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European Structural and Investment Funds

Guidance for Member States on

Article 46 - reporting on financial instruments and on

Article 37(2)(c) - leverage effect

DRAFT

**DISCLAIMER**

**“***This is a working document prepared by the Commission services. On the basis of applicable EU law, it provides technical guidance for colleagues and bodies involved in the monitoring, control or implementation of the European Structural and Investment Funds on how to interpret and apply the EU rules in this area. The aim of this document is to provide Commission services' explanations and interpretations of the said rules in order to facilitate the programme implementation and to encourage good practice(s). This guidance is without prejudice to the interpretation of the Court of Justice and the General Court or decisions of the Commission.***”**

# Introduction

This guidance is intended to the ESI Fund managing authorities (MA). It is designed (i) to provide practical support when preparing report on the operations comprising financial instruments as an annex to the annual implementation report (AIR), and (ii) to explain the main concepts and calculation methods of the leverage effect of ESI Funds supported financial instruments for the purpose of their set up, implementation and reporting.

# Regulatory references and text

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| **Regulation** | **Articles** |
| Reg. (EU, Euratom) N° 966/2012  *(here after Financial Regulation)* | Article 140(2)(d) |
| Rules of Application  *(hereafter RAP)* | Article 223 |
| Reg. (EU) N° 1303/2013  Common Provisions Regulation  *(hereafter CPR)* | Article 37(2)(c)  Article 46  Article 50  Annex IV |
| Reg. (EU) N° 480/2014  Commission Delegated Regulation  *(hereafter CDR)* | Article 8  Article 12 |
| Reg. (EU) N° 821/2014  Commission Implementing Regulation  *(hereafter Commission Implementing Regulation 821/2014)* | Article 2  Annex I |
| Reg. (EU) N° 2015/207  Commission Implementing Regulation  *(hereafter Commission Implementing Regulation 2015/207)* | Article 5  Annex V |

# Reporting on financial instruments (Article 46 CPR)

The guidance part on reporting provides an overview of the regulatory requirements in relation to the reporting on financial instruments and is based on enquiries received from MAs. In order to support the managing authorities in the reporting exercise and to ensure the coherent reporting of the collected data, the Commission has prepared the annotated template based on the model for reporting on financial instruments in Annex I of the Commission Implementing Regulation 821/2014. The annotated template explains the detailed technical characteristics of the requested information to be provided in the reporting module in SFC2014.

## Objectives of the reporting

The information reported in accordance with Article 46(2) CPR allows the Commission to assess progress made in financing and implementing financial instruments and present it, once per year, in summaries of the data pursuant to Article 46(4).

For the purposes of the specific report on financial instruments referred to in Article 46(1) CPR, the managing authorities should use the model set out in Annex I of the Commission Implementing Regulation 821/2014. The reporting model ensures that a specific report covering the operations comprising financial instruments and annexed to the annual and final implementation reports includes all categories of information required in Article 46(2) CPR and that they are reported in a consistent and comparable way and can be consolidated and aggregated.

The reporting obligations, as set-up in Article 46(2) (a)-(j) CPR should be applied at the level of financial instrument, including fund of funds where appropriate, and not at the level of final recipient.

For the purpose of assessment of performance of financial instruments the Commission should collect and aggregate the information provided by the managing authorities in the summaries of data as required by Article 46(4) of the CPR on the progress made in financing and implementing the financial instruments. The regular reporting of data and assessment of its performance should ensure transparency of the implementation process and ensure appropriate monitoring by the Member States and by the Commission.

## Main changes compared to the programming period 2007-2013

The reporting model as in Annex I to the Commission Implementing Regulation 821/2014 has a similar structure to the reporting model used for ERDF and ESF Operational Programmes as of 2011, which was developed to fulfil the reporting requirements under Article 67 (2) (j) of Council Regulation (EC) No 1083/2006, under the programming period 2007-2013.[[1]](#footnote-2) Compared to the previous programming period, in 2014-2020 there is one reporting model for financial instruments implemented under all five ESI Funds (ERDF, CF, ESF, EAFRD and EMFF) programmes. This model may be further adapted to EAFRD and EMFF, according to the specific regulations of those Funds.

The main changes concern the introduction of new elements as set out in Article 46(2) of the CPR and in line with the Financial Regulation i.e.:

* inclusion of reporting on financial instruments that are implemented directly according to Article 38(4)(c);
* reporting by priority axis or measure from which support from the ESI Funds is provided to the financial instrument;
* additional information on implementing arrangements (ex-ante assessment, selection etc.);
* information on interest and other gains generated by support from the ESI Funds to the financial instruments;
* resources paid back to financial instruments from investments or from the release of resources committed;
* the value of equity investments; total amounts re-invested by the financial instrument;
* progress in achieving the expected leverage;
* total amount of investment mobilised through investments made by ESIF financial instruments;
* and contribution of the financial instrument to the achievement of the indicators of the priority axis or measure concerned.

# Reporting the FI information to the Commission

All parts and sections in the reporting model are mandatory, however:

* the reporting information required in paragraphs (h) and (j) of Article 46(2), should be provided only in the annual implementation reports submitted in 2017 and 2019, as well as in the final implementation report. The "lighter" annual implementation reports, including the financial instrument information required in Article 46(2) (a)-(g) and (i) should be submitted in 2016, 2018, 2020, 2021 and 2022.
* the categories of information defined in fields 18, 19, 20 and 21 of the section IV of reporting model should be provided only in the final implementation report.

The managing authorities should submit the reporting information on financial instruments as an annex to their annual and final reports on implementation of programmes. The first report to be submitted by 31 May 2016 should cover the financial years 2014 and 2015, and where applicable for the ERDF, ESF and CF for the period between the starting date for eligibility of expenditure and 31 December 2013.

The reporting model as in the Annex I of the Commission Implementing Regulation 821/2014 contains some indications of the format of the information required (i.e. text, number or date), however detailed technical characteristics of the requested information (as for example: input method, format and length of each field and links to the other information already available in the AIR, like priority axes/measures, indicators) is further developed in the electronic reporting module in SFC2014, similar to the reporting module in SFC2007. An annotated template with detailed reporting instructions is also made available.

The reporting model, once transposed to the electronic module of SFC2014, has to be completed separately for each financial instrument, including where applicable, fund of funds. If the financial instrument/fund of funds receives contributions from more than one ESI Fund and/or programme, the managing authority should report only on the information relative to the programme under its responsibility and priority axes or measures.

# Specific points to pay attention to in providing FI information

A limited number of technical changes between the model in Annex I of the Commission Implementing Regulation 821/2014 and the SFC2014 module have been made. These changes are explained further on in the text and the additional fields have been marked as optional. The changes are made to fulfil the reporting requirements set out in Article 46 of the CPR. In order to allow consistency the numbering from the model is kept in SFC2014 and the annotated template for reporting.

* All amounts should be reported **cumulative** from the set-up of the financial instrument until the end of the reporting year in line with the reporting in the annual implementation report.
* **Amount of ESI Funds committed to the individual thematic objectives (3.1)** *(optional)* **–** in cases where one priority axis contributes to several thematic objectives the model according to Annex I the Commission Implementing Regulation 821/2014 does not provide sufficient quantitative information. In order for the Commission to be able to report per thematic objective further data are needed. The commitment per thematic objective will need only to be provided on the level of priority axis. For other data sets the numbers will be calculated pro-rata based on the breakdown of commitments per thematic objectives.

The information by thematic objective will allow the MSs to assess the contribution of their financial instruments in the key investment areas[[2]](#footnote-3) such as SME-support, energy efficiency, Information and Communication Technology, transport and R&D support set out in the Investment Plan for Europe[[3]](#footnote-4).

* **ESI Fund committed in funding agreements (14.1)** – in order for the Commission to be able to report on the amounts planned in financial instruments per fund the fields 14.1.1 to 14.1.5 *(optional)* have been added.
* **Date of signature of the funding agreement for the financial product (23)** – does not need to be provided. The data are already available on the level of financial instruments (13).
* **Date of completion of the ex-ante assessment (30)** and **Number of selection procedures already launched (31.1)** have been moved to section I, in order to capture instruments where ex-ante assessment have been completed or selection procedures have been launched, but no financial instrument has yet been set up. Furthermore, this eliminates the need to repeat this information for each financial instrument.
* **Total value of new debt finance created by the SME Initiative (CPR Article 39 (10)(b)) (26.1)** *(optional)* added to fulfil the reporting requirements of Article 39(10)(b) CPR.
* **Number of funding agreements already signed (31.2)** does not need to be provided. This information can be derived from the data in the field "Date of signature of the funding agreement with the body implementing the financial instrument (13)".
* **Achieved leverage effect for other support combined with financial instruments (39.2).** In order to ensure consistency on the reporting on leverage this number will not be entered by the users in SFC, but provided by the system, based on the formula of "Achieved leverage effect" presented in section 4.2 of this note.
* **Investment mobilised through investments made by ESIF financial instruments for loan/guarantee/equity and quasi-equity investment by product (39.3)** *(optional)* has been added in view that the definition of leverage of the financial instrument does not capture the total amount of investment mobilised through ESIF financial instruments. In order to report on the wider impact of financial instrument it would be useful to have additional information. The total size of the project supported by the ESIF financial instrument should be reported.

# Compliance and quality check of the FI information

In accordance with Article 50(6) of the CPR, the Commission should, within 15 working days of the date of receipt of the report, assess the admissibility of the implementation report, including the information on financial instruments where applicable according to Article 46(1)(2) of the CPR. In the absence of the information the report is considered inadmissible and MSs are informed accordingly.

The Commission examines the quality of the information reported and, in accordance with Article 50(7) of the CPR, informs the MSs of its observations within two months of the date of receipt of the report. MSs have to ensure that the information provided in section 2 of the annual report (Annex V CIR No 2015/207) with respect to financial instruments is consistent with the information recorded in the specific report on financial instruments.

# Leverage

## Background

The ability to attract additional resources is a key characteristic of financial instruments and one of the main arguments for promoting their use to deliver ESI Funds policy objectives.

Evidence from the 2007-2013 programming period shows that financial instruments supported by the Structural Funds did under certain circumstances indeed attract significant levels of additional public and private funding, although the legislative framework for that period did not request a full set of quantitative data on the leverage effect, nor a qualitative assessment of the conditions for its achievement.

In the 2014-2020 programming period, a reference to the leverage effect is included in the CPR at the stages of establishment and implementation of financial instruments. This section provides guidance on how to calculate the leverage effect of ESI Funds-supported financial instruments for the purposes of their set-up, implementation and reporting.

## Main concepts and calculation methods

The CPR does not contain a definition of 'leverage effect'. The 'expected leverage effect' is referred to in Article 37(2)(c) CPR as '*an estimate of additional public and private resources to be potentially raised by the financial instrument down to the level of the final recipient (expected leverage effect)'*. In the context of the Financial Regulation, the leverage effect is referred to in Article 140(2)(d): *'Leverage effect: the Union contribution to a financial instrument shall aim at mobilizing a global investment exceeding the size of the Union contribution'* and Article 223 of the RAP: *'the amount of finance to eligible final recipients divided by the amount of the Union contribution*', but the latter article does not provide a definition of "the amount of finance to eligible final recipients" or "the amount of the Union contribution".

In the light of the above, this section aims to ensure a uniform understanding of terminology and its consistent use by Member States for the purposes of ESI Funds and the related reporting under Article 46 CPR and suggest a uniform method for its calculation.

The leverage effect is referred to in the CPR in two main contexts:

1. Before launching the financial instrument, already at the stage of the preparation of the ex-ante assessment and the subsequent signature of the funding agreement with the body implementing the financial instrument - an analysis and establishment of the **expected leverage effect** as a result of the additional public and private resources to be raised by the financial instrument (Article 37(2)(c) and Annex IV CPR);
2. After launching the financial instrument, at the stage of monitoring and reporting on its implementation – monitoring the **progress in achieving the expected leverage** as part of the mandatory reporting for the years 2017, 2019 and in the final implementation report (Article 46(2)(h) CPR) (hereafter 'achieved leverage effect')

For the sake of comparability and simplicity, the leverage indicated above should be established at the level of the financial instrument as a whole (i.e. not at the level of each individual transaction). For the same reasons (simplicity and comparability), it should also be calculated in nominal terms (i.e. not in real terms). This means that there will be no discount rate applied to the forecasted future cash flows of the ESI Funds contribution and the total amount reaching final recipients.

Leverage should be calculated by reference to the first cycle of investments only, because resources paid back from the first cycle of investments into final recipients do not constitute any more ESI Funds, but national resources. In this regard, the resources re-used pursuant to Articles 44 and 45 CPR (i.e. second and subsequent investment cycles) should not be taken into account for the calculation of the leverage. For the same reason, repayments and revenues generated by previous instruments of 2007-2013 programming period and used to co-finance the 2014-2020 instrument are not ESI Funds resources and therefore do not count as part of the ESI Funds contribution. Repayments and revenues generated by a (2014-2020) financial instrument itself, which are re-used by the instrument should not count as part of the ESI Funds contribution either, but should be taken into account for the calculation of the amounts repaid (revolved) according to Article 46(2)(g) CPR

Own contributions from final recipients should not be taken into account for the calculation of the leverage effect, because such own contribution is not "additional public and private resources" raised by the financial instrument and provided **to** final recipients.

For other forms of support combined within the financial instrument in a single operation according to Article 37(7) CPR no separate leverage is to be reported because they are established to facilitate equity, guarantee or loan instruments.

Calculation of the expected leverage effect

The **expected leverage effect** should be determined before the effective implementation of the instrument, as part of the obligatory ex-ante assessment pursuant to Article 37(2)(c) CPR, and – except in duly justified cases[[4]](#footnote-5) – should remain constant throughout the duration of the financial instrument.

It will be then an obligatory element of the business plan, included in the funding agreement to be concluded between the managing authority and the body implementing the financial instrument[[5]](#footnote-6) (Annex IV to the CPR), i.e. it will become an agreed target.

It should be calculated as follows:

**Total expected amount of finance to eligible final recipients**

**Expected leverage effect = --------------------------------------------------------------------------------**

**ESI Funds amount committed to the financial instrument**

Total expected amount of finance to eligible final recipients

This has to correspond to an estimate/forecast of the total amount of investments which are expected to reach the final recipients that are eligible for support under the financial instrument and mobilised by the investment from the financial instrument. This estimate/forecast should be equal to the overall volume of finance expected to be mobilised and provided by the financial instrument, notably:

I. The sum of**:**

(1) the expected ESI Funds contribution to the financial instrument;

(2) the expected national co-financing (public or private);

(3) the expected contribution by other investors;

(4) interest and other gains expected to be generated from treasury management (Article 43 CPR)

II. minus Management costs and fees expected to be paid for running the financial instrument(as these amounts do not reach the final recipients).

The amounts reaching final recipients should be understood as follows, depending on the specific instrument:

* for equity instruments, total amount of finance (equity/quasi-equity) expected to be paid to eligible final recipients by the financial intermediaries and co-investors at the level of the final recipients (if any), but not the amount of debt raised through an increase of equity.
* for guarantee instruments covering loans, total amount of underlying loans which are guaranteed.
* for loan instruments, total amount of loans paid to eligible final recipients by the financial instrument.

Committed amount of ESI Funds contribution

The expected leverage effect in the ex-ante assessment corresponds to the total amount of ESI Funds resources which the ex-ante assessment considers necessary for the financial instrument (while the ultimate decision about this amount will be taken by the managing authority, after having consulted the Monitoring Committee, subject to the availability of resources and the policy choices made).

The expected leverage effect in the funding agreement or the strategy document corresponds to the total ESI Funds contribution to the financial instrument as indicated in the funding agreement or the strategy document, committed to cover the FI expenditure for individual transactions inclusive support combined with FI in a single operation and management cost and fees during its entire duration.

Calculation of the progress in achieving the expected leverage

The **progress in achieving the expected leverage effect** should be calculated throughout the financial instrument implementation. Contrary to the initially calculated expected leverage effect, the progress will vary during the implementation. Both values (expected and achieved leverage effect) should be compared in order to assess the progress of the financial instrument in meeting its objectives.

However, as during the financial instrument implementation, at the end of a particular reported year part of the ESI Funds contribution may be paid into the financial instrument, but without reaching yet final recipients, this part of the ESI Funds contribution must be excluded from the calculation, in order to provide for comparability of data and a correct presentation of the leverage effect.

An intermediate **progress in achieving the expected** leverage effect reached during the financial instrument implementation should therefore be calculated as follows:

**Total amount of finance which reached eligible**

**final recipients as of the** end of a reported year

**Achieved leverage effect = --------------------------------------------------------------------------------**

**Eligible ESI Funds support which effectively contributed to the total amount of finance indicated in the nominator**

Total amount of finance which reached eligible final recipients

This should be equal to all resources invested in final recipients, irrespective whether they are private or public, as of the end of a reported year for the calculation, namely:

I. The sum of:

(1) the ESI Funds contribution which reached the final recipients;

(2) the national co-financing. public or private which reached the final recipients;

(3) the contribution by other investors which reached the final recipients,

(4) interest and other gains generated from treasury management (Article 43 CPR) and invested in final recipients

II. minus Management costs and fees expected to be paid for running the FI(as these amounts do not reach the final recipients)

The amounts reaching final recipients should be understood as follows, depending on the specific instrument:

* for equity instruments - the amount paid to eligible final recipients (equity, quasi-equity) by the financial intermediaries and co-investors at the level of the final recipients (if any), but not amount of debt raised through an increase of equity.
* for guarantee instruments covering loans - the total amount of the underlying and disbursed loans to final recipients.
* for loan instruments - the total amount of loans paid to eligible final recipients by the financial instrument.

ESI Funds support which contributed to the total amount of finance reaching final recipients

During the financial instrument implementation this will be the portion of ESI Funds support paid into the financial instrument which effectively contributed to the total amount of finance reaching the final recipients as of the end of a reported year, and management cost and fees.

At closure, this will be the ESI Funds support paid into the financial instrument and considered eligible expenditure under Article 42(a)(b)(d) of the CPR.

## A correct perception of the leverage effect

Care should be taken not to apply automatically the simple assumption 'higher leverage = better performing instrument.' While a situation of not attracting any additional resources to the financial instrument is clearly not acceptable as it goes against its concept, the leverage performance of each individual financial instrument will be directly depending on the market gap/sub-optimal investment situation it addresses, its type, location and type of final recipients, as well as to choices made by programme authorities regarding the trade-off between leverage and revolving effect.

It should be considered that:

• Leverage varies between products (for guarantees it is usually higher), between types of investment (could be lower for research and innovation and other high risk investments), between regions (in richer regions a priori there is more readiness of private sector to co-invest), and between the development stages of final recipients supported (seed and start-up capital are more risky as compared to expansion investments).

• A high leverage effect may be intentionally waived. EU funds in financial instruments with very high leverage usually cover the highest risk share of the investment, and are consequently the first to be lost (first loss piece). The impact of EU funds will in this case be very high in the short term (significant leverage), but there could be little or no revolving effect over time. Depending on the objectives which the FI is meant to support, managing authorities may therefore consciously opt for long-term impact and sustainability of EU support through loans which imply lower leverage but bring higher revolving amounts.

* Attracting additional private resources is an important source for achieving leverage, but this should be looked at correctly in the specific context of the ESI Funds, which intervene in cases where public support is really needed, in order to avoid deadweight and to address a suboptimal market situation/fill in a market gap. It is therefore unreasonable to expect that such FI interventions will always attract massive private capital, but rather that the public resources can help catalyse private funds in sectors/areas which otherwise may not have been considered at all.
* In 2014-2020, managing authorities are taking decisions on ESI Funds programme contributions to financial instruments on the basis of a mandatory ex-ante assessment. This will examine evidence of market failures or sub-optimal investment situations and estimated level and scope of public investment needs, as well as the expected leverage effect and financial products to be offered.

# . Reference, links

# Questions and answers

1. Reporting Instructions for the Financial Engineering Instruments ( EGESIF\_15-0015-01) <http://ec.europa.eu/regional_policy/sources/thefunds/fin_inst/pdf/guidance_reporting_instruction_air2014.pdf> [↑](#footnote-ref-2)
2. Member States were recommended to deliver through FIs a percentage of the allocations made in their Partnership Agreements to each of “the key investment areas” as follows: 50% in the field of SME support; 20% in the field of CO2 reduction measures; 10% in the field of Information and Communication Technology; 10% in the field of sustainable transport ; 5% in the field of support for Research Development and Innovation ; and 5% in the field of environmental and resource efficiency. The use of micro-finance facilities to provide preferential loans was also deemed to be helpful to promote self-employment, entrepreneurship and develop micro-enterprises. [↑](#footnote-ref-3)
3. **Communication from the Commission to the European Parliament, the Council, the European Central Bank, the European Economic and Social Committee, the Committee of the Regions and the European Investment Bank: An Investment Plan for Europe:** <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2014:903:FIN> [↑](#footnote-ref-4)
4. For example, unexpected significant change in the market conditions that could not have been envisaged at the time of drafting the ex-ante assessment, but has occurred subsequently and has an impact on the performance of the FI, thus leading also to an update of the ex-ante assessment. [↑](#footnote-ref-5)
5. Or the strategy document in the case of direct implementation under Article 38(4)(c) CPR. [↑](#footnote-ref-6)