

FICHE NO 10

FINANCIAL INSTRUMENTS – DELEGATED ACTS

VERSION 1 - 03 JUNE 2013

Regulation	Article
Common Provisions Regulation (CPR)	<ul style="list-style-type: none">• 32(10): Delegated act laying down additional specific rules on purchase of land and on combination of technical assistance with financial instruments.• 33(4): Delegated act laying down additional specific rules on the role, liabilities and responsibility of the entities to which implementation tasks are entrusted and related selection criteria.• 34(5): Delegated act concerning controls to be performed by managing and audit authorities, arrangements for keeping supporting documents, elements to be evidenced by supporting documents, and management and control and audit arrangements concerning financial instruments implemented by the bodies and institutions mentioned in Article 33 (4)(b) taking into account the specificities, objectives and characteristics of financial instruments relative to other forms of support.• 36(4): Delegated act concerning the establishment of a system of capitalisation of annual instalments for interest rate subsidies and guarantee fee subsidies.

This document is provisional, without prejudice to the on-going negotiations in the Trilogues between the European Parliament and the Council (in line with the principle that "nothing is agreed until everything is agreed"). This document is a draft that shall be adjusted following the expert meeting.

It does not prejudice the final nature of the basic act, nor the content of any delegated or implementing act that may be prepared by the Commission

1. Empowerment

- Article 32(10) of the CPR sets out that:

"The Commission shall be empowered to adopt delegated acts in accordance with Article 142 laying down additional specific rules on purchase of land and on combination of technical assistance with financial instruments."

- Article 33(4) of the CPR sets out that:

"The Commission shall be empowered to adopt delegated acts in accordance with Article 142 laying down additional specific rules on the role, liabilities and responsibility of the entities to which the implementation tasks are entrusted and related selection criteria. The Commission shall notify the delegated acts, adopted in accordance with Article 142, simultaneously to the European Parliament and the Council within four months of the adoption of this Regulation."

- Article 34(5) of the CPR sets out that:

"The Commission shall be empowered to adopt delegated acts in accordance with Article 142 concerning controls to be performed by managing and audit authorities, arrangements for keeping supporting documents, elements to be evidenced by supporting documents, and management and control and audit arrangements concerning financial instruments implemented by the bodies and institutions mentioned in Article 33(4)(b) taking into account the specificities, objectives and characteristics of financial instruments relative to other forms of support. The Commission shall notify the delegated acts, adopted in accordance with Article 142, simultaneously to the European Parliament and the Council within four months of the adoption of this Regulation."

- Article 36(4) of the CPR sets out that:

"The Commission shall be empowered to adopt delegated acts in accordance with Article 142 concerning the establishment of a system of capitalisation of annual instalments for interest rate subsidies and guarantee fee subsidies. The Commission shall notify the delegated acts, adopted in accordance with Article 142, simultaneously to the European Parliament and the Council within four months of the adoption of this Regulation."

This document is based on the most recent Presidency compromise text, and is a provisional text, without prejudice to the on-going negotiations (in line with the principle that "nothing is agreed until everything is agreed").

2. Main objectives and scope of the Delegated act

The delegated act is to provide non-essential supplementary elements that will ensure (i) a coherent framework for all stages of financial instruments implementation and (ii) continuity of guidance previously provided by the Commission. The delegated act reflects the principles agreed by the Coordination Committee of the Funds (COCOF) for the programming period 2007-2013 and established in the most recent COCOF Guidance Note on Financial Engineering Instruments (COCOF 10-0014-04) (hereinafter referred to as the 'COCOF

Guidance Note'). It also takes into consideration a set of recommendations made by the European Court of Auditors¹, as well as the principles contained in the Financial Regulation.

3. Main elements of the Delegated act and key changes compared to the period 2007-2013

In line with the empowerments contained in the CPR, the delegated act will include the following elements: **Purchase of land (empowerment under Art 32(10) CPR)**

Article 32 of the CPR includes general rules on eligibility in relation to financial instruments. However, in line with the latest COCOF Guidance Note, supplementary elements are required to provide further clarity concerning eligibility rules and the applicability of CPR definitions in relation to sustainable urban development.

In line with the empowerment under Article 32(10), the following elements will be covered:

- Financial instruments financed by the ERDF, the Cohesion Fund and the EAFRD can support investments that include the purchase of land not built on and land built on for an amount of up to 10% of the total eligible expenditure incurred by the financial instrument for individual support provided to final recipients.
- However, where financial instruments are dedicated to provide support to final recipients in the area of sustainable urban development, this 10% limit will apply at the level of the final beneficiary, and not at the level of the individual final recipient of support. This way, the 10% limit can be exceeded in a single investment, provided the 10% threshold is respected at the level of the financial instrument overall.

3.2. Combination of technical support with financial instruments (empowerment under Article 32(10) CPR)

Compared with the current programming period, the CPR will enable a better combination of financial instruments with other forms of support and with technical support. Article 32(5) CPR provides that financial instruments may be combined with grants, interest rate subsidies and guarantee fee subsidies. Compared to 2007-2013 Regulations, additional detailed elements will be needed to enable appropriate practices when it comes to the combination of grants for technical support and a financial instrument in a single operation.

In line with the empowerment under Article 32(10), the following element would be covered:

- Grants for technical support, which are combined with a financial instrument in a single operation, should be provided only for the preparation of the prospective investment, i.e. for the benefit of the final recipient to be supported from this operation.

3.3. Selection of bodies implementing financial instruments (empowerment under Article 33(4) CPR)

¹ European Court of Auditors, Opinion 7/2011.

Article 33 of the CPR offers a wide range of options to managing authorities when further entrusting the implementation of financial instruments. In this context, additional specific rules and basic parameters are required to guide managing authorities when selecting bodies implementing financial instruments. These rules should build on previous COCOF guidance, principles reflected in the Financial Regulation and best practice in implementing financial instruments at both EU or national/regional level.

In line with the empowerment under Article 33(4), the following element would be covered:

- Selection criteria: *Before selecting bodies implementing financial instruments (including funds of funds)*, the managing authority should obtain evidence that the entity in question is entitled to carry out relevant implementation tasks under EU and national law. Moreover, it should be verified that the entity in question is economically and financially viable and that it has the adequate capacity, organisational structure and governance framework to implement the financial instrument. Entities to which implementation tasks are entrusted need to demonstrate that effective and efficient internal control and accounting systems are in place and they need to agree to being audited by Member states audit authorities, the Commission and the European Court of Auditors.
- For all implementation options under Article 33(4)(a) and (b) of the CPR, managing authorities need to carefully assess the nature of the financial instrument to be implemented as well as the track record and the operational and financial capacity of the potential bodies implementing the financial instrument (including funds of funds). Their choice has to be transparent, justified and on objective grounds, and it should not give rise to conflict of interest.
- *When selecting bodies implementing financial instruments (including funds of funds)* under Article 33(4)(a) and (b) of the CPR, managing authorities should take into account the following criteria:
 - prior experience with the implementation of similar financial instruments, including, where applicable, the expertise and experience of proposed team members;
 - a robust and credible methodology for identifying and appraising financial intermediaries or final recipients as applicable;
 - the level of management costs and fees for the implementation of the financial instrument and the methodology proposed for their calculation;
 - where applicable, terms and conditions applied in relation to support provided to final recipients, including pricing;
 - the ability to raise resources for investments in final recipients additional to programme contributions;
 - for existing financial instruments, the ability to demonstrate additional activity through the financial instrument in comparison to the present activity and overall strategy in the sector; and
 - in cases where bodies implementing the financial instrument allocate own financial resources to this financial instrument or share the risk, proposed measures to mitigate a possible conflict of interest.

Where financial instruments are implemented in accordance with the provisions of Article 33(4)(b)(i) of the CPR, managing authorities can give a mandate to the EIB through a direct

award of contract. In this case, the above selection and award criteria are not applicable (e.g. pricing) or are considered to be met as the case may be. The body that implements the fund of funds, including the EIB where applicable, shall apply the above conditions when further entrusting part of the implementation to bodies implementing financial instruments.

3.4. Role, liabilities and responsibility of bodies implementing financial instruments (empowerment under Article 33(4) CPR)

Article 33(4) CPR stipulates that additional specific rules are necessary concerning the responsibility of bodies implementing financial instruments, when they receive EU budget resources for investment in final recipients. It is necessary to ensure that these selected bodies (including bodies implementing funds of funds) manage ESI resources with the appropriate degree of integrity and professionalism, and that basic principles (such as sound financial management) as well as EU and national rules are adhered to during the full implementation cycle of the instruments, including the delivery of its financial products. The proposed provisions would primarily reflect the principles laid down in the most recent COCOF guidance as well as good practice from EU central level instruments implemented under the Financial Regulation.

In line with the empowerment under Article 33(4), the following elements would be covered:

Bodies implementing financial instruments (including funds of funds) need to

- comply with applicable Union and national law (e.g. rules covering the ESI Funds, state aid, public procurement) and relevant standards and/or legislation on the prevention of money laundering and finance of terrorism. They should act with the diligence of a professional manager and in good faith;
- ensure that the choice of final recipients receiving support from financial instruments is transparent, justified on objective grounds and taking into account the potential economic viability of the final recipient (or project); and may not give rise to a conflict of interest.
- ensure that those taking part in an operation receiving contributions from programmes and final recipients have been informed of that funding in accordance with the information and publicity requirements laid down in the CPR and the Fund-specific regulations;
- provide support from financial instruments to final recipients in a proportionate and least distortive manner. In this regard, preferential treatment of private investors needs to be limited to the minimum necessary to generate expected market returns for private investors;
- for guarantee products, establish an appropriate multiplier ratio by way of prudent *ex-ante risk assessment for guarantees* [in addition to the financial instrument-specific ex-ante assessment under Article 32(2) of the CPR] between the amounts established to cover expected and unexpected losses from loans or other risk-sharing instruments and the corresponding new loans or other risk-sharing instruments issued and disbursed which are covered by these guarantees.

The programme contribution committed to honour guarantees should reflect such an ex-ante risk assessment. During the programming period, the ex-ante risk assessment can be reviewed provided this is justified by subsequent market conditions.

If the bodies implementing the financial instrument or the entities benefitting from the guarantees have not at least issued and disbursed the planned amount of new loans or other

risk-sharing instruments to final recipients that would justify the full use of the guarantees, the eligible expenditure should be reduced by taking into account the proportion between planned and effectively disbursed loans or support that is provided by other risk-sharing instruments.

The bodies implementing financial instruments need to ensure that no claims can be made on ESI Funds beyond the amounts committed to the financial instrument. Direct financial liability of the managing authority towards bodies implementing financial instruments or final recipients as well as any other debt or obligation of the financial instrument should not exceed the amounts committed to the financial instrument in accordance with the relevant funding agreements.

Notwithstanding the responsibilities of Member States, in case of irregularities, the managing authority, the bodies implementing financial instruments, including bodies that implement fund of funds where applicable, or the final recipient responsible for causing the irregularity will be liable for reimbursement to the programme, for the part of the programme contribution affected by such irregularities, and in addition any gains resulting from this programme contribution.

3.5. Controls to be performed by managing and audit authorities, arrangements for keeping supporting documents, elements to be evidenced by supporting documents, and management and control and audit arrangements concerning financial instruments implemented by the bodies and institutions mentioned in Article 33(4)(b) taking into account the specificities, objectives and characteristics of financial instruments relative to other forms of support. (empowerment under Art 34(5) CPR)

The implementation of financial instruments involves new procedures and actors in delivering ESI Funds support on the ground. Article 34(5) CPR provides that specific arrangements on management and control provisions should be laid down. These rules take into consideration both the COCOF Guidance Note (in particular sections 6 and 7) as well as the recently presented audit methodology for financial engineering instruments under the Structural Funds in the current programming period².

In line with the empowerment under Article 34(5), the following elements would be covered:

- Managing authorities should ensure that financial instruments operations comply with applicable Union and national law as well as the provisions of the relevant programmes and funding agreements.
- Eligible expenditure should be evidenced by adequate supporting documents, to be kept at the appropriate level of the operation until three years after closure (a non-exhaustive list of appropriate supporting documents will be proposed); supporting documents should be available to allow verification of the legality and regularity of the expenditure declared to the Commission.
- Management verifications should be carried out throughout the programming period.

² DG Regional Policy, Common Audit Framework - Financial engineering instruments in the context of Structural Funds, 31 July 2011.

- An adequate audit trail should be established for reporting and audit purposes; for Funds other than EAFRD, audits could be conducted at the level of the final recipients when the supporting documents are not available at the level of the financial instrument or at the level of the managing authority or in case of insufficient monitoring and verifications, or of legitimate doubt that the documents do not reflect the reality of the support provided through financial instruments; financial instruments should be audited throughout the programming period until closure; the audit rights of the ECA and OLAF would not be constrained.
- For financial instruments implemented by the EIB and receiving support under the ERDF, ESF and CF, the managing authority should mandate a firm operating under a common framework contract as established by the Commission to carry out on-the-spot verifications or audits on the operation or the management and control systems relating to those instruments. The audit authority could draw up its audit opinion on the basis of the information provided by this firm.
- For financial instruments supported by the EAFRD in accordance with Article 33(1)(b) of the CPR, specific control obligations, including additional supporting documents to those already defined in this delegated act, are set out in the applicable delegated and implementing act on control of the EAFRD.

3.6. Capitalisation of annual instalments for interest rate subsidies and guarantee fee subsidies (empowerment under Art 36(4) CPR)

The CPR introduces new categories of eligible expenditure that allow for a more effective functioning of financial instruments and specific products beyond the end of the eligibility period. Article 36(1)(c) provides for the eligibility of capitalised interest rate subsidies or guarantee fee subsidies. To ensure a consistent calculation of such capitalised subsidies, detailed rules should be adopted.

In line with the empowerment under Article 36(4), the following elements would be covered:

- Calculation at the end of the eligibility period for the purpose of the payment of the final balance as the total of discounted payment obligations for the purposes and periods laid down in the CPR, based on the outstanding portfolio under management.
- Transfer of the total amount to an escrow account from which they can be drawn down only as required; and
- Any residual resources left in this escrow account after the maximum period referred to under Article 36(1)(c) of the CPR, or as a result of unexpected winding-up of the instrument before the end of this maximum period, should be used in accordance with the legacy provisions of Article 39 of the CPR.