreover the assessment of the projects [is] made by the partners themselves which is a conflict of interest ...'

**The KICs have stimulated an innovation network and entrepreneurial culture but with little evidence of tangible results or impact to date**

**89**

Through the EIT, the KICs have brought together over 500 partners across disciplines, Member States and sectors. The number of partners of the first three KICs created in 2010 has increased considerably: Climate-KIC grew from 24 partners at the start in 2010 to 209 active partners at the end of 2014, EIT Digital from 31 to 115 and KIC InnoEnergy from 27 to 242<sup>35</sup>. The list of partners includes several top European companies, as well as top European universities and research institutes. Businesses account for 56 % of all KIC partners, universities 19 % and research institutes 13 % (see **Figure 9**).

**90**

The KIC partnership has offered new opportunities to innovate (as agreed by 86 % of the respondents to the survey). These include some of the biggest names in business. Working with them are prestigious higher education institutions and research centres together with cities, regions and non-governmental organisations. This contributes to reducing the fragmentation of the European innovation landscape in the areas of operations of the KICs. No other EU programme has such a pan-European network.

**91**

KIC partners generally agree that through the EIT a number of education activities have been launched successfully: around 75 % of the respondents to the survey confirmed that the KIC partnership has generated education programmes that create new profiles of entrepreneurial and skilled talents (see **Box 12**).

35 Defined as KIC partners that have declared KIC activities/costs during the period 2010-2014.

**Box 12**

**EIT Digital Master School programme**

The EIT Digital Master School programme offers eight technical majors and a minor in innovation and entrepreneurship. Twenty top EU universities, renowned researchers and leading businesses are in partnership to provide cutting-edge ICT excellence in combination with innovation and entrepreneurship training, leading to a double degree and an EIT-labelled certificate.

## Observations

### 92

All persons interviewed and almost 80 % of the respondents to the survey agreed that KIC partnerships have promoted an entrepreneurial, creative-thinking culture. However, there is as yet no assessment of the impact of the EIT on business creation and whether there has been a real increase in the level of risk acceptance in Europe. The indicator 'number of start-ups or new businesses created' is not informative without context or a benchmark.

### 93

Using the EIT's core KPIs, in 2014 the three KICs together reported the creation of 90 start-ups, the incubation of more than 400 business ideas, 52 new and 19 improved products, services or processes, 126 cases of knowledge transfers and 159 cases of knowledge adoption. These are output-based indicators (see paragraph 54). For example, the EIT's assessment report for EIT Digital points out that 'the innovation activities have produced few tangible results in terms of products that are close to the market'.

### 94

The 2014 results in the area of education are mixed. The number of master's and PhD students enrolled in EIT-labelled programmes in 2014-2015 rose to almost 1 000, but the enrolment for the master's and doctoral schools organised by two of the three KICs remained below expectations. The drop-out rate at registration of students who have been accepted to the programmes is reported to be particularly high. Furthermore, without proper monitoring, the low intake of EU students in KIC master's and PhD programmes further raises the question of the EIT's European added value<sup>36</sup> because it is unknown if non-EU students will stay in the EU or work for an EU organisation.

### 95

According to the assessment of the 2014 KIC reports by the EIT, EIT Digital and KIC InnoEnergy have achieved only modest progress towards the integration of the KIC knowledge triangle actors during the 5 years since their creation.

<sup>36</sup> European added value is the additional value which the EIT creates for the EU or its Member States. It is additional and has a European dimension because it could not have been created by Member States acting alone.

## The future

### New logo (2015)



### 96

During 2015, the EIT took several measures to address many of the shortcomings highlighted in this report. Their impact remains to be seen.

### Financial sustainability principles have been introduced

### 97

In 2015 the EIT adopted the financial sustainability principles<sup>37</sup>. This document sets definitions, funding principles and incentives for the KICs to achieve financial sustainability.

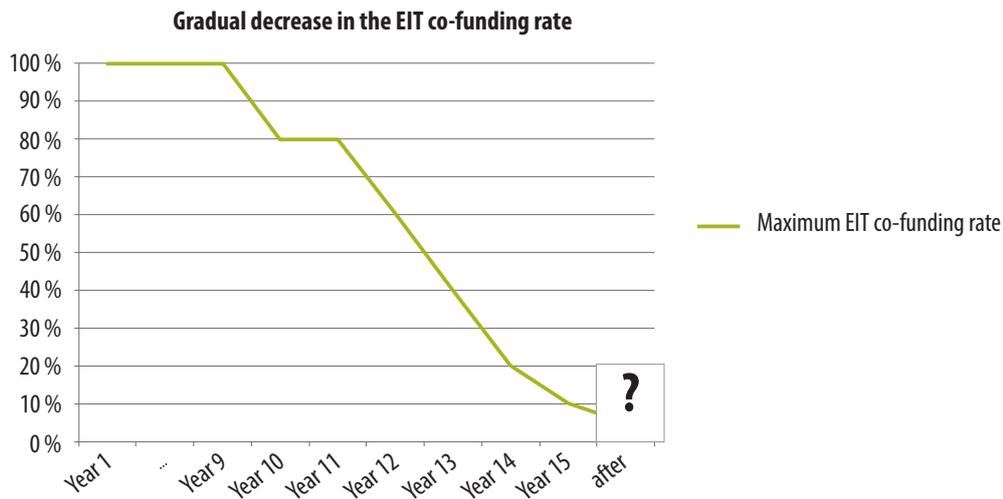
### 98

After 10 years of a KIC's existence, the maximum EIT contribution to a KIC will be gradually reduced from up to 100 % of the EIT-funded activities costs to a maximum of 10 % in year 15. After year 15, a pre-defined minimum level of EIT funding to a KIC can be decided (see **Figure 11**). The sustainability principles do not indicate how the KICs will replace the EIT funding. It is considered the responsibility of the KICs to develop and implement their sustainability strategies. Detailed strategies are not yet in place. By 2015, the KICs had made little progress in this area and the EIT continued to fund close to 90% of the EIT-funded activities costs.

37 Decision 4/2015 of the Governing Board of the EIT, 'Principles on KIC's financial sustainability'.

Figure 11

## Scaling down of the EIT co-funding rate



Source: ECA.

### The definition of KIC complementary activities has been revised

#### 99

In 2015 the EIT amended the definition of KIC complementary activities and provided additional guidance to the KICs. It also reviewed, for the first time, the KIC complementary activities over the 2010-2014 period. The review was limited in scope and consisted of two parts: a certification by independent auditors of the KIC complementary activities expenditure reported in the financial statements; and a review by the EIT project officers of the proportionality and the existence of a clear link between the EIT-funded activities and the KIC complementary activities.

#### 100

The EIT also introduced new guidance for the preparation of business plans. Starting from the 2016 grant agreements, KIC complementary activities will be reviewed at the business plan assessment stage to ensure a clear link between planned EIT-funded activities and the KIC complementary activities.

### **More meaningful key performance indicators will be developed**

#### **101**

In the 2015-2017 triennial work programme the EIT stated that a refined monitoring system will be put in place 'geared towards results and impacts'. In 2015, it launched a tender procedure to design impact-based KPIs and created a working group to address this particular issue. In addition, it intends to draw up specific KPI measurement results in knowledge-triangle integration.

### **The EIT is trying to involve more countries**

#### **102**

The guiding principle of the EIT to date has been technical excellence, thereby favouring partners in Member States with advanced research and innovation infrastructure. The EIT has realised that this has led to a high geographical concentration of KIC partners in a limited number of EU Member States (see paragraph 86) and has created the regional innovation scheme, an outreach mechanism to better promote innovation in specific regions, to spread its support more widely. In order to achieve this, 10% of the annual competitive EIT contribution to the KICs will be allocated from 2016 to support and mainstream the regional innovation scheme.

### **New framework partnership agreements are currently being discussed**

#### **103**

To align its framework with that of H2020, the EIT endeavoured to make the KIC partners sign new framework partnership agreements in 2015. The governance principles to be introduced through a code of conduct, as well as the proposed rules on intellectual property rights, met a lot of resistance. The signature of the new framework partnership agreements has therefore been postponed.

## 104

We conclude that, despite a valid *raison d'être*, the EIT's complex operational framework and management problems have impeded its overall effectiveness. The impact of the actions undertaken by the Commission and EIT in 2015 (see paragraphs 96 to 103) remains to be seen. The following conclusions and recommendations are pertinent and need to be followed up.

### Rationale

## 105

The establishment of the EIT in 2008 was built on an ambitious and groundbreaking idea: promoting innovation through the integration of the three sides of the knowledge triangle. The reasons to build such an instrument were valid: weak links between the worlds of education, science and business; a lack of entrepreneurial culture; and little success in bringing EU research results to the market (see paragraphs 19 to 23). The EIT is the first EU initiative to cover the entire innovation cycle at EU level, from laboratory to market, bringing together over 500 partners across disciplines ranging from academia to research and business, allowing a critical mass required to tackle major societal challenges to be built up (see paragraphs 89 and 90).

### Design

## 106

While some unique features of the EIT have been successfully designed (see paragraphs 65 to 68), some key concepts and strategic elements were not sufficiently considered from the outset (see paragraphs 24 to 64). Because the activities not funded by the EIT are included in the calculation of the amount to be paid, the funding model is overly complex. The 'strong leverage effect' asserted by the EIT has not yet been demonstrated.

## Conclusions and recommendations

### **Recommendation 1 — The Commission should propose an amended EIT legal basis to the European Parliament and Council, revising the EIT's funding model.**

---

The KIC activities not funded by the EIT should not be included in the calculation basis when determining the EIT'S financial contribution to the KICs, as was the case in the original 2008 legal basis establishing the EIT. Removing the 25 % funding condition would alleviate much of the operational and financial reporting burden of the KIC partners. The leverage effect should be measured to demonstrate the EIT'S success in attracting additional funding for innovation.

**Target implementation date:** As soon as possible after the 2017 evaluation.

### **107**

There are weaknesses in the design of the core operational processes. The means of granting the EIT financial support are ill suited given the needs of the KIC partners; the annuality of the grant and its systematic late signing make the smooth implementation of the innovation activities the EIT is aiming to promote difficult (see paragraphs 41 to 50). The grant payment cycle is a significant constraint for financially weaker partners such as SMEs, which do not have the financial capacity to pre-finance expenditure (see paragraph 59).

### **Recommendation 2 — The EIT grant agreement (a) should cover a longer period than the calendar year and (b) should be signed before the start of the activities.**

---

A longer time perspective would not only offer greater legal and financial security for the KIC partners but would also further consolidate the innovation activities in line with the multiannual strategy adopted by the KICs. It would also ease the administrative burden by reducing the annual reporting of the KIC partners and would facilitate the assessment of the KICs' performance over a longer period of time. Signing the grant agreement in due time would allow the legal and financial continuity of the KICs' innovation activities, thereby preventing a 'stop-go' situation.

**Target implementation date:** Grant agreement for the period starting 1 January 2017.

### Implementation and impact

#### 108

Seven years after inception, the EIT is still not fully operationally independent from the European Commission. It is not the impact-driven institute that was envisaged (see paragraphs 70 to 71). The performance of a KIC is not sufficiently taken into account when the final payment of the grant is made (see paragraph 72). The EIT is a unique instrument within the EU's initiatives but follows the general EU research and innovation framework too strictly (see paragraph 74). The EIT is under-resourced and has in the past been poorly managed (see paragraphs 80 to 84).

**Recommendation 3 — The EIT should refocus its approach to delivering impact. To that end, it should seek greater autonomy and make use of the flexibility in Horizon 2020's legal basis. In particular, it should adopt specific rules tailored to the needs of the KIC partners. The EIT should resolve its staffing issues to enable it to continuously monitor KICs' performances.**

---

The EIT should urgently obtain its financial autonomy, as the original target set by the European Commission was 2010. Granting more autonomy to the EIT can only boost its leadership capacity, a prerequisite for this public scheme to be successful. Moreover, the EIT should better reflect its mission statement and become an impact-driven institute by tailoring its own rules. Filling vacant posts and stability in senior management are essential.

**Target implementation date:** During 2016.

#### 109

The EIT has contributed to the integration of the knowledge triangle and has encouraged a culture of entrepreneurship. However, it is difficult to assess the performance of the EIT since the start of operations in 2010. There is a lack of robust and relevant reporting and monitoring processes and few impacts are visible (see paragraphs 51 to 53). The KICs lack transparency in the selection of the activities to be financed by the EIT (see paragraphs 87 to 88).

### **Recommendation 4 — The EIT should develop impact-based analysis. The EIT should also streamline its monitoring and reporting processes.**

---

The Court welcomes the EIT's decision to review its indicators in 2015 by implementing a new key performance indicator management system. This should be aimed at measuring the impact of each KIC as the current processes do not allow a detailed analysis of the achievements of the activities financed by the EIT. In particular, the impact of the innovation activities is currently undemonstrated. Furthermore, to enhance the monitoring process and to better fine-tune financial analysis (especially for SMEs and the management costs of the KICs), the EIT should consider standardising the financial reporting processes across all KICs.

**Target implementation date:** During 2016.

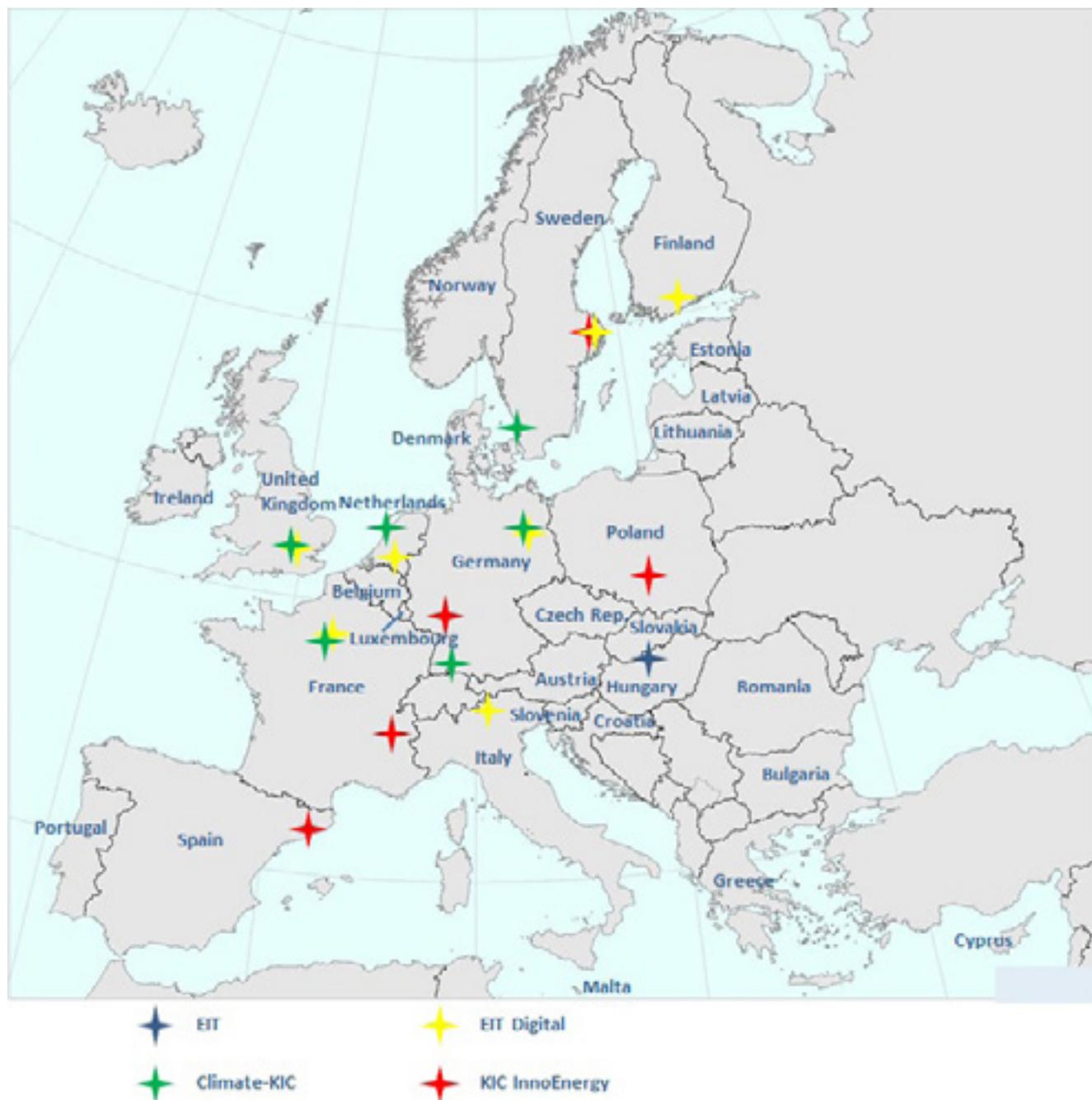
This Report was adopted by Chamber IV, headed by Mr Milan Martin CVIKL, Member of the Court of Auditors, in Luxembourg at its meeting of 3 February 2016.

*For the Court of Auditors*



Vítor Manuel da SILVA CALDEIRA  
*President*

## Regional co-location centres across Europe



Source: Based on Eurostat data.

## Objectives of the EIT

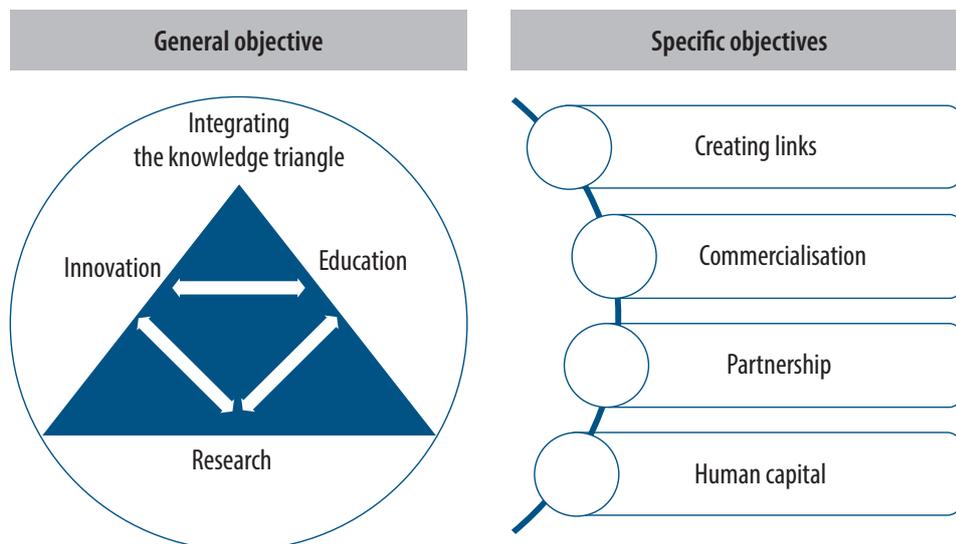
The general objective of the EIT is ‘to contribute to sustainable European economic growth and competitiveness by reinforcing the innovation capacity of the Member States and the Union in order to address major challenges faced by European society. It shall do this by promoting synergies and cooperation among, and integrating, higher education, research and innovation of the highest standards, including by fostering entrepreneurship’<sup>1</sup>.

This general objective has been fine-tuned by Horizon 2020’s legal basis into four specific objectives for the 2014-2020 period<sup>2</sup>:

- create links by integrating education and entrepreneurship with research and innovation;
- adopt a business logic and a results-oriented approach;
- overcome fragmentation with the aid of long-term integrated partnerships; and
- nurture the EU’s main innovation asset — its highly talented people.

See **Figure** below for an overview of the objectives of the EIT.

### Overview of the objectives of the EIT



Source: ECA.

<sup>1</sup> Article 3 of Regulation (EU) No 1292/2013.

<sup>2</sup> Horizon 2020, the framework programme for research and innovation.

Other sub-objectives of the EIT include:

- the development of an EIT label to attract and retain the best innovators from the knowledge triangle;
- the sustainability of the KICs; and
- the promotion of SME participation.

Thus the EIT aims to pool the best minds and ideas from universities, research centres and private companies to reach a critical mass 'to reinforce the innovation capacity of the Union and its Member States in order to boost their capacity to convert outputs from research into high-value products and services'<sup>3</sup>. It is this 'boosting' which the EIT should be able to demonstrate.

<sup>3</sup> As set out in Section 1.1 of Decision 1312/2013/EU.

## Executive summary

### IV

The EIT has adopted a series of measures to address shortcomings in effectiveness. The EIT has addressed the complexities in the operational framework through the Task Force for Simplification, the EIT monitoring strategy and the good governance and financial sustainability principles. Finally, the EIT has strengthened its leadership, management and governance structures.

### VI (a)

The KIC complementary activities are essential for the joining together of private and public innovation efforts. They also measure the building of innovation capacity on top of existing structures and capacities.

The Commission and the EIT acknowledge that the reporting and monitoring of the KIC complementary activities need further reflection and improvement. To improve the way KIC complementary activities are used as part of the EIT funding model, the EIT in 2015 carried out a review to provide assurance that the amounts accepted in the 2010-2014 period were proportionate and duly linked to the KAVA and that the rule of financing a maximum 25% of the total expenditure of the KICs was respected. Furthermore, additional guidance was provided in 2015 to strengthen the link between KAVA and the KIC complementary activities.

KAVA are EIT-funded activities carried out by partner organisations or KIC legal entities, if applicable, contributing to the integration of the knowledge triangle of higher education, research and innovation, including the establishment, administrative and coordination activities of the KICs, and contributing to the overall objectives of the EIT.

### VI (b)

The long-term relations between the KICs and the EIT are governed by the FPA and developed contractually through the grant agreements, largely based on the Horizon 2020 model. In order to allow for long-term planning and assessment of KIC strategies and activities, a strategic agenda for the KIC is annexed to the FPA. The document presents the strategy of the KIC, its objectives, its expected impact and its activities under the framework partnership together with a multiannual business model and financial plan for achieving market targets and strategic milestones. The EIT awards specific annual grants under the umbrella of the FPAs. The fact that grants are awarded on annual basis reflects the need to adapt quickly to the changing environment in which innovation happens.

Furthermore, the success and results of many EIT activities that have created entrepreneurial students, start-ups and business ideas that are being developed show that the EIT model is suitable to deliver innovation activities. A Task Force for Simplification is working to further enhance the efficiency of the delivery and has already adopted a series of concrete measures with a roadmap for further simplifications under way.

### VI (c)

The achievement of financial sustainability is one of the most challenging aspects of the EIT's mission. Progress towards financial sustainability has been made since the financial sustainability principles were adopted by the EIT in March 2015. The two KICs designated in 2014 have substantial own funding — one of them is able to fully finance all management and overhead costs of the KIC legal entity in its first year of operation. See the reply to paragraph 38.

The level of business interest in the EIT-KIC innovation model is high, as indicated by businesses comprising 56% of total KIC partners. This creates an outstanding potential to strengthen the level of business involvement in the KICs, as detailed in replies to paragraphs 56 to 58.

Pursuant to the EIT founding regulation, the EIT should operate through excellence-driven, autonomous partnerships of higher education institutions, research organisations, companies and other stakeholders. The principle of excellence implies a certain level of concentration in Member States with high innovation capacity. Nevertheless, the EIT has taken robust initiatives to spread the support of the EIT to a higher number of beneficiary Member States by way of the EIT regional innovation scheme (EIT RIS). The new EIT RIS guidance, issued by the EIT in 2015, is being implemented in the 2016 business plans of the KICs, ensuring a widening of participation. Finally, the growth of KIC partners to over 800 in recent months and the opening of new co-location centres across the EU by new KICs demonstrates that funding is no longer so concentrated in a few Member States or partners.

### VI (d)

The EIT performs exhaustive performance assessments of the KICs. The EIT analyses the implementation of the KIC business plan annually, both through quantitative performance indicators and through qualitative reviews done by external experts and the EIT's staff. More widely, the EIT also conducts on-site monitoring and topical reviews of the KICs' activities. These tools, taken together, provide a very informative picture of KIC performance.

The EIT Governing Board adopted a comprehensive monitoring strategy on 3 December 2015, which will measure results and impact.

### VII

By design, the EIT balances between being an impact-driven institute and a responsible provider of Community funds. The EIT cannot provide funds without assurance any more than it can fund underperformance. The EIT has been consistently improving its verification of the KICs' performance. Most recently, the EIT rejected more than 1.5 million euros of activity costs from one KIC as a result of the EIT's assessment of the KIC's performance. The EIT has been further strengthening its impact assessment: the latest spring review between the EIT Governing Board and the KICs focused on impact; the revision of the key performance indicators aims to increase impact; the adoption of financial sustainability principles and the ongoing feasibility study for an impact fund are all evidence of the EIT's continuing focus on the impact and performance of the KICs (please also see replies to paragraphs 71 to 73).

### VIII

The Commission and the EIT are confident that the measures launched in 2015, including those covered in paragraphs 97 to 105, address the main problems identified by the Court.

### IX (1)

The Commission and the EIT accept the recommendation.

### IX (2) a)

The Commission and the EIT partially accept the recommendation and will explore to what extent it is possible to further extend multiannuality.

### IX (2) b)

The Commission and the EIT accept the recommendation.

## Reply of the Commission

### IX (3)

The EIT and Commission accept this recommendation.

### IX (4)

The Commission and the EIT accept the recommendation. The EIT will continue to develop focus on impact as already launched during 2015.

## Introduction

### Box 2 — The definition of innovation

The EIT has, since it was established in 2008 (Regulation (EC) No 294/2008), been operating under a definition of innovation which includes the creation of new markets and of value to society. The definition used here has been updated by the OECD to reflect this broader concept of innovation in its 2010 and 2015 innovation strategies<sup>1</sup>.

The EIT's mission, and thereby also its objectives, rests on the definition of innovation, which includes societal goals.

## Observations

### 25

Placing the EIT under the lead responsibility of DG Education and Culture (which also fully participates in Horizon 2020 via its Marie Skłodowska-Curie actions) was indeed a way to ensure that the higher education sector is well reflected within the knowledge-triangle integration which is essential to the EIT. The primary mechanism to ensure this is the EIT Governing Board, where the balanced participation of the different sides of the triangle has always been assured. The Commission (DG Education and Culture) takes the necessary steps to ensure that there is good coordination between the relevant services of the Commission.

---

1 OECD 2015 innovation strategy, page 15 (<http://www.oecd.org/sti/OECD-Innovation-Strategy-2015-CMIN2015-7.pdf>), 'A scope beyond science and technology, involving investments in a wide range of knowledge based assets that extend beyond R & D. Social and organisational innovations, including new business models, are increasingly important to complement technological innovation.'

OECD 2010 innovation strategy, page 20 (<http://www.oecdbookshop.org/browse.asp?pid=title-detail&lang=en&ds=&ISBN=9789264084704>), 'Innovation, thus defined, is clearly a much broader notion than R & D and is influenced by a wide range of factors, some of which can be affected by policy. Innovation can occur in any sector of the economy, including government services such as health or education.'

The Horizon 2020 reference ([https://ec.europa.eu/research/participants/portal/desktop/en/support/reference\\_terms.html](https://ec.europa.eu/research/participants/portal/desktop/en/support/reference_terms.html)).

### 26

The coordination of the different Commission services is ensured by DG Education and Culture and takes the form of direct interaction between the KICs and the EIT with the relevant Commission services. DG Education and Culture has developed different formats to facilitate this, from the operational level to the strategic level. DG Education and Culture organises every year a 1-day conference with workshops where KICs and EIT meet the Commission services from various DGs. Informal ad hoc meetings — EIT with Commission services or KICs with Commission services — are also organised when needed to facilitate collaboration. DG Education and Culture also coordinates the inter-service consultation prior to the adoption of the triennial work programme in which all DGs are formally involved. All concerned Commission services take part in the Inter-Service Steering Group for the mid-term EIT evaluation.

The EIT also regularly and directly interacts with the Commission services, notably but not exclusively with DG Research and Innovation and DG Internal Market, Industry, Entrepreneurship and SMEs. For example, the EIT is in direct contact with the services of DG Research and Innovation concerning the next KIC call or concerning access to Horizon 2020 IT tools. As part of the annual meeting, DG Education and Culture supports bilateral EIT services meetings to coordinate the year's work on specific initiatives.

Significant contacts have been established during 2015 between DG Education and Culture, the EIT and DG Regional and Urban Policy in regard to the shared objectives of the EIT's regional integration scheme and smart specialisation strategies.

### 27

The presence of both types of activities is essential for the EIT's innovation model. It reflects the objective to build innovation (EIT-funded activities) on top of existing structures and capacities (complementary activities). The Commission and the EIT consider that the KIC added-value activities and the KIC complementary activities form a coherent set of innovation activities.

### 29

The KIC complementary activities concept was initially not sufficiently defined in detail, but it has been strengthened over time (see also paragraphs 100 and 101).

The weakness of the link between EIT-funded activities and the complementary activities addressed here by the Court has been recognised and the EIT has put in place changes in the first half of 2015 that will strengthen the verification of this link at the business planning stage.

### 31

The EIT has significantly strengthened the link between EIT-funded activities and KIC complementary activities. The 2015 business plan and grant agreements first introduced the principle of proportionality between the two. As of 2016, this link is further strengthened: the KIC complementary activities are now reviewed by the EIT at the KICs' annual business plan assessment stage. The results of these changes will be visible in 2016.

The EIT also takes into account the results and outcomes of each particular complementary activity. If there is a strong result, a relatively high cost of a KIC complementary activity can be accepted. The cost of KIC complementary activities must be proportionate to the cost of the EIT-funded activity and/or to the expected impact. Therefore, a relatively high KIC complementary activity can also be accepted if that activity has high impact in furthering the mission of the KIC.

## Reply of the Commission

### 32

The EIT is strengthening the verification of the EIT-funded activities and KIC complementary activities links at programming stage, i.e. when assessing the business plans, as from the 2016 business plan cycle. Consequently, the KICs will no longer be able to replace planned KIC complementary activities at the reporting stage without the EIT's approval, and there will no longer be uncertainty as to whether the costs of KIC complementary activities will be accepted at the reporting stage.

### Box 3 — Example of a KIC complementary activity with a less than 'clear link' to an EIT-funded activity

Complementary activities contribute in two ways to the achievement of KIC goals. They may either build on EIT-funded activities or form the basis from which the EIT can fund further innovation. Using the KIC complementary activities as only a funding lever takes too narrow an approach to innovation.

Furthermore, the EIT has further refined its guidance on KIC complementary activities to KICs as part of the annual business plan guidelines.

### 33

Innovation does not occur in isolation and requires complementary activities and ecosystems in which EIT-financed activities can be embedded.

However, the Commission and the EIT agree that the definition of complementary activities and how to measure more accurately the leverage from EIT funding requires further attention. The Commission and EIT therefore welcome the suggestions of the Court. The EIT has as a consequence already taken steps in this direction.

### 35

KIC complementary activities that provide the knowledge base for new added-value activities will logically always be 'retroactive' in the sense that the KIC complementary activities in question are completed before the EIT-funded activities start.

Some KIC complementary activities will be, by definition, non-additional. Instead, they will be the foundation for EIT-funded activities. These EIT-funded activities can lead to further leverage later in the process as they create products, processes or services which bring returns. If an original KIC complementary activity had not been in place, then the outcomes from an EIT-funded activity that relied on it could not appear either. For this reason, retroactive KIC complementary activities are needed in the EIT innovation model.

At the same time, the Commission and the EIT accept that such KIC complementary activities cannot be directly taken into account when calculating the financial leverage effect of EIT-funded activities.

As explained above, complementary activities are essential for innovation systems to function effectively, and are in line with a multiannual perspective.

### **Box 4 — A financial leverage effect cannot stem from a retroactive activity**

Complementary activities are necessary to provide the basis for or complement EIT financed activities. Not all complementary activities can be considered as providing leverage and improved definitions are needed to measure the leverage effect.

#### **37**

In kind contributions as complementary activities or cash contributions to complementary activities are essential for functioning innovation systems.

### **Box 5 - Example of non-additional KIC complementary activities**

The inclusion of new students does always involve more costs in terms of time of teachers to attend tutorials, lab equipment (notably in courses with a high practical component), management of internships in companies (which requires attention on the one-to-one basis) and the use of university services. That is why non-EIT-funded student costs can be justified as differentiated KIC complementary activity costs for an EIT-funded course.

#### **38**

The financial sustainability should not be understood as a complete halt in the EIT funding to KICs, but the EIT funding will decrease to a 'pre-defined minimum level' as defined in the *Principles on KICs' financial sustainability* adopted by the EIT Governing Board on 5 March 2015.

It is still to be demonstrated that 15 years are insufficient to develop and successfully implement a strategy towards financial sustainability.

The EIT Foundation was established to function on a different level and with a different purpose than the KICs. The KICs raise and secure funds with a possible return on investment in mind, and can generate income from their own activities, which was never the case for the EITF.

#### **39**

While it is accepted that achieving financial sustainability will be challenging, it is too early to pass judgment. OECD emphasises in its 2015 innovation strategy that a long-term perspective needs to be taken when measuring returns on investments in innovation. As a result, the data from the first 5 years of KIC operations are not enough to draw conclusions about long-term financial sustainability.

The EIT has been strengthening its efforts in this field. In line with the *Principles on KICs' financial sustainability*, the EIT is currently developing a template for reporting on KICs' financial sustainability that will be introduced in the reporting guidelines to ensure the proper reporting of income by KICs. The 2016 business plans and their assessments by EIT experts already show significant progress. All KICs have made this one of their priority objectives and activities are reviewed accordingly to create a return of income from activities. For example, one of the new KICs fully finances its management and overhead costs from own funds, which is a strong starting point to become financially sustainable.

The progress made by KICs towards financial sustainability will be assessed in 2016, after the reception of the first reports. In line with the principles for financial sustainability, the KICs will be reviewed more thoroughly on the progress made by the EIT after 7 years. The EIT has also set up a working group, hired an expert and launched a series of initiatives to support the KICs in their drive towards financial sustainability.

For all these reasons, it is too early to make a judgment about the KICs' financial sustainability in 10 years' time.

### 42

The amendment of business plans during implementation is a regular process that provides a high degree of flexibility for including innovation projects even in the last months of the duration of the grant agreements. This possibility was used extensively by KICs in the years 2010-2014. In 2014, five amendments that included new KIC activities were approved by the EIT.

Furthermore, the 2014 guidelines for the preparation of KIC business plans allowed KICs to include in the business plan KIC added-value activities not fully specified up to 15 % of the budget. The approach is being followed in an analogous manner in 2015, i.e. business plans include a description of the process for the selection of new activities and the precise definition of activities is provided when details are available.

In addition, KICs have the possibility to transfer up to 100 % of their budget between activities within the same budget heading, and up to 20 % across budget headings without any prior approval by the EIT. This provision is much more flexible and advantageous than in any other EU programme and further demonstrates that specific mechanisms were designed to support changes in a fast-reacting environment, which responds to the needs of innovation projects.

### 43

The annual budget of the EIT depends on the amount voted in the annual EU budget, typically in December of year  $n-1$ . The budgetary commitments of the EIT cannot be higher than the funds approved in the EU budget. This is the reason why the EIT signs annual grant agreements with KICs. However, additional measures aiming to take into account the multiannual dimension of some activities are being explored, in particular through the Task Force for Simplification.

### 44

The EIT's competitive funding allocation approach is based on performance-based budgeting, which has an in-built uncertainty and rewards excellence and impact. Providing long-term certainty on funding may be detrimental for a result- and impact-driven approach.

In addition, as indicated in replies to paragraphs 41 and 44, the KICs have a number of instruments at their disposal to provide insurance against short-term funding fluctuations. These include general financial market instruments, as well as flexibility in business plan design.

### **Box 6 — The European Fund for Strategic Investments<sup>2</sup> and its impact on the EIT budget — Second paragraph**

While funding for the KICs in 2016 has indeed been reduced, it is nevertheless sufficient for the three mature KICs to maintain substantial business plans and for the two newly established KICs to have a rapid growth path. More than €233 million was allocated to the three mature KICs, while €41 million went to the two new KICs in 2016.

<sup>2</sup> Opinion No 4/2015 concerning the proposal for a regulation of the European Parliament and of the Council on the European Fund for Strategic Investments and amending Regulations (EU) No 1291/2013 and (EU) No 1316/2013.

### 45

The arguments presented on the inappropriateness of the annual grant agreements should be balanced by taking into account the initiatives the EIT takes to combine the annual with the multiannual perspectives. It is important to note that the multiannual perspective is taken into consideration in the framework of the annual competitive funding allocation. Furthermore, in addition to the competitive funding there is a support funding element in the annual funding allocation to KICs. The support funding is distributed equally among the KICs and provides high-level security of funding. Also, it is important to note that the FPA provides the legal basis and 'commitment' from the EIT to support the KICs over a long-term period. As outlined above, there is also in-built flexibility within the annual grant cycle to stop and introduce innovative projects during the year, i.e. the annual cycle does not prevent flexibility for individual activities but provides an overall planning framework.

### 46

Education is one of the EIT's major pillars of activity. The EIT takes special care that its education programmes are adequately funded. The provision of guaranteed support funding for each KIC for a significant proportion of the budget reduces uncertainty for multiannual priority activities such as the education programmes.

### 47

The provision of support funding reduces the risk of discontinuity for a large share of the programme.

See Commission and EIT reply to paragraphs 41 and 44.

### 48

The significant support funding element of the EIT funding model provides a certain amount of long-term planning security.

See Commission and EIT reply to paragraphs 41 and 44.

### 49

Due to the annual nature of the EIT's budget, and the fact that the EU budget is generally not adopted before mid December, grant agreements for a given year cannot be signed before 1 January of that particular year. This issue was first addressed by the European Court of Auditors in the specific annual report for the 2011 financial year and the EIT provided its comments. The EIT committed itself to decreasing the gap between the starting date of the action, as defined in the KICs' business plans, and the date of signature of the grant agreements. As a result of this effort, the grant agreements for 2013 and 2014 were signed with the three KICs in February 2013 and 2014, respectively.

The year 2015 was exceptional, as KICs asked for a delay in applying the new FPA in order to further clarify the implications of specific provisions between the EIT, the KICs and the European Commission in the context of the alignment with Horizon 2020 rules. Furthermore, due to the legal consultations needed, the *ex ante* approval of the new grant agreements by the Commission took longer than usual. The EIT expects timely signature of grant agreements from 2016, when the new FPAs will already be in place, i.e. the late signature in 2015 was a one-off event.

### 50

While this was the usual practice until 2015, the KICs could, under certain conditions such as the consumption of the previous pre-financings, and subject to some interim reporting obligations, request additional pre-financing payments.

While the EIT would like to provide pre-financing up to 70 % of the grant awarded in order to help KICs in managing their cash position, it is important to note that the level of pre-financing is subject to availability of payment credits, which is beyond the EIT's control. The pre-financing for the GA 2016 is foreseen to be around 60 %.

The KICs as powerful innovation networks, including strong industrial partners and universities, are in a position to resolve cash flows, for example, via loans taken from a bank, as some KICs have already demonstrated. This allows them to increase pre-financing rates to partners or beneficiaries (e.g. students or start-ups) where the cash flow otherwise creates a problem.

### 51

The EIT Governing Board adopted the EIT monitoring strategy on 3 December 2015, which will measure data for Horizon 2020, for the EIT's impact via its own and KIC activities and for KIC results. Further, the EIT is an active contributor to the Horizon 2020 annual monitoring report for 2014, and will have a section in the report.

### 52

Past changes in the core KPIs were done in order to fine-tune their concept/meaning to ensure a level playing field between the different KICs and to respond to the evolving nature of the KICs. The changes were made after consultation with the KICs in order to address, among others, the differences in the KICs' sectors of operation and wider environments.

The changes in KPIs over time therefore directly address the finding in paragraph 52.

### 53

The EIT performs comprehensive analyses to compare the KICs based on several factors, not simply on the basis of the core KPIs. The implementation of KICs' business plans is assessed both through quantitative performance indicators and through qualitative reviews done by external experts and the EIT's staff. More widely, the EIT also conducts on-site monitoring and topical reviews of the KICs' activities. These tools, taken together, provide a very informative picture of the differences between the KICs.

### 54

The EIT recognises that outcomes and impacts can only be measured with a combination of qualitative and quantitative indicators. This is comprehensively addressed in the EIT monitoring strategy, adopted by the EIT Governing Board in December 2015, and through the ongoing KPI review, as reported in paragraph 102.

### 55

The business community is strongly represented in the governance of KICs, playing a leading role in the formation of the KIC strategies. A non-exhaustive list of representatives of the respective industries in KICs' Governing Boards is as follows:

- EIT Digital: Deutsche Telekom AG, Philips, Nokia, British Telecom, Alcatel-Lucent, Ericsson;
- Climate KIC: Bayer Technology Services GmbH, GDF Suez, South Pole Carbon, Velux A/S;
- KIC InnoEnergy: Total SA, Gas Natural Fenosa, Electricité de France, ABB AB, Areva SA.

### 56

The level of EIT grant funding is not a sufficient measure of the level of involvement in KICs. For example, funding provided to higher education is geared towards supporting more entrepreneurial curricula and students graduating from university, which directly benefits business. A measurement of involvement ought to take into account the number of partners, since it is the direct measure of the attractiveness of a KIC, as well as the nature of activities supported, rather than the type of institution which implements it.

### 57

The EIT and the KICs have been designed to address the EU-wide problem of a low level of university–business cooperation. This is why the business community is strongly represented in the governance of KICs, playing a leading role in the formation of the KIC strategies. It was, nevertheless, to be expected that there would be initial problems in achieving the desired level of university–business cooperation. In order to address this, the EIT has been changing the guidelines for the business plans and providing strategic suggestions to the KICs. The KICs have also been changing their internal rules and procedures as well.

The progress made by the EIT and the KICs in this field shows that the KIC model is the right one for the development of long-term university–research–business cooperation, and we are convinced that, in future, results will continue to improve.

### 58

While the EIT does not have a target for the share of the budget going to SMEs, it does have quantified targets for SME creation. SME start-up companies created by the EIT are one of the EIT's KPIs and are therefore highly incentivised. For 2014, the three first wave KICs reported that 90 new start-ups had been created, all of which are SMEs according to the definition of the Commission recommendation (C(2003) 1422). Furthermore, many other existing small enterprises were supported by sub-grants or through the provision of services in the KICs' accelerators.

## Reply of the Commission

### 59

The EIT has achieved exceptional results in promoting and supporting SMEs' participation in innovation activities.

Many EIT activities specifically target SMEs. As a financial incentive for SMEs, the EIT even had a specific derogation from the EU financial regulation in the 2010-2013 period that allowed SMEs, as KIC partners, to claim 40% indirect costs on top of their direct costs, as opposed to the 20% allowed for non-SME companies.

As regards targeted support for existing SMEs, the KIC partnerships provide a strong ecosystem in which they can receive support. Existing SMEs with exceptional innovation potential would therefore be ideally placed to join a KIC partnership and take full advantage of the support offered by the EIT. As a result, an increasing number of SMEs participate both as partners in KICs and as beneficiaries of KIC sub-grants and recipients of business creation and acceleration services.

### 60

As KICs are aiming to become financially sustainable and are able to use financial instruments (e.g. bank loans) and sources of income other than EIT funding, they are able to ensure that payments to SMEs are made in a timely manner regardless of when EIT funding is received. The EIT is not in a position to impose payment conditions on KICs with respect to the contractual relations which they have with partners as the KICs are autonomous in this respect. However, as support payments to SMEs are limited in size compared to the programme as a whole, KICs have the possibility to increase the advance payments to SMEs through adequate cash flow management (Commission and EIT replies to paragraphs 41 and 44 provide further examples of the flexibility of KIC funding).

### 61

The EIT systematically gathers information on the status of new KIC partners upon their joining the KICs. Therefore, the EIT has up-to-date information on the number of KIC partners that are SMEs.

Furthermore, larger organisations are in the majority in the first years of a KIC's life, as they have the capacity to prepare a solid strategic agenda and a winning proposal to be selected as a KIC in the first place. SMEs typically join the KICs at a later stage when their participation can add value to the activities of the established partnerships.

As an example, KIC InnoEnergy had 25 SMEs as KIC partners in the 2010-2013 period. However, 55 and 50 new SMEs joined KIC InnoEnergy in 2014 and 2015 respectively, thereby increasing the number of SME partners to 130.

Many SMEs participate in the EIT-KIC programme, and are final recipients of EIT grants, by way of sub-contracting or sub-granting arrangements with other KIC partners such as universities, research centres or industrial companies. The acceleration and incubation programmes of KICs particularly target start-up SMEs and the EIT has a KPI that tracks the establishment of new SMEs. The growing number of SMEs in the KIC partnerships, as well as through EIT grants, will naturally lead to a higher share of grant absorbed by SMEs as well.

### 62

The EIT is actively supporting SMEs. Clear objectives for the creation of start-ups exist, and it is one of the EIT's core key performance indicators.

See Commission and EIT reply to paragraph 57.

### 64

The promotion of synergies and complementarities with other EU initiatives is a priority for the EIT and for DG Education and Culture. The aim is embedded in the EIT's strategic innovation agenda and regulation.

Synergies and complementarities are facilitated by DG Education and Culture and the EIT (e.g. annual meeting with Commission services, EIT and KICs, as well as selection criteria for new KICs) and are built into the KIC model, elements of which reflect objectives and lessons learned from other EU programmes (e.g. the knowledge triangle concept echoes aspects of Erasmus+ and the university–business dialogue; the co-location centre concept echoes EU regional policy; the societal challenges approach is shared across Horizon 2020; the EIT funding model builds on lessons learned across other programmes). There are concrete examples of synergies within the thematic areas of the KICs such as EIT Digital: Future Internet and Big Data PPPs; KIC InnoEnergy: SET Plan; and Climate-KIC: cooperation with DG Climate Action in the preparation of the United Nations Climate Change Conference in Paris in December 2015.

The EIT continues to foster synergies at the level of concrete projects, more recently in the context of the European Fund for Strategic Investments (EFSI), with European Cooperation in Science and Technology (COST) and the European Space Agency (ESA).

### 69

The EIT has already requested to launch the process to reach the full financial autonomy. This process is expected to be finished before the end of 2016.

### 71

In addition to ensuring compliance with the rules, the EIT also increasingly rewards performance and incentivises impact. For example, poor performance will have an increasingly negative effect on a KIC's budget. As part of the principles for the KICs' financial sustainability, the KICs' EIT budget will have an increasing share of competitive funding. As this share — which rewards performance — increases over time, a KIC with poor performance will have an ever stronger financial incentive to improve.

### 72

The EIT reinforced, in 2015, the direct impact of low performance on the amounts to be paid — parts of a KIC's expenditure claim will not be accepted by the EIT when the implementation of the activity was insufficient. See Commission and EIT reply to paragraph VII of the executive summary.

Following the Court's intervention, the EIT has continued to strengthen its verification of costs in the annual audit reports. EIT is strongly rewarding performance while at the same time ensuring a high level of assurance for the eligibility of costs incurred.

## Reply of the Commission

### 74

The EIT and the Commission consider the threshold according to Article 34 of the Horizon 2020 rules for participation as appropriate for EIT grants paid to KICs. We consider it proportionate to require an audit certificate from a beneficiary of EU/EIT funds who claims an annual grant in excess of 325 000 euro. In any case, the EIT would need a specific derogation from Article 34 of the Horizon 2020 rules for participation in order to use a different or higher threshold than 325 000 euro for grants claimed by participants.

See also Commission and EIT replies to paragraphs 79 and 80.

### 76

It is important to note that the 'financial reports' are not EIT-specific any more, as the cost reports have been fully aligned with the Horizon 2020 templates starting from the 2016 grant agreements.

### 79 Second indent

This recommendation would require a specific derogation from the Horizon 2020 rules for participation and the financial regulation<sup>3</sup>.

### 79 Third indent

This recommendation is beyond the control of the EIT, as it would require a specific derogation from the Horizon 2020 rules for participation and the financial regulation<sup>4</sup>.

### 81

Outsourcing the technical assessment of projects is a common practice in R & D programmes. This happens in particular in the case of very complex projects covering, and integrating, several domains of activity, like education, innovations and business.

### 83

It is important to note that the EIT has improved the trend of staff turnover since 2013. The low country coefficient for Hungary (currently 69 %) is a significant factor contributing to staff turnover. However, this is beyond the EIT's control.

### 84

In the meantime, significant improvements in the EIT's management capacity took place. The vacant Head of Unit post has been filled and the selection of the other Head of Unit is ongoing. Furthermore, the selection of the EIT Director is also ongoing.

---

3 [https://myintracomm.ec.europa.eu/budgweb/EN/leg/finreg/Pages/leg-020-08\\_finreg2012.aspx#fr135](https://myintracomm.ec.europa.eu/budgweb/EN/leg/finreg/Pages/leg-020-08_finreg2012.aspx#fr135)

4 [https://myintracomm.ec.europa.eu/budgweb/EN/leg/finreg/Pages/leg-020-08\\_finreg2012.aspx#fr135](https://myintracomm.ec.europa.eu/budgweb/EN/leg/finreg/Pages/leg-020-08_finreg2012.aspx#fr135)

### 86

The EIT's focus on excellence makes it natural that Member States with higher innovation capacity are more strongly represented in KICs. While it is a clear goal for the EIT to strengthen existing capabilities and centres of excellence in the EU, the EIT also ensures that it delivers benefits to areas of the EU not directly participating in KICs by way of the EIT RIS.

### Box 11 — Concerns over the concentration of EIT financial support and the lack of transparency

There is a reasonable balance between the sides of the knowledge triangle, in the distribution of both partners and funding. Clear procedures exist for the selection of projects by KICs, which ensure quality control and transparency.

### 89

Evidence of the EIT's results is beginning to emerge. The EIT has produced over 1 000 entrepreneurial graduates, numerous start-ups, a series of success stories and a strong pan-EU network of co-location centres and business accelerators and has promoted an entrepreneurial culture.

### 92

The business creation review completed in November 2015 provides strong evidence of the added value provided by EIT/KIC accelerator programmes, and term sheets exist for supported ventures which demonstrate significant results from EIT support into business creation.

### 93

The KPIs show that significant outputs have been provided, many of which have by now translated into tangible results (see the examples mentioned in paragraph 90).

### 94

It is worth highlighting that non-EU students also integrate into EU companies or to start their own ventures after finishing their studies, thus creating an impact on and added value for our society. The EIT's KICs have created an environment where the gap between academia and business has narrowed, and therefore such students already have a clearer path towards working for a KIC business partner following their studies and thus staying in the EU.

### 98

In line with Article 6(2)(e) of the EIT's founding regulation, all three first-wave KICs have established strategies for financial sustainability. A summary of these strategies has been presented in the KIC business plans since 2014. For the 2016 business plan, an EIT expert focused specifically on financial sustainability issues and assessed the plans for each KIC.

### 103

The new framework partnership agreements are under signature at the beginning of 2016.

## Conclusions and recommendations

### Recommendation 1

The Commission and the EIT accept the recommendation.

Any proposal for amendments to legal regulations will have to be prepared in accordance with the better regulation principles, in particular the principle to 'evaluate first'. The EIT's legal basis requires the Commission to evaluate the EIT by the end of 2017 and an evaluation is currently being prepared with the participation of all relevant Commission services.

The evaluation will take into consideration also the critical opinion of the audit and the independent evaluators will have access to this audit. Based on the evaluation results, any future steps will be decided in compliance with the better regulation principles.

The Commission will take a position on the change of the EIT's legal basis on the basis of the findings of the independent expert evaluation and on the outcome of this audit.

### 107

See Commission and EIT replies to paragraphs 40 to 49 and 60, summarising their position on these issues.

### Recommendation 2 (a)

The Commission and the EIT partially accept the recommendation and will explore to what extent it is possible to further extend multiannuality.

### Recommendation 2 (b)

The Commission and the EIT accept the recommendation.

For (a): complete review by spring 2017, and implementation (conditional on that review) by 2018.

### 108

See Commission and EIT replies to these paragraphs, summarising their position on these issues.

### Recommendation 3

The EIT and Commission accept this recommendation.

### 109

See Commission and EIT replies to these paragraphs, summarising their position on these issues.

### Recommendation 4

The Commission and the EIT accept the recommendation.

The EIT will continue to develop focus on impact as already launched during 2015.

## HOW TO OBTAIN EU PUBLICATIONS

### Free publications:

- one copy:  
via EU Bookshop (<http://bookshop.europa.eu>);
- more than one copy or posters/maps:  
from the European Union's representations ([http://ec.europa.eu/represent\\_en.htm](http://ec.europa.eu/represent_en.htm));  
from the delegations in non-EU countries ([http://eeas.europa.eu/delegations/index\\_en.htm](http://eeas.europa.eu/delegations/index_en.htm));  
by contacting the Europe Direct service ([http://europa.eu/eurodirect/index\\_en.htm](http://europa.eu/eurodirect/index_en.htm)) or  
calling 00 800 6 7 8 9 10 11 (freephone number from anywhere in the EU) (\*).

(\* The information given is free, as are most calls (though some operators, phone boxes or hotels may charge you).

### Priced publications:

- via EU Bookshop (<http://bookshop.europa.eu>).

The European Institute of Innovation and Technology (EIT) has the ambitious objective of strengthening the links between education, science and business, and thus being a driver of innovation in the EU. We conclude that, despite a valid *raison d'être*, the EIT's complex operational framework and management problems have impeded its overall effectiveness. We identified several weaknesses in the EIT's funding model, the reporting arrangements between the EIT and the knowledge and innovation communities and the financial sustainability of the latter. Seven years after its inception, the EIT is not yet fully operationally independent from the European Commission. This has hampered its decision-making. We conclude that if the EIT wants to become the ground-breaking innovative institute it was originally conceived to be, legislative and operational adjustments are required to better foster the EU's innovation potential.



EUROPEAN  
COURT  
OF AUDITORS



Publications Office