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Barriers to the implementation of financial instruments under cohesion policy

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Agnieszka Kłos

Barriers to the implementation of financial instruments under cohesion policy

Abstract: One of the main sources of financing investments in the public sector are preferential loans or guarantees granted under European funds. The article presents the current legal system for the implementation of financial instruments, legal and systemic issues that hinder the use of this form of support, including the overlapping of financial instruments of two financial perspectives, and a proposal for new legal solutions aimed at simplifying the implementation of financial instruments in the 2021-2027 financial perspective.
Keywords: cohesion policy, financial instruments, EU budget, financial perspective 2014-2020

Introduction

The 2007 crisis revealed the weakness of EU institutions regarding the possibility of taking remedial measures. In response to the events that were a consequence of the crisis, such as the financial crisis in Greece, steps were taken to, among others, develop legal solutions to stabilize the public finance situation in the Member States, and establish a Banking Union, a Capital Union, etc.[1] As part of actions undertaken within the cohesion policy, it was decided that the economic activation of Member States be arrived at through preferential financial instruments. Those financial instruments are launched at the level of

1 See: A. Visvizi, 'The Eurozone crisis in perspective: causes & implications', in: A. Visvizi, T. Stepniewski (eds.), 'The Eurozone crisis: implications for Central and Eastern Europe', *Yearbook of the Institute of Central-East Europe*, vol. 10, issue 5, 2012, pp. 13-32.

the European Union, but also under the European Structural and Investment Funds at the level of Member States and regions.

The aim of this publication is to present the specificity associated with the definition of financial instruments, problems related to their implementation at the level of Member States, barriers regarding their re-distribution, including the overlapping of financing, and proposed legal solutions for the forthcoming 2021-2027 financial perspective. The article comprises of an introduction, the main content part consisting of four points, and a summary.

This study was carried out mainly on the basis of EU legal acts and guidelines detailing their interpretation regarding the implementation of financial instruments. Analysis and synthesis were applied as the chief research methods. The study is a voice on the effectiveness and efficiency of the use of financial instruments in the economic development of EU Member States. Due to the complexity of the implementation process of financial instruments and their impact on the economy, the study will be subject to continuation.

1. Definitions of financial instruments implemented under the EU cohesion policy for 2007-2013 and 2014-2020

Financial instruments are, in addition to the grant system, used as the second instrument in the implementation of the EU cohesion policy. Initially, financial instruments were implemented to a limited extent, however, since the crisis in 2008 and the announcement of the Juncker Plan, they have gained in popularity and are being implemented by all Member States to an ever greater extent, both at the regional and at the national level. Originally, the term used in EU legislation was "financial engineering instrument"[2], but in the 2014-2020 financial perspective it was replaced by "financial instrument". In general terms, the locution "financial engineering instrument" is associated mainly with the field of finance which focuses on the use of financial theory and financial instruments (in particular derivative instruments, i.e. options or futures) to solve complex financial problems or to take speculative actions in order to achieve a higher-than-average profit.

2 This was the prevailing term for the 2007-2013 programming period.

Such an understanding of the financial engineering instrument has nothing to do with the term "financial engineering instrument" as defined in the context of the implementation of cohesion policy. In the Council Regulation (EC) No 1083/2006 of 11 July 2006 laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund and repealing Regulation (EC) No 1260/1999[3] no definition of a financial engineering instrument is provided, however, in article 44 of the Regulation it was indicated that "as part of an operational programme, the Structural Funds may finance expenditure in respect of an operation comprising contributions to support financial engineering instruments for enterprises, primarily small and medium-sized ones, such as venture capital funds, guarantee funds and loan funds, and for urban development funds, that is, funds investing in public-private partnerships and other projects included in an integrated plan for sustainable urban development. When such operations are organised through holding funds, that is, funds set up to invest in several venture capital funds, guarantee funds, loan funds and urban development funds, the Member State or the managing authority shall implement them through one or more of the following forms:

a) the award of a public contract in accordance with applicable public procurement law;

b) in other cases, where the agreement is not a public service contract within the meaning of public procurement law, the award of a grant, defined for this purpose as a direct financial contribution by way of a donation:

(i) to the EIB or to the EFI; or

(ii) to a financial institution without a call for proposal, if this is pursuant to a national law compatible with the Treaty".

In the 2007-2013 financial perspective, the legal regulations regarding financial engineering instruments were rather general, and all the details, guidelines, recommendations and good practices were included in the notes of the Coordinating Committee of the Funds (COCOF).

3 EU OJ No L 210.

In the 2014-2020 financial perspective, however, more emphasis was put on the implementation of financial instruments under cohesion policy, that being predominantly due to the financial crisis.

Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006[4] introduces broader provisions regulating the implementation of "financial instruments". What is more, there was a change in the name of the concept from financial engineering instruments to financial instruments, which seems to be more adequate to the nature of the instruments implemented from structural funds. The definition of "financial instruments" was provided in Regulation (EU, Euratom) No 966/2012 of the European Parliament and of the Council of 25 October 2012[5] (the so-called Financial Regulation), which applies to all budgetary chapters. According to article 2 point p) of said regulation "financial instruments" are "Union measures of financial support provided on a complementary basis from the budget in order to address one or more specific policy objectives of the Union. Such instruments may take the form of equity or quasi-equity investments, loans or guarantees, or other risk-sharing instruments, and may, where appropriate, be combined with grants." Article 2 point 11 of the aforementioned Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 provides the only reference to the definition of 'financial instruments' as set out in the financial regulation. In that regulation all information regarding the specifics of the implementation of financial instruments is included in *Title IV Financial Instruments* (articles 37 to 46). In general, "Eu-

4 EU OJ No L 347.

5 Regulation of the European Parliament and of the Council (EU, EURATOM) No. 966/2012 of 25 October 2012 on the financial rules applicable to the general budget of the Union and repealing Council Regulation (EC, Euratom) No. 1605/2002, EU Journal od Laws L 298/1 of 26.10.2012.

ropean Structural and Investment Funds (EFSI)[6] may be used to support financial instruments under one or more programmes, including when organised through funds of funds, in order to contribute to the achievement of specific objectives set out under a priority."

The Regulation puts forward in a rather detailed way the stages of work that precede the implementation of financial instruments. Such a pre-emptive action is the preparation of an "ex-ante analysis", in which the failure of market mechanisms or the suboptimal level of investment should be demonstrated, as well as the estimated level and extent of demand for public investments. In addition, the types of financial instruments to be supported should be indicated[7]. In the 2014-2020 financial perspective the managing authorities may provide a financial contribution to:

a) financial instruments set up at Union level, managed directly or indirectly by the Commission, or

b) financial instruments set up at national, regional, transnational or cross-border level, managed by or under the responsibility of the managing authority.

Contributions from the ESI Funds to financial instruments set up at Union level and managed directly or indirectly by the Commission are to be placed in separate accounts and used, in accordance with the objectives of the respective ESI Funds, to support actions and final recipients consistent with the programme or programmes from which such contributions are made.

When supporting financial instruments set up at national, regional, transnational or cross-border level, the managing authority may:

a) invest in the capital of existing or newly created legal entities, including those financed from other ESI Funds, dedicated to implementing financial instruments consistent with the objectives of the

6 The European Structural and Investment Funds (ESI Funds) consist of: European Regional Development Fund (ERDF), European Social Fund (ESF), Cohesion Fund, European Agricultural Fund for Rural Development (EAFRD), European Maritime and Fisheries Fund (EMFF).

7 More information on ex-ante analysis can be found in article 37(2) of Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013 laying down common provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund and repealing Council Regulation (EC) No 1083/2006 (OJ L 347).

respective ESI Funds, which will undertake implementation tasks; the support to such entities shall be limited to the amounts necessary to implement new investments in accordance with Article 37 and in a manner that is consistent with the objectives of the Regulation;

b) entrust implementation tasks to:

(i) the European Investment Bank (EIB);

(ii) international financial institutions in which a Member State is a shareholder, or financial institutions established in a Member State aiming at the achievement of public interest under the control of a public authority;

(iii) a body governed by public or private law; or

c) undertake implementation tasks directly, in the case of financial instruments consisting solely of loans or guarantees.

In the case of entrusting implementation tasks, managing authorities should apply national law as regards public procurement, with the exception of the EIB and international financial institutions in which a Member State is a shareholder (for example the World Bank).

All matters related to the implementation of financial instruments are regulated not by COCOF notes, as it was the case in the previous financial perspective, but by other delegated[8] and implementing[9] regulations and by guidelines of the European Commission[10] regarding the

8 Commission Delegated Regulation (EU) No 480/2014 of 3 March 2014 supplementing Regulation (EU) No 1303/2013 of the European Parliament and of the Council establishing common rules for the European Regional Development Fund, European Social Fund, Cohesion Fund, European Agricultural Fund for the Development of Rural Areas and the European Maritime and Fisheries Fund and laying down general provisions on the European Regional Development Fund, the European Social Fund, the Cohesion Fund and the European Maritime and Fisheries Fund.

9 Commission Implementing Regulation (EU) No 964/2014 of 11 September 2014 laying down rules for the application of Regulation (EU) No 1303/2013 of the European Parliament and of the Council as regards standard conditions for financial instruments; Commission Implementing Regulation (EU) No 821/2014 of 28 July 2014 laying down rules for the application of Regulation (EU) No 1303/2013 of the European Parliament and of the Council as regards detailed arrangements for the transfer and management of programme contributions, the reporting on financial instruments, technical characteristics of information and communication measures for operations and the system to record and store data.

10 For example: Guidance for Member States on Article 37(2) CPR – Ex-ante assessment, EGESIF_14_0039-1 27/03/2015; European Commission, EC Regulatory Guidance (Guidance for Member States on Article 37(4) CPR, Support to enterprises/working capital), EGESIF_14_0041-1 27/03/2015; Guidance Member States Request for payment, European Commission, EGESIF_15-0006-01 08/06/2015; European Structural and Investment Funds Guidance for Member States and Programme Authorities CPR_37_7_8_9 Combination of support from a Financial Instrument with other forms of support, European Union, European Commission 2015;

application of the relevant articles of Regulation (EU) No. 1303/2013 of the European Parliament and of the Council of 17 December 2013.

2. Main problem areas regarding the implementation of financial instruments in 2014-2020

The implementation of financial engineering instruments in the 2007-2013 and the 2014-2020 financial perspectives entails solving legal, operational and financial issues in all institutions involved in the implementation of financial instruments. Barriers of various nature and intensity appear at different levels of the management and implementation system of these instruments. The gradation of problems depends on the place a given institution, which is facing the issues in question, occupies in the system. A. Faiña, J. Lopez-Rodguez, P. Montes-Solla and L. Varela Candamio point out that in Spain, for example, a significant problem experienced in using financial instruments as part of cohesion policy is caused by the complexity of management and verification systems. In particular, the management and control procedures do not always match some financial products. Also, a lack of cooperation between entities at different levels of the management body, regional intermediary bodies, national management authorities and control and audit institutions leads to an unnecessary repetition of processes and actions[11].

In the special report *Implementing the EU budget through financial instruments – lessons to be learnt from the 2007-2013 programme period* the European Court of Auditors formulated opinions on the general conclusions drawn from the implementation processes at EU level. Among others, issues such as the following were pointed out:

Guidance for Member States on Article 42(1)(d) CPR – Eligible management costs and fees, European Union, 2015; New guidelines on combining European Structural and Investment Funds with the EFSI, European Commission March 2016; Guidance for Member States on Interest and Other Gains Generated by ESI Funds support paid to FI (Article 43 CPR), European Commission, EGESIF_15-0031-01, Final 17/02/2016.

11 A. Faiña, J. Lopez-Rodguez, P. Montes-Sollaand L. Varela Candamio, *Expert evaluation network delivering policy analysis on the performance of Cohesion policy 2007-2013 Year 2 – 2012 Task 1: Financial engineering, Spain*, Jean Monnet Research Group on Competition and Development, University Of Coruña, A report to the European Commission Directorate-General Regional Policy, pp. 11-12.

- low disbursement rates caused by excessive initial capital endowment of financial instruments;
- market needs for financial instruments were not always properly assessed. In nearly half of the audited cases, market needs had been assessed too high, which resulted in an overcapitalisation of the instrument or little or no real impact on the ground situation[12];

It was also pointed out that the ERDF and ESF financial instruments are significantly smaller than centrally managed funds or private investment funds[13] and that the Commission failed to provide a measurement of the multiplier effect on financial instruments, which would take into due consideration to what extent public funding attracts additional funds[14].

With regard to the 2014-2020 financial perspective, Member States note that it is necessary to simplify the provisions on the implementation of cohesion policy in order to ensure the achievement of assumed EU development objectives for this period. Equally important is the need to ensure sound financial management and the implementation of a result-oriented approach. The cohesion policy is based on the principle of shared management and responsibility, while any simplification in its implementation and the ensurance of full benefits resulting from its implementation can be achieved if it is undertaken as a joint challenge by the Commission, Member States and all bodies involved in management, and if provisions to avoid additional obligations or burdensome application of rules are developed and adopted. When developing simplifications of the implementation of cohesion policy the fears and concerns of the beneficiaries, especially in the SME sector, should not be disregarded. Those entities also play a part in the implementation process of structural funds and more and more often they point out the multiplicity and complexity of existing laws and procedures, their instability, the overlapping and inconsistency with other EU policies and with the assistance within those policies. Such a state of affairs increases the sense of legal uncertainty and makes

12 *Implementing the EU budget through financial instruments – lessons to be learnt from the 2007-2013 programme period*, Special Report No 19/2016 European Court of Auditors, 2016, p. 44.
13 Ibid., p. 47.
14 Ibid., p. 49.

it more difficult to actually understand the rules and provisions and their interpretations. Simplification measures should apply to the entire cycle of programming and implementation processes, also taking into account the needs of all entities involved in the management and control processes, and should be treated in a consistent and coherent manner.

During the Dutch Presidency in the Council of the European Union, the European Committee of the Regions and Holland organized two joint informal simplification workshops, i.e. on 27 January 2016 and on 10 March 2016, during which experts from Member States and regional and local authorities discussed challenges as well as proposals for solutions for the simplification of regulations with respect to the implementation of cohesion policy. The discussion and developed proposals for changes focused on auditing, reporting, public aid and public procurement procedures. A joint report from those two previous expert seminars was the basis for discussion at the informal meeting of the Directors-General responsible for cohesion policy, which took place on 13 May 2016 in Amsterdam[15].

During the above-mentioned meetings the representatives of the regions expressed the view that the entire administrative system of cohesion policy should be streamlined and simplified for both the managing authorities and the beneficiaries. The multitude of guidelines for the implementation of financial instruments and the legal provisions for their implementation, result in hindering and lengthening the very process of their implementation. The emergence of more and more new guidelines translates into a general sense of uncertainty in the implementation of financial instruments, lack of control over information coherence and a growing complexity of the entire topic, which can be illustrated for example by investments using the ESIF merger mechanism with the European Fund for Strategic Investments (ESI Funds), the importance of which in the development of Europe was pointed out by the President of the European Commission, Jean-Claude Juncker.

15 *Simplification of the implementation of Cohesion Policy*, Workshops on 27 January and 10 March 2016, Final Report, Committee of Regions, Brussels, April 2016, pp. 4-10.

One of the areas that requires a thorough change is, for example, the "ex-ante analysis", which should be prepared before implementing measures are undertaken and which should be subject to updates. Although article 37 of Regulation 1303/2013 covers a wide range of issues with a high degree of detail, the decision on when the ex-ante assessment should be updated was left to the managing authority. An update should be performed when the ex-ante analysis does "no longer accurately represent the market conditions existing at the time of implementation". The problem of preparing and updating the ex-ante analysis is also linked to the need for flexibilising portfolio management by the financial institution. An ex-ante document will never reflect the current market situation due to constant changes in demand and supply of capital as well as investment opportunities in the SME sector. In this context, it seems that the scope of information provided in the analysis should be narrower and should not be subject to constant changes.

Basing on the ex-ante analysis an investment strategy is developed by the institutions managing the operational programme. Just like the afore-mentioned ex-ante analysis, it should be of flexible nature as the effectiveness of interventions in the formula of financial instruments is closely related to the current situation on the market, which in turn is characterized by high dynamics and uncertainty. The need for experts and expertise in carrying out research and financial issues makes this type of research expensive and time-consuming. Another problematic component is the monitoring and capturing the moment of the gap in the future.

The conditions for granting financial instruments to SMEs should not differ from the available market products. For beneficiaries, a few percent of savings (especially in microfinance) are not encouraging enough to take out loans or obtain guarantees that then entail keeping extended project documentation in the company. The entrepreneur is interested in acquiring cheap capital and in efficient execution of investments. Increasing the level of bureaucracy within financial instruments will result in entrepreneurs moving away from preferential products that would require a lot of involvement in the preparation and keeping of documentation comparable in its amount to the grant system.

The implementation of financial instruments is related to ensuring the distribution of financial resources in the economy. Optimal implementation of financial instruments at the regional level is hindered by the dynamic changes in their range and variety at the national level (for example businessmax guarantee, which is a continuation of the de minimis guarantee, repayable assistance for thermo-modernization under the Operational Programme Infrastructure and Environment, etc.).

Another important aspect, from the point of financial management and ensuring financial liquidity to financial institutions, is the introduction of the possibility of transferring payments by the managing authority to a financial instrument in the amount of 25% of the total contribution from the programme allocated to a given instrument and of the dependence of transferring subsequent tranches from the level of their involvement, i.e. loans/guarantees to final beneficiaries[16]. Such an approach hinders the flexibility of financial instruments management, it also leads to difficulties in the certification of funds and achieving the so-called "milestones" in the use of financial resources, which in extreme cases could even result in a failure to use the allocation. With the next financial perspective in sight, consideration should be given to the idea of going back to the system of financial funding of funds in the form that was adopted in the 2007-2013 financial perspective, i.e. the transfer of funds to the financial institution in its entirety.

Another area which deserves attention is the matter of accounting of management costs. According to Commission Delegated Regulation (EU) No 480/2014, the aggregate amount of management costs and fees over the eligibility period, i.e. between 1 January 2014 and 31 December 2023, may not exceed 7% of the total amount of programme

16 In each application for interim payment submitted during the eligibility period, the amount of programme contribution paid to the financial instrument shall not exceed 25% of the total programme contributions committed to the financial instrument under the relevant financing agreement. Subsequent applications for interim payment can submitted within the eligibility period, i.e. from January 1, 2014 to December 31, 2023, if they respect the following rules:
- in the case of a second application for interim payment, once 60% of the amount included in the first interim payment has been spent as eligible expenditure;
- in the case of third and subsequent applications for interim payment, once 85% of the amounts included in the previous applications for payment have been spent as eligible expenditure.

contributions paid to the fund of funds[17]. Management costs and fees which can be declared as eligible costs may not exceed the sum of:

a) 3% for the first 12 months after the signature of the funding agreement, 1% for the next 12 months, thereafter 0,5% per annum, of the programme contributions paid to the fund of funds, calculated pro rata temporis from the date of effective payment to the fund of funds until the end of the eligibility period, repayment to the managing authority or the date of winding up, whichever is earlier; and

b) 0,5% per annum of programme contributions paid by the fund of funds to financial intermediaries, calculated pro rata temporis from the moment of effective payment by the fund of funds until repayment to the fund of funds, the end of the eligibility period or the date of winding up, whichever is earlier.

However, in the case of bodies implementing financial instruments providing equity, loans, guarantees, as well as micro-credits, including when combined with grants, interest rate subsidies or guarantee fee subsidies, management costs and fees may not exceed the sum of base remuneration or performance-based remuneration. The amount of costs depends on the type of instrument offered. The amount of management fees calculated with the current formula may turn out to be insufficient in relation to the actual costs incurred by financial institutions. Thus, said institutions might be more reluctant to get involved in the implementation of financial instruments.

3. Barriers to combining financial instruments from 2007-2013 and 2014-2020 financial perspectives

The revolving nature is characteristic of financial instruments, which means that funds returned to a financial institution by final beneficiaries are subject to re-distribution. According to article 78 paragraph 7 of Council Regulation (EC) No. 1083/2006 of 11 July, 2006, "resources returned to the operation from investments undertaken by funds as defined in Article 44 or left over after all guarantees have been hon-

17 Commission Delegated Regulation (EU) No 480/2014 includes also other percentage thresholds regarding incurred costs depending on whether the financial instruments are implemented in a form different than the fund of funds.

oured shall be reused by the competent authorities of the Member States concerned for the benefit of urban development projects or of small and medium-sized enterprises". In the years 2007-2013 and 2014-2020 financial instruments can be implemented in the areas of:

- investments in the SME sector,
- renewable energy sources,
- energy efficiency, and
- regeneration of marginalised areas included in an integrated plan for sustainable urban development[18].

In the 2014-2020 financial perspective the area of using financial instruments is decided by an ex-ante analysis, which describes the financial gaps and the proposed instruments which are to contribute to their reduction. To this end, an investment strategy is developed, providing detailed information on the implementation of financial instruments in a given area, including schedule of actions, financial plan, types of final beneficiaries, etc.

Taking into account the above-mentioned provisions of article 78 paragraph 7 of the Council Regulation (EC) No. 1083/2006 of 11 July 2006, funds from the 2007-2013 financial perspective may be re-used by the competent authorities of a Member State for specific types of projects. Apart from developing a new system for implementing financial instruments in the new financial perspective, Member States are also obliged to ensure an appropriate system enabling the reallocation of funds returning from final beneficiaries within the 2007-2013 financial perspective. In the case of Poland, the mode of re-distribution of these funds was sanctioned in article 98 of the Act of 11 July 2014 on the principles of implementation of the cohesion policy programmes, financed under the 2014-2020 financial perspective[19], according to which "Financial resources from contributions made under national and regional operational programmes to financial engineering instruments implemented on the basis of article 44 of the Council Regulation (EC) No. 1083/2006 of July 11, 2006, after the fulfilment of obligations resulting from the contracts on co-financing

18 *Financial Engineering Instruments in Cohesion Policy*, Directorate-General for Internal Policies, European Parliament 2013, p. 17.
19 Dziennik Ustaw [Journal of Laws] from 2016 item 217.

in the scope of their use in accordance with article 78 paragraph 7 of this regulation, not involved in contracts with recipients of support, granted by financial engineering instruments and funds returned by these recipients to financial engineering instruments, are re-used to achieve the objectives set out in article 78 paragraph 7 of this regulation, in accordance with article 152 paragraph 1 of the general regulation." In order to re-use financial resources, the managing institution of a given operational programme opens a bank account in the Bank Gospodarstwa Krajowego [Polish national development bank] for the servicing of financial engineering instruments. The financial service of this account is maintained in accordance with the agreement signed between the managing authority and the Bank Gospodarstwa Krajowego. The legislator also points out that the sole administrator of funds accumulated on these accounts is the minister competent for regional development – in relation to funds coming from the national operational programme, and the voivodeship board – in relation to funds from the regional operational programme. The funds that are accumulated on the account are released by the Bank Gospodarstwa Krajowego only at the request of the relevant entity.

The resources involved in the financial instruments of the 2007-2013 financial perspective, once their certification and settlement with the European Commission are complete, lose the status of European funds, but they are still public funds at the disposal of the minister competent for regional development or the voivodeship board. These resources do not constitute income of local government units or budget revenues. Indicated entities may also make decisions regarding the remaining funds for further distribution in existing financial institutions or transfer them to other ones. For this purpose, as mentioned before, a so-called exit strategy for a financial instrument and a system for their re-implementation need to be developed.

Considering that the above-mentioned funds remain in the economy and new funds are introduced as part of the 2014-2020 perspective, some issues regarding their allocation might arise. The main doubts concern the following areas:

a) What types of projects will be supported in the form of financial instruments? If investment gaps overlap in the same areas as in the previous perspective, a demarcation line should be provided between instruments re-introduced to the market and the new ones implemented under the new financial perspective. It should be remembered that demarcation concerns both the area (i.e. the type of projects) and the proposed financial product (i.e. the rules for granting loans, guarantees, interest rates, etc.).

b) Will it be possible to combine public funds (for example granting guarantees with the resources from the 2007-2013 financial perspective for loans granted with the resources from the 2014-2020 perspective) and the incurred financial risk? In the case cited, 100% of the risk would concern only public funds, without involving the equities of financial institutions, which would result in lower economic efficiency of their use.

c) How will the own contribution of the grant beneficiary be defined? For example, can a commercial loan, guaranteed by public funds, be qualified as own contribution of the grant beneficiary? In this case, the problem relates to what happens when repayments of a loans are discontinued and the need to launch surety funds, which are public funds, may arise. This is important from the point of view of the final beneficiary, since a guarantee (from funds that are subject to re-use) of loans taken out on the market to finance own contribution in projects with subventions in the form of subsidies under 2014-2020 operational programmes is treated as co-financing from EU resources (overlapping of funding), which may result in repayment of funds to the budget should irregularities be found during checks.

d) Is it possible to use financial instruments implemented from funds of the current financial perspective to pre-finance expenditures covered by grant support? The current EC Guidelines on combining support and the Guidelines on eligibility of expenditure under the ERDF, ESF and CF for the years 2014-2020 do not allow for the mentioned operations.

e) Is it possible to finance funds subject to re-use of capital entries in enterprises (or possibly in other projects or an enterprise co-financed from public funds)? Currently, there is overliquidity of public funds on the market for this type of support. At the same time, interesting start-ups seek support from private investors whose funds are not „burdened" with restrictive access procedures or monitoring of use like in the case of public funds.

Another issue is the development and introduction of separate, detailed reporting for both types of resources, which means additional administrative burden on the part of the financial institution and other entities, as well as difficulties in finding appropriate staff to ensure proper quality of design and implementation of financial products subject to re-distribution.

The examples given above are only a few reflections on the systemic and interpretational problems resulting from the applicable EU and national legal provisions. It should also be kept in mind that the financial instruments of the current financial perspective will be subject to re-use after 2023, that is after the period of their final settlement with the European Commission. In the meantime, financial instruments will be implemented as part of the forthcoming 2021-2027 financial perspective. In this case, it will be necessary to provide appropriate demarcation lines for the financial instruments of the three perspectives.

When considering the question of distribution of financial instruments, what should also be taken into consideration is whether the introduction of new instruments (and those would be resources up to tens or hundreds of millions of euros at the level of a Member State) will not at some point contribute to the destabilization of the financial sector in the Member States and as a result crowd out private funds with public funds. Financial institutions that undertake cooperation with institutions that manage operational programmes within the scope of distribution of financial instruments are obliged to involve own capital into this process, which means a depletion of equity in relation to their commercial activity. Theoretically, the case may arise where the beneficiaries will be more interested in available instruments financed from public funds, and not the financial products offered by these institutions with market interest rates. Of course, the opposite situation might also occur, depending on the preferences of the beneficiaries, the economic situation of a given country or region, the range of financial products offered by financial institutions, specifically developed for certain project types, which were indicated in ex-ante analyses, on the rules for granting them and on obligations relating to their settlements. Extensive administrative requirements resulting from EU or national legislation may in the future be of little interest to final beneficiaries, and the established rules may prove too strict, which will exclude some beneficiaries from the possibility of applying for this type of assistance.

4. Proposals for solutions regarding the implementation of financial instruments in the 2021-2027 financial perspective

On May 2, 2018, the European Commission presented a proposal regarding the shape of the future seven-year EU budgetary framework for 2021-2027. It assumes a total sum of EUR 1,279 billion in commitments and a total sum of EUR 1,246 billion in payments[20]. Currently, work is underway on a package of legal acts regarding the implementation of cohesion policy in the upcoming financial perspective. In the reflection paper on EU finances, as well as in the ex-post evaluation and public consultations, the introduction of administrative simplification was considered the main objective. So far experience shows that the provisions are excessively complicated and fragmented, which results in an unnecessary burden on programme managers and final beneficiaries. The ex-post evaluation of ERDF and the Cohesion Fund found that financial instruments have the potential to be a more efficient means of funding investment in some policy areas, but there are delays in implementation and it is a challenge to spread their use. The evaluation found that different rules made it difficult to tap into complementarities between funds. Therefore, it was recommended that the rules on financial instruments be streamlined and aligned[21]. The Proposal for a Regulation of the European Parliament and of the Council laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, and the European Maritime and Fisheries Fund and financial rules for those and for the Asylum and Migration Fund, the Internal Security Fund and the Border Management and Visa Instrument introduces a series of new definitions to organize the subject matter within financial instruments. The proposal for a new regulation puts forward

20 Communication From The Commission To The European Parliament, The European Council, The Council, *The European Economic And Social Committee And The Committee Of The Region, A Modern Budget for a Union that Protects, Empowers and Defends The Multiannual Financial Framework for 2021-2027*, Brussels, 2.5.2018COM(2018) 321 final, European Commission, p. 25.

21 *Proposal for a Regulation of the European Parliament and of the Council laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, and the European Maritime and Fisheries Fund and financial rules for those and for the Asylum and Migration Fund, the Internal Security Fund and the Border Management and Visa Instrument*, COM(2018)375 final, European Commission, Strasbourg, 29.05.2018, pp. 1-3.

a definition of „financial instrument" as a structure through which financial products are delivered, which is a further departure from the general meaning of the notion of a financial instrument. Moreover, the proposal also introduces other definitions within the realm of financial instruments, i.e.:

- "financial product" which means *equity or quasi equity investments, loans and guarantees*;
- "final recipient" which means *a legal or natural person receiving support from the Funds through a beneficiary of a small project fund or from a financial instrument*;
- "body implementing a financial instrument" which means *a body, governed by public or private law, carrying out tasks of a holding fund or of a specific fund*;
- "holding fund" which means *a fund set up by a managing authority under one or more programmes, to implement financial instruments through one or more specific funds*;
- "specific fund" which means *a fund, set-up by a managing authority or a holding fund, to provide financial products to final recipients*;
- "leverage effect" which means *the amount of reimbursable financing provided to final recipients divided by the amount of the contribution from the Funds*;
- "multiplier ratio" which *in the context of guarantee instruments, means a ratio between the value of the underlying disbursed new loans, equity or quasi-equity investments, and the amount of the programme contribution set aside as agreed in guarantee contracts to cover expected and unexpected losses from those new loans, equity or quasi-equity investments*;
- "management costs" which mean *direct or indirect costs reimbursed against evidence of expenditure incurred in the implementation of financial instruments*, and
- "management fees" which mean *a price for services rendered, as determined in the funding agreement between the managing authority and the body implementing a holding fund or a spe-*

cific fund; and, where applicable, between the body implementing a holding fund and the body implementing a specific fund[22].

With the introduction of these new definitions and concepts the issue of implementing financial instruments is to become easier to understand and less complicated to implement.

In the 2021-2027 period financial instruments are to be the main mechanism for the execution of investments that generate income and provide savings. The rules for their usage have been improved and updated to ensure better and easier implementation as well as a quicker set-up of instruments. Proposed legal solutions are supposed to bring about the following:

- Financial instruments will be better integrated into the programming and implementation process from the outset and the ex-ante assessment streamlined accordingly;
- Managing authorities will have the same basic flexible implementation options – management under the responsibility of the managing authority or direct management by the managing authority – but the related conditions have been simplified;
- Combination of EU resources will be possible under one set of rules; there will be no more multiplication of diverse rules applied to similar situations;
- Flexibility is proposed for the combination of grants with financial instruments;
- The eligibility rules have been clarified, and rules on management costs and fees have been simplified while keeping them performance based to encourage efficient management;
- The rules on payments have been considerably simplified while maintaining the all-important link between payments to financial instruments and the corresponding disbursements to final recipients;
- Reflows and fund recycling have been simply codified, to enable a smoother flow from one period to next;
- There will be no additional separate reporting on financial instruments as these are incorporated under the same reporting system as all other forms of finance.

22 Ibid., p. 27.

- Further simplifications include:
- The combination of different funds – and of financial instruments and grants – is codified in simple rules;
- There will no longer be specific rules for revenue generating investments;
- There will be no major project process (instead, strategic projects will be followed by the monitoring committee).
- Funding will be simplified, for example through the seal of excellence approach.
- Strengthening of provisions on business relocation in order to avoid wasteful subsidy competitions[23].

Lastly, it was recognized that financial instruments should support all types of new investments in line with the relevant policy objectives, thereby upholding the restriction on using financial instruments to support refinancing activities, such as replacing existing loan agreements or other forms of financing that have already been physically completed or fully implemented at the time of the investment decision.

The directions of the proposed changes are proper, however, how these changes are introduced in practice will verify the assumptions made.

Summary

Undoubtedly, the decision to launch financial instruments in the period of financial crisis in the form of preferential loans and credits should be assessed positively. Increasing the presence of such financial instruments in the implementation of cohesion policy may contribute to a more efficient use of public funds and economic growth across all Member States. The process of implementing public funds as repayable instruments is subject to detailed and complex EU and national legal regulations combining both public finance law, banking, public aid as well as the implementation of structural funds under cohesion policy. All these areas overlap and permeate, creating a complicated web of legal provisions for both public and banking institutions and final beneficiaries. What follows from these requirements as well as

23 Ibid., pp. 10-11.

from detailed EC guidelines is the fact that proposed products relate to selected types of projects, indicated in the ex-ante analyses as potential financial gaps. While the introduction of preferential financial products may meet with demand, the multitude of products offered by institutions and created specifically for the types of projects indicated in ex-ante analyses (also including the rules for granting them, the obligations regarding settlements and the extensive administrative requirements), may in the future prove to be of little interest to final beneficiaries, or even unavailable to many of them. Therefore, it is important to make every effort, basing on the past experiences, to improve and align the rules and regulations within this field.

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