



EUROPEAN COMMISSION

European Structural and Investment Funds

**FINANCIAL INSTRUMENTS - OVERVIEW OF CHANGES  
IN TITLE IV OF THE CPR FOLLOWING THE OMNIBUS  
REGULATION**

**DISCLAIMER**

*This information document has been prepared by the Commission services in order to provide an overview of the modifications concerning financial instruments introduced in Title IV of Regulation (EU) 1303/2014 (CPR) with the Omnibus Regulation (Regulation (EU, Euratom) 2018/1046). The aim of this document is to provide support to Managing Authorities and other stakeholders, without prejudice to the interpretation of the Court of Justice and the General Court or decisions of the Commission.*

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## I. Introduction

Financial instruments play an increasingly important role in delivering the ESI Funds. In the context of the Investment Plan for Europe, it is essential to ensure that the legal framework is adapted to facilitate the use of financial instruments more widely and when appropriate.

On 2 August 2018, Regulation (EU, Euratom) 2018/1046 of the European Parliament and of the Council (the Omnibus Regulation) on the financial rules applicable to the general budget of the Union came into force, repealing the previous Financial Regulation No 966/2012 and introducing changes to several sectoral regulations, including a limited number of targeted changes for financial instruments (**FIs**) in Title IV of Regulation (EU) No 1303/2013 (CPR).<sup>1</sup>

The changes are meant to facilitate implementation of FIs and have the following main objectives:

- to take better account of the Investment Plan for Europe, which was launched after the adoption of the CPR in November 2014, and in particular to allow smooth interaction and complementarity between support from the ESI Funds and the European Fund for Strategic Investments (**EFSI**);
- to clarify the provisions related to the selection of bodies implementing ESIF financial instruments;
- to maintain for the whole programming period the implementation option of the SME Initiative – initially intended to be a crisis response instrument of more limited duration;
- other technical changes to facilitate implementation, including in relation to ex ante assessment, audit, replacement of expenditure for individual irregularities, treasury management and reporting.

*This document presents an overview of the changes introduced by the Omnibus Regulation in Title IV CPR, and explains the rationale and reasoning behind them. It is meant to help Member States' managing authorities and other stakeholders who want to understand the new rules better and make use of them. It has to be noted that changes in several Commission implementing and delegated acts are underway to reflect the modifications introduced in the CPR; these are however not covered by the present document.*

## II. Information on main CPR changes concerning financial instruments

### 1. Ex-ante assessment (Article 37(2) and (3) CPR)

The Financial Regulation, as replaced by the Omnibus Regulation, requires pursuant to its Article 209(2) that centrally managed FIs are based on an ex-ante evaluation which includes explanations concerning the choice of the type of the financial operation and which takes into account the policy objectives pursued and the associated financial risks and savings for the budget. If such ex-ante evaluation exists and is relevant for a FI considered for support through the ESI Funds by a Member State, the modified Article 37(3) CPR clarifies that such existing ex-ante evaluation can be taken into account for the ex-ante assessment for the ESIF

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<sup>1</sup> Official Journal of the European Union, L193, 30.7.2018, p.1

FI required by the CPR. This will avoid a possible duplication of work, should data relevant to the ESIF FI be already available in the ex-ante evaluation for the centrally managed FI.

An alignment of terminology was also necessary in this Article to reflect the new term 'differentiated treatment' of investors, introduced with the Omnibus Regulation (for more details see point 7 below).

## 2. Direct award (Article 38(4)(b)(iii) CPR)

Many Member States have established publicly-owned banks or institutions that operate under a public policy mandate and have as a goal the promotion of economic development. Such banks or institutions have specific characteristics which differentiate them from private commercial banks in relation to their ownership, their development mandate and the fact that they do not have the objective of maximising profits. Their role is rather to mitigate market failures, where, in certain regions or for certain policy areas or sectors, financial services are underserved by commercial banks. As set out in particular in the Investment Plan for Europe, the Commission's policy is to facilitate the role of such banks or institutions both in the implementation of ESIF financial instruments, as well as in the combination of support from the ESI Funds with EFSI financing.

Managing authorities already have the possibility to award contracts directly to a body implementing FIs supported through the ESI Funds based on the exceptions of the Public Procurement Directive 2014/24/EU, including its Article 12.<sup>2</sup>

Stakeholders' feedback during 2014-2016 revealed, however, that there was a need to clarify further the direct award possibility for the implementation of FIs supported through the ESI Funds. This would provide legal certainty to Member States and regions willing to engage their publicly-owned banks or institutions, establish a level playing field, and facilitate combinations with EFSI, where the implementing body is a publicly-owned bank or institution. The Omnibus Regulation therefore clarified in the CPR that managing authorities have the possibility to award contracts directly also to international financial institutions in which a Member State is a shareholder (IFIs) and to publicly-owned banks or institutions, subject to several detailed conditions. These conditions have been defined to ensure that the possibility of direct award remains in compliance with the Treaty and consistent with the principles of the internal market and with the requirements of the Public Procurement Directive 2014/24/EU. It needs to be ensured that there is no undue advantage over competitors, no distortion of the market, and that high standards of transparency and accountability are met. Managing authorities shall assess the fulfilment of all such conditions.

## 3. Prolongation of the SME Initiative (Article 39)

The SME Initiative was introduced as a crisis-response instrument of limited duration that could be used by Member States to make a contribution to an EU-level FI supporting uncapped guarantees or securitisation. Member State commitments had to be made until 31.12.2016.

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<sup>2</sup> Official Journal of the European Union, L94, 28.3.2014, p. 65.

There was, however, a political will to prolong the SME Initiative, which would allow further Member States to implement it or Member States already implementing it to add additional resources. The Omnibus Regulation has therefore made it possible for Member States to make use of ERDF and EAFRD funding for the SME Initiative during the entire eligibility period.

This entailed several other related changes, including the following:

- given that the ex-ante assessment by the Commission for the purposes of the SME Initiative was carried out in 2013, the possibility was given that Member States' contributions are based, where more recent data is available, on a more recent ex ante assessment at Union, national or regional level;
- under its original set-up, the SME Initiative was to be implemented through a "Single Dedicated National Programme" (SDNP) for each participating Member State. To take account of the mid-term situation, where programmes under the CPR have already been adopted, the Omnibus Regulation provided for greater flexibility by allowing also to implement the SME Initiative through a dedicated priority axis of an existing programme (for ERDF only);
- given the extended period of implementation, changes were also necessary to ensure that the SME Initiative is subject to standard evaluation provisions (i.e. ex-post evaluation in 2023 rather than 2019).

#### 4. Combinations with EFSI (Articles 38(1)(c) and 39a)

Prior to the Omnibus Regulation, the CPR had provided two main implementation options for FIs:

1. Under the first option (under Article 38(1)(a)), a contribution from an ESIF programme to an EU-level instrument.
2. The second option (under Article 38(1)(b)) consists of a contribution from an ESIF programme to a financial instrument set up at national, regional, trans-national or cross border level, managed by or under the responsibility of the managing authority.

Under the new Article 38(1)(c) introduced by the Omnibus Regulation, a third implementation option allows for specific ways of combining ESI Funds and EFSI funding streams that had not been possible before the Omnibus Regulation.

More specifically, in the new Article 39a CPR introduced by the Omnibus Regulation, a series of 16 paragraphs establish the rules applicable to the ESIF funding in the case of combination of ESIF FIs with EFSI under that Article, as follows:

- paragraph (1) highlights that the purpose of combining public support under the ESI Funds and EFSI is to attract additional private sector resources;
- paragraph (2) sets the thresholds for ESI Fund participation – these must not exceed 25% of total support to final recipients, except in less developed regions where duly justified by ex-ante assessment/EIB<sup>3</sup> preparatory assessment and even then not more than 40%;

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<sup>3</sup> When this document refers to the 'EIB', it means the EIB Group, including both the European Investment Bank and the European Investment Fund.

- paragraph (3) gives a possibility for reliance on the preparatory assessment/ due diligence conducted by EIB relating to its contribution to the financial product under EFSI – i.e. no need for a new ex-ante assessment for the ESI Fund part;
- paragraph (4) specifies that when reporting under Article 46 for the ESIF contribution under this Article, managing authorities shall base themselves on reporting information kept by the EIB for reporting under the EFSI Regulation;
- paragraph (5) clarifies the implementation options which are similar to those available for FIs managed under the responsibility of a managing authority;
- paragraph (6) ensures compliance with applicable Union law on tax avoidance and money laundering;
- paragraph (7) provides that the relevant Commission delegated acts are applicable to the new implementation option;
- paragraph (8) specifies that when a fund of funds further entrusts implementation to financial intermediaries, these shall comply with the relevant principles and conditions in the Financial Regulation and be selected on the basis of open, transparent, proportionate and non-discriminatory procedures, avoiding conflict of interests;
- paragraph (9) allows for reliance on the selection procedure of the EIB, IFIs or a publicly-owned bank or institution fulfilling the conditions set out under Article 38(4)(b)(iii) when ESIF contributions are made to an existing EFSI instrument;
- paragraph (10) provides – in the case of an existing EFSI instrument – that the ESI Fund stream shall follow the payment schedule already established for other investors;
- paragraph (11) specifies that the requirements for the content of the funding agreement in Annex IV to the CPR apply to the ESI Fund stream;
- paragraph (12) states that for ESI Fund contributions to investment platforms which receive contributions from instruments set up at EU level, State aid consistency shall be ensured in line with the relevant provision in the Financial Regulation (for other types of ESIF contribution State aid compliance is necessary);
- paragraph (13) gives the possibility for ESI Fund contributions to different tranches in the case of guarantee instruments and for their subordination to EFSI;
- paragraph (14) provides for the possibility of a co-financing rate of up to 100%;
- paragraph (15) clarifies that ESI Fund contributions can be used to give rise to new finance in the entire territory of a Member State ('pooling of risk'); and
- paragraph (16) includes a provision for review by the Commission of the application of this Article by end 2019.

It is important therefore to clarify that this instrument:

- does not imply a contribution of an ESI Fund to an EU-level instrument in the sense of Article 38(1)(a), or the mixing of these two funds into one (the two streams of funding will stay apart and distinct);
- for the ESI Fund stream of funding, the new implementation option follows the approach of instruments under Article 38(1)(b) – i.e. applicability of the ESIF legal framework (Title IV of the CPR and the relevant delegated and implementing acts) as regards the ESIF part, with the addition of some specific rules for the ESIF programme contribution;

- the EFSI stream of funding falls under the EFSI Regulation ((EU) 1017/2015, as amended);
- the two streams of funding do not need to be combined at the same time. There will be cases where the EIB financial product under EFSI contributes to an existing ESI Fund FI already established under the CPR, or conversely, the managing authority may decide to contribute ESI Fund programme resources to an existing instrument already established with an EIB financial product under EFSI (e.g. an investment platform). An important feature of such combination is that the ESI Fund and EFSI will then collectively provide support to final recipients.

It should also be noted that the fact that the legislation refers to "EIB financial product under EFSI" does not mean that these products have to be implemented by the EIB only – the implementation of a combined financial instrument can be entrusted to another body, including the bodies referred to in point (b)(iii) of Article 38(4) CPR.

## 5. Audit and replacement of individual irregularities (Article 40 CPR)

Prior to the Omnibus Regulation, Article 40 CPR defined the assurance model for FIs implemented in the form of contributions to EU-level instruments under Article 38(1)(a). The experience of the Member States that started first implementing such FIs (notably the SME Initiative) showed that it would be useful to clarify the framework.

Furthermore, some Member States reported difficulties regarding the selection of entities performing the on-the-spot verifications under a common framework, as envisaged by the EU legislation (CIR (EU) No 1011/2014).<sup>4</sup>

Based on these experiences, Article 40 CPR was modified in the Omnibus Regulation in order to define an assurance model for all FIs implemented by the EIB and other IFIs and to address the above-mentioned issues, and ensure equal treatment across FIs regardless of the identity of the fund manager.

The Omnibus Regulation clarifies that for EU-level FIs established by a funding agreement signed before the date of entry into force of the Omnibus Regulation, the rules applicable at the moment of the signature of the funding agreement continue to apply.

The Omnibus Regulation also clarifies the conditions for the reuse of contributions in case of individual irregularities. Article 40(5a) therefore provides that:

- if an irregularity occurs at the level of a final recipient, the contribution cancelled may be reused only for other final recipients within the same financial instrument, in line with the eligibility rules of the underlying programme/priority axis;
- if an irregularity occurs at the level of a financial intermediary operating under a fund of funds structure, then the contribution cancelled may be reused only for other financial intermediaries under this fund of funds structure, in line with the eligibility rules of the underlying programme/priority axis;
- if an irregularity is detected at the level of the body implementing the fund of funds, or at the level of the body implementing financial instruments where a financial

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<sup>4</sup> Official Journal of the European Union, L 286, 30.9.2014, p. 1

instrument is implemented without a fund of funds, the contribution cancelled may not be reused within the same operation;

- where a financial correction is made for a systemic irregularity, the contribution cancelled may not be reused at all for any operation affected by the systemic irregularity.

## 6. Extension of the deadline for follow-on investments (Article 42(3) CPR)

The Omnibus Regulation introduced a one-year extension of the end date for signing funding agreements with financial intermediaries for equity instruments for which escrow accounts can be used: from 31.12.2017 to 31.12.2018, thereby giving further time to managing authorities wishing to benefit from the longer time period for such implementation.

The Commission did not propose a modification to this Article as part of its Omnibus proposal of 14 September 2016. The Commission has therefore issued a statement underlining that the modification of Article 42(3) CPR will lead to practical difficulties related to the reporting and auditing of amounts paid into escrow accounts and to increased amounts of the EU budget being paid to escrow accounts, contrary to the principle that support from Cohesion policy should be implemented and accounted for by the moment of closure of the operational programmes.

## 7. Differentiated treatment of investors (Article 43a)

The same concept had existed already in the CPR, prior to the Omnibus Regulation, under Article 44(1)(b) as 'preferential remuneration'.

To clarify this concept further, a new Article 43a was introduced by the Omnibus Regulation into the CPR using instead the term 'differentiated treatment' in a stand-alone legal provision. This term concerns the use of the ESI Funds to offer incentives to investors operating under the market economy principle – either in the form of more advantageous profit or risk sharing vis-à-vis the ESIF – in order to help attract private resources. Moreover, following the launch of the Investment Plan for Europe and EFSI, the new provision states that the EIB can be a recipient of such differentiated treatment when using the EU EFSI Guarantee.

The following important points should be noted:

- the new Article 43a refers to 'investors operating under the market economy principle' – this covers private and public investors operating under the market economy principle i.e. investing at own risk from own resources. Such investors can be, for example, banks, business angels, corporate investors, insurance companies, pension funds, or private individuals. This change of terminology was proposed for alignment with the terminology used in the State aid legal framework;
- the possibility to use support from the ESI Funds for the differentiated treatment of EIB, when using the EU EFSI Guarantee was made in the context of the Investment Plan for Europe in order to maximise the synergies and combination between ESIF and EFSI. One of the advantages of such combination is the possibility to achieve higher leverage of private funds or to allow for riskier investments. Even if EFSI allows the EIB to take higher risks, EFSI per se may not be sufficient to allow the EIB to invest at all in some cases, or if even if it does allow, it could mean higher pricing of the EIB investment which would be passed on to final recipients. This situation

could reduce the attractiveness of the financial support to final recipients. In the situations above, providing differentiated treatment to EFSI allows the EIB to invest at a lower price, thus making the funding conditions attractive to final recipients while increasing leverage and the volume of potential investments;

- when differentiated treatment is offered to investors, its type and level should be proportionate, meaning that it should not exceed what is necessary to attract an investor operating under market economy principle (including the EIB when using the EU EFSI Guarantee). For example: if investors are ready to co-invest with(in) a financial instrument without additional incentives, differentiated treatment from support from the ESI Funds should not be proposed. When differentiated treatment is indeed needed, it should be established at the lowest possible level (e.g. if it is enough that the support from the ESI Funds covers the first loss of 10%, there should not be an automatic proposal to cover 25%, even if allowed by State aid rules);
- this is without prejudice to Union State aid rules.

## 8. Treasury management (Article 44(1)(b))

Article 43 CPR requires that support from the ESI Funds that has been paid to a financial instrument, but which has not yet reached final recipients, is invested on a temporary basis in line with the principles of sound financial management.

In the last years however, the economic and financial crisis had a major impact on the economies and financial markets and led, *inter alia*, to a widespread reduction in interest rates applied to deposits and other assets held for investment purposes. As a result, it is possible that the ESI Fund contribution to the FI generates a negative interest rate, leading to losses of nominal investments instead of gains from the ESIF resources invested.

In order not to penalise bodies implementing financial instruments, the Omnibus Regulation introduced in Article 44 an amendment that negative interest occurring despite active treasury management by the body implementing the FI could be covered by the resources returned to the FI, if agreed so with the managing authority in the funding agreement.

Active treasury management could take the form of longer maturities, more frequent tranching for lower amounts etc. The concrete modalities though need to be agreed between the managing authority and the body implementing the FI.

## 9. Reporting (Article 46 CPR(2)(h) and (i))

The Omnibus Regulation was also used to address a problem of duplication of the provisions on value of equity investments in the CPR article on reporting for FIs (Article 46(2)(h) and (i)).

The Omnibus Regulation has corrected this overlapping by deleting the repeated text from Article 46(2)(h), i.e. to read as follows:

*(h) progress in achieving the expected leverage effect of investments made by the financial instrument;*