Mid-term review

Cohesion Policy funds

Brussels, March 2024

Executive Summary

The Cohesion Policy Funds are an appropriate promotional instrument to increase competitiveness and reducing the gaps in notably economic development between different regions. ELTI members are long-standing Implementing Partners. We would like to share the following observations and recommendations:

- Regarding the simplification in the new CPR 2021-2027 the European Commission achieved significant progress. It is essential that new provisions are implemented and maintained, if not extended in some cases, in future CPR.
- The option given to managing authorities to directly award a contract for the implementation of a financial instrument to a publicly owned promotional institution would facilitate the implementation.
- The audit trail needs to be simplified.
- Continued support for working capital requirements and business capital expenditure is needed.
- Management Fees needs to be adequate.

For an even more efficient implementation of financial instruments the following recommendations should be considered:

- Harmonise the rules and thresholds applicable to environmental requirements across EU programmes. Private Investors and final beneficiaries just don't accept this diversity.
- Enable effective and straightforward ex-ante assessments,
- Clarify the verifications and audits on guarantee instruments,
- Relax the rules around the responsibility of beneficiaries.

Along with the CAP, Cohesion Policy Funds represent one of the EU's largest budgets by volume. They are crucial to increasing competitiveness and reducing the gaps in development between different regions. Some progress was achieved in respect of the new regulation laying down common provisions for the Cohesion Policy Funds, the Common Provisions Regulation (CPR) 2021-2027[1]. It is advisable to step up simplification of the legal basis, while simultaneously making the provisions clearer to remove any legal uncertainty in relation to the management of the Cohesion Policy Funds.

[1] EUR-Lex - 32021R1060 - EN - EUR-Lex (europa.eu)

Financial instruments in particular are playing an expanding role in EU regional policy. These are "repayable" financing methods – such as loans, guarantees or equity – that finance close-to-market, revenue-generating investments, and supplement the subsidies on offer. They serve to ensure the long-term future of resources and help attract private sources to jointly finance riskier projects. They also simplify the disbursement of funds, given how they are managed.

Considering the repayable nature of these financial instruments, they should be managed flexibly and proportionately a key prerequisite for leveraging private-sector co-investors, facilitating synergies with other domestic or EU financing programmes, and embedding them into national promotional institutions' mechanisms in the long term. This is also necessary to allow Cohesion Policy Funds to play a counter-cyclical role if an economic crisis occurs, as seen with the impact of the Covid-19 pandemic.

National Promotional Banks and Institutions (NPBIs) are reliable Financing Partners for the European Commission for many years. They are implementing Cohesion Policy Funds for many years and they offer their proximity to public and private players at national, regional and sub-regional level, their understanding of specific regional needs, their financial and technical expertise and their financial intervention capacity.

The need for more simplification is not exclusive to financial instruments, and it should also be an objective for subsidies, which at this time remain the leading way in which Cohesion Policy Funds are allocated. Private Investors and final beneficiaries increasingly refrain from using EU promotional Instruments due to the extensive rules regarding reporting, eligibility criteria, sustainability or information needs. ELTI commented on this topic in a separate contribution[2].

I. Main progress points in the Cohesion Policy Funds regulation (CPR 2021-2027)

Regarding the simplification in the new CPR 2021-2027 the European Commission achieved significant progress. It is essential that new provisions are implemented and maintained, if not extended in some cases, in future CPR (for more details see also annex 1).

1. **The option given to managing authorities to directly award a contract** for the implementation of a financial instrument **to a publicly owned promotional institution (Article 59.3.c)**

NPBIs are acting under a public policy mandate given by a Member State or regional authority that includes carrying out economic development activities contributing to the objectives of Cohesion Policy Funds. They are consequently playing a vital role in deploying the Cohesion Policy Funds at the local level. Direct selection of this kind therefore simplifies and accelerates grass-roots funds allocation, but it is currently limited to financial instruments and could usefully be expanded to financing in the form of subsidies.

[2] https://www.eltia.eu/images/2023.12.01_-_Reduction_of_information_requirements_under_EU_legislation_-_Have_your_say_procedure_-_ELTI.pdf

2. Simplification of the audit trail for financial instruments (Annex XIII.II.10)

The CPR 2021-2027 stipulates that evidence of the use of funds for their intended purpose is provided *ex-ante* (and no longer *ex-post*), meaning before granting the financing. This approach aligns the audit rules for the Cohesion Policy Funds, with those used for centrally-managed financial instruments (InvestEU, EIB and EIF financial instruments) and makes them more in line with market practices. Prior checks make it possible to confirm the project or business meets the eligibility criteria, and are based on regulatory documents (e.g., a company's articles, financial documents), commitments from the business owner and examination of the business plan.

3. Continued support for working capital requirements and business capital expenditure with the Cohesion Policy Funds (Article 58.2)[3]

Provision of financing to businesses is now the top "sector" by volume for implementation of financial instruments under the cohesion policy. It is therefore essential that the Cohesion Policy Funds are able to fund all of their financing needs, which can be highly changeable: SMEs have ongoing working capital requirements that are intensified in times of crisis, as it was shown by Covid-19 and the EU's successful response to it with the CRII and CRII+ regulations[4], SMEs' tangible and intangible capital expenditure, business transfer (including change of ownership within a family, which still engenders a need for transfer financing).

Small mid-caps (businesses with between 200 and 500 employees) in the regions continue to have specific financing requirements. The current ERDF regulations limit support for small mid-caps to financing for research, development, and innovation. The provision could be broadened to financing expenditure on tangible and intangible assets and their WCR if an *ex-ante* examination by the managing authorities shows a sub-optimal investment situation.

4. Ensure the caps for management costs and fees do actually cover the costs related to financial instruments (Article 68.4)

The rules relating to management costs and fees have been simplified and adapted for the 2021-2027 programme.
The European Commission's original proposal was aimed at reducing management costs and fees to 5% for all types of financial instruments regardless, drastically reducing, sometimes by three-quarters, the previous programme's caps[5]. This 5% cap was not in keeping with the reality of the costs incurred and resulted in the risk of some financial instruments that had proven successful coming to a halt.

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[3] "Financial instruments shall provide support to final recipients only for investments in both tangible and intangible assets as well as working capital expected to be financially viable and which do not find sufficient funding from market sources. (...) Such support shall be provided only for the elements of the investments which are not physically completed or fully implemented at the date of the investment decision."

[4] Regulation (EU) 2020/460 known as "CRII" being "specific measures to mobilise investments in the healthcare systems of Member States and in other sectors of their economies in response to the COVID-19 outbreak (Coronavirus Response Investment Initiative)" adopted on 30 March 2020; and Regulation (EU) 2020/558 known as "CRII Plus" being "specific measures to provide exceptional flexibility for the use of the European Structural and Investments Funds in response to the COVID-19 outbreak" adopted on 23 April 2020.

[5] ***"****The aggregate amount of management costs and fees over the eligibility period laid down in Article 65(2) of Regulation EU no. 1303/2013 shall not exceed the following limits:*

The caps on management costs and fees applying to the CPR 2021-2027 are a minimum. It would be advisable to maintain, if not actually increase in the future:

- For holding funds (loans and guarantees) selected through a direct award of contract, the cap is 5% of the total amount of programme contributions disbursed to final recipients, and 7% where contributions are disbursed as equity and quasi-equity investments;
- For specific funds selected through a direct award of contract in the form of loans or guarantees, the cap is currently 7% and is expected to be raised to 10% so as to cover all management costs, in line with the provisions of the CPR 2007-2014, and not cause any financial intermediaries to drop out. This cap is 15% where fund contributions are disbursed as equity and quasi-equity investments.

We believe the above factors have made the management rules for Cohesion Policy Funds in the form of financial instruments both simpler and more secure, and they should be maintained in the future.

II. Additional simplifications could usefully be made to the CPR

1. Harmonise the rules and thresholds applicable to environmental requirements across EU programmes

➔ The CPR 2021-2027 introduces a reference to the "do no significant harm" (DNSH) principle for the first time (Article 9.4 and having regard to Article 10), such that funds' objectives cannot cause significant harm to the environment. Inspired by the Taxonomy Regulation, this principle must be met *ex-ante* by the managing authorities' operational programmes, which seems proportionate. In actual fact, nothing prevents managing authorities from postponing the DNSH burden *ex-post* onto the bodies responsible for implementing financial instruments. As a result, it seems helpful to introduce the following proportionality measures:

- Limit DNSH to direct financing operations otherwise there is the risk of private-sector co-funders feeling unable to help finance projects.
- Introduce a DNSH compliance threshold per project, so it applies only to projects exceeding €10m. This threshold already applies to projects under the InvestEU programme.

➔ The principle of DNSH dovetails with that of "climate proofing" requirement (Article 73.2.j), which requires an evaluation of climate impacts for infrastructure projects, with no threshold stated in the CPR. We believe it is necessary to stipulate more proportionate measures by restricting climate proofing to direct financing and projects exceeding €10m or subject to

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(a) for a fund of funds, 7% of the total amount of programme contributions paid to the fund of funds;
(b) for a financial instrument providing equity, 20% of the total amount of programme contributions paid to the financial instrument;
(c) for a financial instrument providing loans, 8% of the total amount of programme contributions paid to the financial instrument;
(d) for a financial instrument providing guarantees, 10% of the total amount of programme contributions paid to the financial instrument;
(e) for a financial instrument providing micro-credit, 10% of the total amount of programme contributions paid to the financial instrument".

Directive 2011/92/EU on the assessment of the effects of certain public and private projects on the environment, as it is the case with the InvestEU programme.

It should be reiterated that the vast majority of projects financed by the Cohesion Policy Funds are very modest in size, and involve micro-enterprises and SMEs, the impact of which on the climate and environment is, by their very nature, limited. The same applies to most of the bodies implementing financial instruments, which in most cases are entities operating on a local scale.

Given the increasing reference to environmental impact assessments for projects financed using EU resources, it seems vital to stipulate rules that are harmonised across all such programmes, with common concepts and requirements in this regard compiled into a single European rule book.

Introducing proportionality into how DNSH and climate proofing are applied would allow to:

- Harmonise the rules under which these new principles are applied across schemes co-financed by Cohesion Policy Funds and those co-financed by InvestEU funds;
- Simplify, improve clarity and ensure equality of treatment between recipient businesses of Cohesion Policy Funds and InvestEU recipients.

2. Enable effective and straightforward *ex-ante* assessments (Article 58.3)

This Article restricts the room for manoeuvre of managing authorities who need to set up instruments able to fill gaps left by market failures. It should be made clear that the purpose of such *ex-ante* examination is to present proposals and indications, while ultimately leaving it to managing authorities to decide on the financial instruments selected and on the investment strategies. This is essential to observe the principle of subsidiarity, good management, and consequently involve managing authorities in allocating financial instruments. A firm of consultants tasked with the *ex-ante* examination should not decide alone which tools are to be used. This role should be left to managing authorities. A proposed amendment is appended to this review.

3. Clarify the verifications and audits on guarantee instruments (Article 81)

The CPR 2021-2027 is a complete change from the provisions that applied during the 2014-2020 period. It is desirable to maintain the previous programme's rules, which stipulated that audits were conducted at the level of the body implementing the financial instrument (without going down to the level of the banks benefiting from that body's guarantee), with the onus on that body to collect documentary evidence that loans were granted in compliance with the intended purpose (appraisal reports, business plan and contracts).
The new CPR provisions (Article 81) intended to ensure management audits are always conducted at the banks delivering the loans as regards guarantee funds could in fact prove counter-productive. The risk is that banks will withdraw from these guarantee schemes, restricting the development of such instruments as a result. To keep guarantee funds' full potential, as the financial instruments with the greatest leverage effect, it is advisable to maintain the current equilibrium seen on ERDF 2014-20 guarantee funds, whereby bank audits should be considered only if the audit on the financial intermediary proves inadequate. A proposed amendment is appended to this review.

4. Relax the rules around the responsibility of beneficiaries (Article 50.3)

Under the CPR, recipients must acknowledge the support provided by Cohesion Policy Funds to an operation, and the applicable responsibility rules are toughened. They now stipulate that "*where the beneficiary does not comply with its [publicity] obligations (...), and where remedial actions have not been put into place, the managing authority shall apply measures, taking into account the principle of proportionality, by cancelling up to 3% of the support from the Funds to the operation concerned*". It is proposed that, given they are repayable in nature, financial instruments do not fall under this rule. A proposed amendment is appended to this review.

5. Other simplification measures

Note that associations have presented other measures designed to simplify how Cohesion Policy Funds are managed.

- Proposals intending to facilitate the setting up of equity financial instruments from Cohesion Policy Funds (ERDF in particular): proposals established in 2019 by PFR Ventures (Poland), Bpifrance and their partners in the European Venture Fund Investors Network (EVFIN) (see annex 2)
- 2022 proposals from some ELTIs members and its partners from the European Long-Term Investors Association (ELTI)[6] to lighten the administrative burden imposed by the financial regulations applying to the European Union budget currently being negotiated.

In conclusion, some simplification measures were achieved in the CPR 2021-2027. It is worth introducing further simplifications to make it easier to use financial instruments and encourage the involvement of privately sourced co-financing.

Regulatory stability and simplicity must be promoted for the CPR after 2027.

Moreover, two additional pathways towards simplification could be further explored. Firstly, it would appear appropriate to consult banks and public-sector promotional institutions when preparing the European Commission's audit methodologies for Cohesion Policy Funds. Secondly, national audit authorities could be encouraged to ratify beforehand the audit trails of banks and public-sector promotional institutions for financial instruments making use of Cohesion Policy Funds. This would not rule audits out but would help make management conditions more secure and accelerate funds deployment.

[6] https://www.eltia.eu/images/2022_10_17_ELTI_Position_Paper_Financial_Regulation.pdf

ANNEX 1

PROPOSED AMENDMENTS TO THE CPR 2021-2027 (REGULATION (EU) 2021/1060)

The proposed amendments are shown in the appropriate place in the text, in bold.

1. **Enable effective and straightforward *ex-ante* assessments (Article 58.3)**

Article 58.3 **Financial instruments** (…) 3. “Appropriate support from the Funds through financial instruments shall be based on an *ex-ante* assessment drawn up under the responsibility of the managing authority. The *ex-ante* assessment shall be completed before managing authorities make programme contributions to financial instruments. The *ex-ante* assessment shall include at least the following elements: **(a)** the proposed amount of programme contribution to a financial instrument and the estimated leverage effect; **(b)** the proposed financial products to be offered, including the possible need for differentiated treatment of investors; **(c)** the proposed target group of final recipients; **(d)** the expected contribution of the financial instrument to the achievement of specific objectives. **On the basis of these proposals, it is incumbent on the managing authority to decide which financial instruments to implement, and their investment strategies.** The *ex-ante* assessment may be reviewed or updated, may cover part or the entire territory of the Member State, and may be based on existing or updated *ex-ante* assessments.”

2. **Clarify the verifications and audits on guarantees (Article 81)**

Article 81
Management verifications and audits of financial instruments

1. The managing authority shall carry out on-the-spot management verifications in accordance with Article 74(1) only at the level of bodies implementing the financial instrument ~~**and, in the context of guarantee funds, at the level of bodies delivering the underlying new loans**~~. The managing authority may rely on verifications carried out by external bodies and not carry out on-the-spot management verifications, provided that it has sufficient evidence of the competence of these external bodies.

2. The managing authority shall not carry out on-the-spot verifications at the level of the EIB or other international financial institutions in which a Member State is a shareholder. However, the EIB or other international financial institutions in which a Member State is a shareholder shall provide control reports supporting the payment claims to the managing authority.

3. The audit authority shall carry out system audits and audits of operations in accordance with Article 77, 79 or 83, as appropriate, at the level of bodies implementing the financial instrument ~~**and, in the context of guarantee funds, at the level of bodies delivering the underlying new loans**~~. The audit results of external auditors of bodies implementing the financial instrument may be taken into account by the audit authority for the purposes of the overall assurance and on this basis, the audit authority may decide to limit its own audit work.

4. In the context of guarantee funds, **managing authorities or external bodies in charge of management verifications and** the bodies responsible for the audit of programmes may conduct **verifications and** audits of the bodies providing new underlying loans only when one or more of the following situations occur:
   a) supporting documents, providing evidence of the support from the financial instrument to final recipients, are not available at the level of the managing authority or at the level of the bodies implementing the financial instrument;
   b) there is evidence that the documents available at the level of the managing authority or at the level of the bodies implementing the financial instrument do not represent a true and accurate record of the support provided.

5. The audit authority shall not carry out audits at the level of the EIB or other international financial institutions in which a Member State is a shareholder, for financial instruments implemented by them. However, the EIB or other international financial institutions in which a Member State is a shareholder shall provide to the Commission and to the audit authority an annual audit report drawn up by their external auditors by the end of each calendar year. This report shall cover the elements included in Annex XXI, and constitute the basis for the audit authority's work.

6. The EIB or other international financial institutions shall provide to the programme authorities all the necessary documents to enable them to fulfil their obligations.

3. **Relax the rules around the responsibility of beneficiaries (Article 50.3)**

Article 50
Responsibilities of beneficiaries

1. Beneficiaries and bodies implementing financial instruments shall acknowledge support from the Funds, including resources reused in accordance with Article 62, to the operation by:

a. providing on the beneficiary's official website, where such a site exists, and social media sites, a short description of the operation, proportionate to the level of support, including its aims and results, and highlighting the financial support from the Union;
b. providing a statement highlighting the support from the Union in a visible manner on documents and communication material relating to the implementation of the operation, intended for the public or for participants;
c. displaying durable plaques or billboards or ~~**permanent**~~ **temporary electronic displays** clearly visible to the public, that present the emblem of the Union in accordance with the technical characteristics laid down in Annex IX, as soon as the physical implementation of operations involving physical investment starts or purchased equipment is installed, in respect of the following: (i) operations supported by the ERDF and the Cohesion Fund the total cost of which exceeds EUR 500,000; (ii) operations supported by the ESF+, the JTF, the EMFAF, the AMIF, the ISF or the BMVI the total cost of which exceeds EUR 100,000;
d. for operations not falling under point (c), displaying at a location clearly visible to the public at least one poster of a minimum size A3 or equivalent electronic display with information about the operation highlighting the support from the Funds; where the beneficiary is a natural person, the beneficiary shall ensure, to the extent possible, that appropriate information is available, highlighting the support from the funds, at a location visible to the public or through an electronic display;
e. for operations of strategic importance and operations the total cost of which exceeds EUR 10,000,000, organising a communication event or activity, as appropriate, and involving the Commission and the responsible managing authority in a timely manner. Where an ESF+ beneficiary is a natural person or for operations supported under the specific objective set out in point (m) of Article 4(1) of the ESF+ Regulation, the requirement set out in point (d) of the first subparagraph shall not apply. By derogation from points (c) and (d) of the first subparagraph, for operations supported by the AMIF, the ISF and the BMVI, the document setting out the conditions for support may establish specific requirements for the public display of information on the support from the Funds where this is justified by reasons of security and public order in accordance with Article 69(5).

2. For small project funds, the beneficiary shall comply with the obligations under Article 36(5) of the Interreg Regulation. For financial instruments, the beneficiary shall ensure by means of the contractual terms that final recipients comply with the requirements set out in point (c) of paragraph 1.

3. Where the beneficiary does not comply with its obligations under Article 47 or paragraphs 1 and 2 of this Article, and where remedial actions have not been put into place, the managing authority shall apply measures, taking into account the principle of proportionality, by cancelling up to 3% of the support from the Funds to the operation concerned. **This provision does not apply to financing provided in the form of financial instruments.**

The European Association of Long-Term Investors – ELTI

ELTI members represent an European-wide network of National Promotional Banks and Institutions who offer financial solutions tailored to the specific needs of their respective country and economy. Multilateral financial institutions complement the activities at national level with specific cross-boarder solutions or investments with an European impact. Following the specific public mission of each member the business model of each institution differs from country to country including different products and approaches. This is the same for multilateral ELTI members. Most of the members offer various debt-products but not all members have a mandate for investment in equity.

The 31 members of the European Long-Term Investors Association (ELTI) a.i.s.b.l. are major long-term investors and represent a combined balance sheet of EUR 2,7 trillion. The Association promotes and attracts quality long- term investment in the real economy, including:

- strengthening cooperation, including at an operational level, between European financial institutions as well as with other Institutions of the European Union (EU) acting as long-term financiers;
- informing the EU and its Institutions on the role and potential of the Members as institutions and agencies for long-term financing;
- strengthening the access of the Members to information on matters related to the EU;
- exchanging information and experiences among Members and with national and international organisations sharing the Association's interest in the promotion of long-term investment;
- developing the concept of long-term investment within the economic and financial sector and promoting academic research on long-term investments;
- representing, promoting and defending the shared interests of its Members in the field of Long-Term Investment in full transparency.

The Full Members of ELTI are generally national official financial institutions dedicated to the promotion of public policies at national and EU level[7]. The European Investment Bank (EIB) as the status of a permanent observer. ELTI also includes Associate Members notably multilateral financial institutions, regional financial institutions and non-banking institutions[8].

[7] Oesterreichische Kontrollbank (OeKB) Austria, Federal Holding and Investment Company (SFPI) Belgium, Bulgarian Development Bank (BDB) Bulgaria, Croatian Bank for Reconstruction and Development (HBOR) Croatia, National Development Bank-CZ (NRB) Czech Republic, Caisse des Dépôts et Consignations (CDC) France, La Banque publique d'Investissement (bpifrance) France, KfW Bankengruppe (KfW) Germany, Hellenic Development Bank (HDB) Greece, Hungarian Development Bank (MFB) Hungary, Strategic Banking Corporation of Ireland (SBCI) Ireland, Cassa Depositi e Prestiti (CDP) Italy, Latvian Development Finance Institution (ALTUM) Latvia, INVEGA Lithuania, Société Nationale de Credit et d'Investissement (SNCI) Luxembourg, Malta Development Bank (MDB), Malta, Invest-NL The Netherlands, Bank Gospodarstwa Krajowego (BGK) Poland, Banco Português de Fomento (BPF) Portugal, Slovak Investment Holding (SIH) Slovakia, Slovenska Izvozna in Razvojna Banka (SID) Slovenia, Instituto de Credito Oficial (ICO) Spain

[8] Nordic Investment Bank (NIB), Council of Europe Development Bank (CEB), Long-Term Infrastructure Investors Association (LTIIA), Participatiemaatschappij Vlaanderen NV (PMV) Belgium, NRW.Bank Germany, Consignment Deposits and Loans Fund (CDLF) Greece, Investment and Development Fund of Montenegro (IRF) – Montenegro, Turkiye Sinai Kalkinma Bankasi (TSKB) Turkey