3rd MEETING of the High Level Expert Group on Monitoring Simplification for Beneficiaries of ESI Funds

Financial Instruments

- 1. The members of the High Level Group noted the political significance of facilitating further the use of financial instruments but the lengthy processes for the Managing Authorities to set up the instruments as well as the administrative processes for the final recipients reduced the incentive to use them. For the final recipient, the process for accessing the financial instrument should be simpler than receiving a grant.
- 2. For the 2014-2020 programming period they recommend the establishment of a working group of practitioners as soon as possible to review and consider concrete issues related to financial instruments as well as specific seminars for auditors to improve their understanding and awareness of financial instruments before the first audits for the period would be carried out.
- 3. The members recommended further capacity building on the use of financial instruments in 2014-2020 and more harmonisation of the rules between ESI Funds and other EU funds for the post 2020 period.

Interim Report on Access to Financial Instruments

from the High Level Expert Group on Monitoring Simplification for Beneficiaries of ESI Funds

Financial instruments represent a resource-efficient way of deploying cohesion policy resources in pursuit of the Europe 2020 Strategy objectives. Targeting projects with potential financial viability, financial instruments provide support for investments by way of loans, guarantees, equity and other risk-bearing mechanisms.

Conclusions:

- The members of the High Level Group noted the increased focus on using financial instruments in the 2014-20 period and the opportunities these instruments could bring to leverage in additional resources to help support the achievement of the investment goals of the ESI Funds. They also acknowledged the political significance of facilitating further the use of financial instruments in the context of complementarity with the European Fund for Strategic Investments (EFSI) and other financial sources.
- However, from the evidence presented during the meeting, they noted the following challenges relating to financial instruments:
 - Setting up the financial instruments involved lengthy processes for the Managing Authorities including an intensive ex-ante assessment.
 - The guidance provided from the Commission on the subject is extensive but often interprets the regulations in a different way than had been understood by Member States, some of which created more difficulties and questions than they answered. EU level "gold-plating" for financial instruments should be avoided to not increase the weight of obligations already incumbent on the private managers of funds, but also to avoid additional administrative demands on the enterprises supported by the financial instruments.
 - There was little sense of proportionality in the requirements for financial instruments according to their size, and therefore little incentive to use them for smaller scale instruments.
 - The rules established for the financial instruments do not take into account the fact, that each type of financial product has its own specific character and therefore some rules applicable to one type of a product may not apply to another one (e.g. what is applicable to loans may not be applicable to guarantees).
 - In many cases an overlap between similar financial products implemented by different financial institutions (established at both EU and national level) can be observed; introduction of these new products diminishes the performance of the existing ones, but also leaves need for financing in other areas unmet.
 - While the widening of the scope of the instruments was welcomed, as well as more legal certainty through the expanded provisions in the CPR, there is less flexibility as a result.

- Contrary to expectations, adding new funds into existing instruments set up in previous periods created a considerable number of complications from questions of how to ring fence resources to issues around the selection of fund managers.
- The burden on the final recipient of the loan is perceived in some Member States as more or less the same as the burden on the beneficiary of a grant in terms of the information required to access the loan and the monitoring of the investment. However, this was not commensurate with arrangements for final recipients of other financial products from commercial sources.
- The members of the High Level Group concluded that the Commission should ensure that the following key principles are taken into consideration for financial instruments:
 - The setting up of a financial instrument for a managing authority should be at least as straight forward as providing support by grant similarly with a combination of financial instruments and grants.
 - Any decision to set up a financial instrument should be preceded by the analysis of existing instruments in the region / instruments aimed at supporting the same categories of recipients to promote complementarity of support instead of allowing for overlapping between similar financial products.
 - For the final recipient, the process for accessing the financial instrument should be simpler than receiving a grant, especially for SMEs, and similar to the requirements for other types of financial products from public and private sources otherwise there will not be an incentive for final recipients to apply for and use financial instruments.
 - New requirements should not be imposed without taking into account the differentiation of particular forms of financial products and the fact, that certain provisions applicable to one product may not be applicable to other ones.
 - Certain privileges that seemed to be offered to the EIB in terms of entrustment of implementation tasks or application of state aid rules should also be offered to Member States or national banks or other public institutions when managing ESI Funds.
 - A specific problem in one Member State should not be addressed by guidance at the EU level. Specific problems should be dealt with on a bilateral basis between the Commission and Member state with feedback in a timely manner.
 - All stakeholders need a reliable legal and regulatory setup to assess and carry out innovative investments. Therefore, once funding agreements are signed, all partners must be able to rely on this agreement so that subsequent legislative changes or guideline interpretations are not to their detriment.

Recommendations to the Commission for the 2014-20 period:

The members of the High Level Group felt there was still a need for greater understanding and awareness from those looking at compliance and audit of the differences between grants and financial instruments. Regular, specific seminars for auditors were recommended to address this issue and improve the awareness in 2014-20 before first audits would be carried out.

A working group of practitioners, including key types of beneficiaries, should be established as soon as possible to review and consider concrete issues related to financial instruments including:

- The requirements for final recipients (documents required, periods for retention of the documents, etc.) to align them as far as possible with market practice.
- The possibility to reduce requirements for smaller instruments or pilots to encourage more use among those managing authorities with limited experience of financial instruments.
- Certain privileges that seemed to be offered to the EIB in terms of entrustment of implementation tasks or application of state aid rules should also be offered to Member States or national banks or other public institutions when managing ESI Funds.
- Alignment of audit and reporting obligations under ESIF and under National and European Banking and Capital Markets Law.
- Rules amongst ESI Funds and between ESI Funds and other sources of EU support such as Horizon 2020 and EFSI, should be further harmonised.
- The impact of the clause on repaying in case of irregularity.
- Public procurement and State Aid rules.
- The strict application of the requirements of Article 38 CPR: selection of financial intermediaries via an open procedure (call for expression of interest), transparent (publication in the UEOJ), non-discriminatory (with objective selection criteria published and a more proactive application of provisions of Article 38.4(b) CPR.
- Follow-up investments in firms that have become a firm in difficulty only after the first ESIF-investment should be permitted if all other private investors are equally willing to invest further.
- Payouts to private investors within the funding period irrespective of whether the financial instrument is classified as State Aid or not.

The proposals prepared by this group should be taken into account in the process of the MFF review in 2016 where the issue of simplification of the EU rules will be one of the key areas considered for the legislative changes.

To facilitate and accelerate implementation of financial instruments, Member states and the Commission should take the advantage of CPR and CDR 480/2014 provisions as regards the selection of bodies implementing financial instruments and select them through open, transparent, proportionate and non-discriminatory procedures, preventing conflicts of interest. Public procurement should not be the primary procedure for selection of such bodies.

Suggestions for further reflection for post 2020:

The High Level Group recommends that the Commission base their review of the legal framework for financial instruments on the key principles identified and in addition it underlines that:

- Capacity building in the area of financial instruments developed throughout the period of 2014-20 will facilitate and improve the use of financial instruments post 2020.
- Rules between ESI Funds and other EU funds should be further harmonised and the possibility of own contribution by the final recipient should be explored.
- A legal framework common to ESIF and state aid regulation covering both regulations would provide a uniform set of common rules and simplify the creation of financial instruments.
- A differentiated and streamlined legal framework for micro-credit, social economy, as well as very small businesses and micro-enterprises should be provided.