advancing with ESIF financial instruments

Responding to the COVID-19 crisis through financial instruments

in the framework of the Coronavirus Response Investment Initiative

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Abbreviations

Abbreviation	Full name
CPR	Common Provisions Regulation
CRII/CRII Plus	Coronavirus Response Investment Initiative/Coronavirus Response Investment Initiative Plus
EAFRD	European Agriculture Fund for for Rural Development
EC	European Commission
EIB(G)	European Investment Bank (Group)
EIF	European Investment Fund
ERDF	European Regional Development Fund
ESIF	European Structural and Investment Funds
ESF	European Social Fund
EU	European Union
GGE	Gross Grant Equivalent
IFI	International Financial Institution
MA	Managing authority
MFF	Multiannual Financial Framework
NPBIs	National Promotional Banks and Institutions
SIH	Slovak Investment Holding
SMEs	Small and Medium-sized Enterprises
Temporary Framework	Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak

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This document aims at helping **the mobilisation of ESIF financial instruments, sometimes in combination with grants, to respond to the COVID-19 health crisis and its social and economic impact**. In this respect, ESIF financial instruments could have a role to play in ensuring the continued supply of affordable finance to individuals and businesses most affected by the crisis, and primarily in need of liquidity and working capital facilities to continue working/operating.

1. Amendments to the ESIF regulatory framework

The European Commission (EC) proposed, and the European co-legislators have approved, the amendments to the Common Provisions Regulation 1303/2013 (CPR) as well as to Regulations (EU) No 1301/2013 (ERDF Regulation) and No 508/2014, in order to rapidly mobilise ESI Funds in response to the COVID-19 health and economic crisis.

The first amending Regulation (EU) 2020/460 came into force on 1 April 2020 as part of the Coronavirus Response Investment Initiative (CRII), followed by a **second amendment, Regulation (EU) 2020/558, entering into force on 24 April 2020 as part of a follow on Coronavirus Response Investment Initiative Plus (CRII Plus) package. The paragraphs below summarise the amendments aimed specifically at the use of financial instruments.**

1.1 Ex-ante assessment

The requirement, under Article 37(2)(g) of the CPR, to review and update existing ex-ante assessments has been relaxed to allow existing financial instruments to be more quickly adapted to respond to the crisis. Therefore, CRII Plus no longer requires **review or update of the ex-ante assessments.**

A **simplified ex-ante assessment** under Article 37(2) CPR is still required where the managing authority decides to set up a **new** financial instrument as a crisis response. It is recommended that the analysis be **focused and short,** relying on existing EC publications and own estimates in relation to assessment of demand as a result of the COVID-19 outbreak. The simplified ex-ante assessment does not need to be outsourced and can be prepared quickly by the managing authority.

1.2 Support to working capital and related verifications

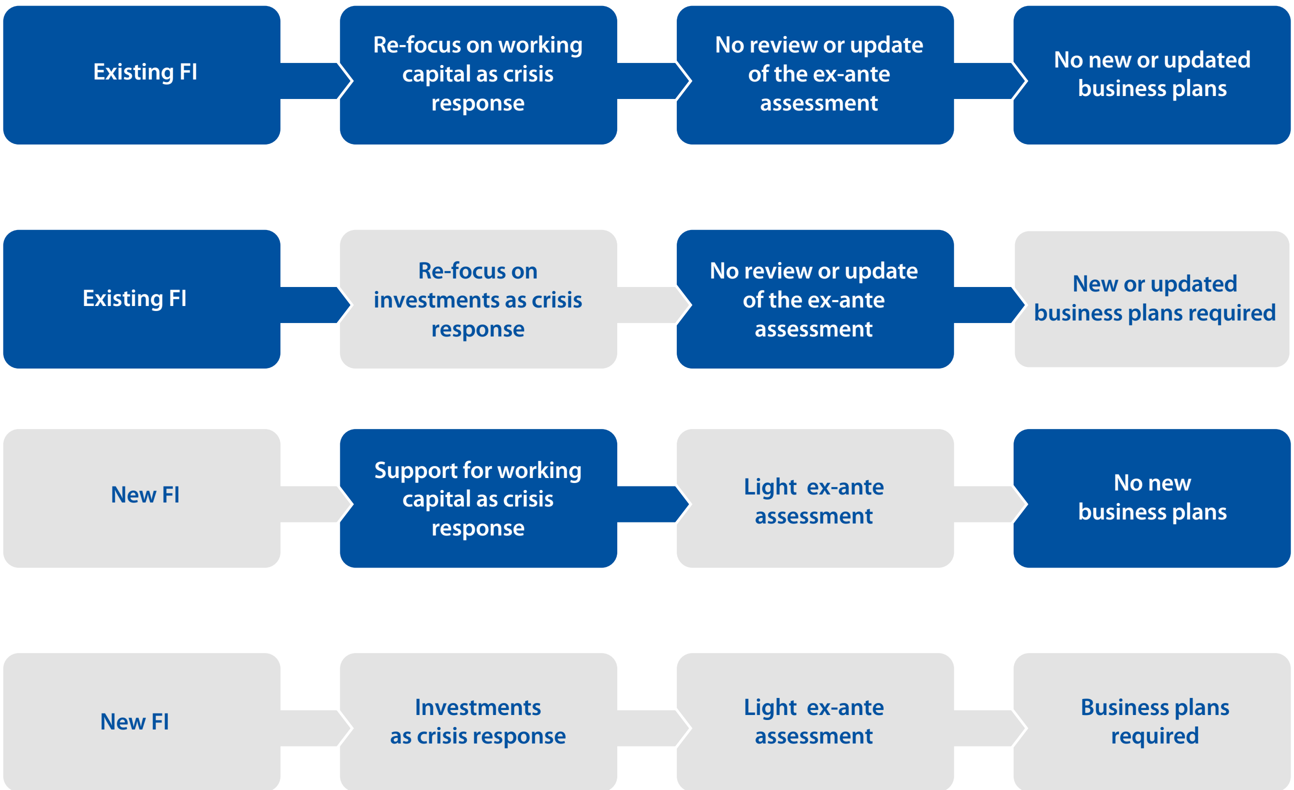
Working capital support for SMEs through financial instruments was already eligible under Article 37(4) of the CPR. The modifications introduced by CRII/CRII Plus enable ESIF financial instruments to **finance SME working capital easily and quickly** as an effective response to the public health crisis.

Any element of the working capital of the business may be supported. Such categories of expenditure may include, amongst others, the financing of payables for raw materials and other manufacturing inputs, including labour, taxes, inventories and overheads, rent, utilities, current debts, funding to finance trade receivables and non-consumer sales receivables.

When financial instruments provide support in the form of working capital financing, the CRII Plus **removes the requirement to provide, as part of the supporting documents, new or updated business plans** or equivalent documents. Evidence allowing verification that the support provided through the financial instruments was used for its intended purpose shall also not be required, so no management verifications or audits can be performed in this respect. However, all the other conditions have to be respected, which in the context of working capital support provided in the context of the coronavirus crisis, should focus on:

- whether the business had been affected by the public health crisis, as defined in national rules, when a given measure targets exclusively such expenditure in line with the amended Article 3(1) of the ERDF Regulation; and
- ensuring that no double financing regarding the same expenditure item is provided in case the SMEs are or have been supported also by other EU funded operations.

Figure 1: regulatory requirements for different implementation options for ESIF financial instruments



The expenditure for operations fostering crisis response capacities in the context of the COVID-19 outbreak shall be eligible as from **1 February 2020**. However, in case of ESIF financial instruments, the expenditure is eligible from the date the adequate amendments (if needed) are introduced in the funding agreements.

By way of derogation from Regulation (EU) No 1305/2013, **support in the form of stand-alone working capital may also be provided by the EAFRD** under measures referred to in Regulation (EU) No 1305/2013 and relevant to the implementation of financial instruments. Such eligible expenditure in this case shall not exceed EUR 200 000 and does not fall under the scope of Article 45(5) of Regulation (EU) No 1305/2013 on EAFRD rules for working capital, i.e., there is no need to link the working capital to any investment project.

1.3 Other relevant measures

The following provisions might also impact the implementation of financial instruments:

- **temporary relaxation of the requirement to co-finance EU resources**. A co-financing rate of 100% may be applied to payment for the accounting year starting 1 July 2020 and ending in 30 June 2021[1];
- full **flexibility to transfer** the 2020 resources for the 'Investment for growth and jobs' goal between ERDF, ESF and the Cohesion Fund. Resources transferred should be used in accordance with the rules of the receiving fund;
- full **flexibility to transfer ESIF between categories of regions** within a Member State for resources available for 2020 programming;
- an amendment to Article 139 CPR allows Member States to **retain ESIF annual pre-financing** as additional funding (otherwise any uncommitted pre-financing would have been recovered by the Commission);
- **postponed deadline for submission of annual implementation report**, including specific reporting on financial instruments, for the year 2019 until 30 September 2020.

The relaxation of the co-financing requirements and additional flexibility to transfer resources between funds is expected to allow for a more rapid deployment of available EU resources to priority sectors in response to the crisis. These measures will apply for a limited period, highlighting the need for managing authorities to mobilise the resources as quickly as possible.

In addition, CRII Plus provides for an **alignment of CPR rules for undertakings in difficulty** with the State aid rules applicable to operations covered by either the State aid Temporary Framework (see Section 2 below) or the *de minimis* Regulation.

1.4 Amendments to the Operational Programme

Managing authorities developing new measures to respond to the COVID-19 outbreak need to consider whether it is necessary to amend the Operational Programme (OP).

If the support for investment grants, working capital, interest rate subsidies fits into **the scope of the priority axis under the current version of the OP**, there would not be any need to modify the OP, but this must be verified in this specific case, as programme-specific conditions might need to be amended in order to cover such new actions. **Neither working capital nor the specific cost items have to be explicitly mentioned** in the description of the priority axis, but should fit into the scope of priority axes and types of projects. In such a case, expenditure is already eligible from 1 January 2014.

In case the programme needs to be amended (which is always the case under EAFRD) to extend eligibility to cover the working capital or to introduce a new financial instrument, expenditure for operations for fostering crisis response capacities in the context of the COVID-19 outbreak is eligible **as of 1 February 2020. This also applies to working capital granted to SMEs to provide an effective response to the public health crisis**. The necessary programme amendment **may be adopted later, without delaying deployment of measures**.

1 The applications for a given accounting year can be made until 31 July 2021, and starting from the submission of the last payment claim for the preceding accounting year, which is one of the days in July, depending on a programme and year.

2. Temporary Framework for State aid measures (Temporary Framework)

As a temporary measure in the context of the COVID-19 outbreak, the European Commission adopted on 19 March 2020 a Temporary Framework[2] to enable Member States to use the **full flexibility foreseen under State aid rules**. The Temporary Framework was amended on 3 April 2020[3]. It will be in place until the **end of December 2020**. The European Commission will assess before that date if the Temporary Framework needs to be extended.

The Temporary Framework allows for various forms of temporary interventions including (only the pertinent categories of aid for ESIF financial instruments are mentioned):

- direct grants, repayable advances, tax or payment advantages or other forms, such as a guarantee, loans, equity of a maximum amount **of EUR 800 000 per undertaking or EUR 120 000 for undertakings active in the fishery and aquaculture sector or EUR 100 000 for undertakings active in the primary production of agricultural products**[4];
- public **guarantees** on loans **at preferential premium**;
- **loans with subsidised interest rates**;
- aid for COVID-19 relevant **research and development**;
- investment aid for **testing and upscaling infrastructure** that contribute to develop COVID-19 relevant products;
- investment aid for the production of COVID-19 relevant products;
- aid in form of deferrals of tax and/or social security contributions;
- aid in form of wage subsidies for employees to avoid lay-offs during the COVID-19 outbreak.

Each of these categories of aid forms part of a specific section that includes the applicable compatibility conditions. In addition, the national temporary measures are subject to monitoring and reporting obligations, set out in Chapter 4 of the Temporary Framework.

2 Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak (OJ C 91I, 20.3.2020, p. 1).

3 First Amendment to the Temporary Framework to support the economy in the context of the coronavirus outbreak (OJ C 112I, 4.4.2020, p. 1). The second amendment of the Temporary Framework is underway: on 9 April 2020, the Commission sent to Member States the draft proposal to further extend the scope of the Temporary Framework to recapitalisation measures (see the official statement: https://ec.europa.eu/commission/presscorner/detail/en/STATEMENT_20_610).

4 In accordance with point (23) of the Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak. C(2020) 1863 final.

Two important points are to be highlighted:

- The aid under **the Temporary Framework can be cumulated notably with *de minimis* aid**. Provided the rules under the GBER and under the different *de minimis* Regulations are respected, the temporary aid measures covered by this Communication may be cumulated in line with the cumulation rules set out in the GBER and in the different *de minimis* Regulations, including Regulation (EU) No 1407/2013[5].
- This means that the EUR 800 000 direct grant may be cumulated with the EUR 200 000 *de minimis* support, to provide a total of EUR 1 million of support per undertaking, provided that both set of State aid rules are respected. Similarly EUR 100 000 direct grant allowance may be cumulated with the EUR 25 000 *de minimis* support in the agriculture sector. The cumulation of aid applies for a limited period since the Temporary Framework is only in place until the end of 2020.
- **Undertakings in difficulty are eligible to aid granted under the Temporary Framework,** as long as they were not in difficulty on 31 December 2019.

Furthermore, aid under the Temporary Framework may be cumulated with support under the ESI Funds provided that the maximum aid intensities indicated in the relevant State aid frameworks or those set in Annex II to Regulation (EU) No 1305/2013 are respected.

To support the use of the Temporary Framework following its amendment, the European Commission has published a consolidated version[6]. Managing authorities may use this document for information purposes, together, where required with the original text of legislation.

The European Commission has already approved a large number of State aid schemes, notified by Member States, under the Temporary Framework. The **decisions** are available on the dedicated page of the European Commission's competition website[7] (under 'Coronavirus related State aid decisions').

A managing authority, when considering to either modify an existing or to establish a new financial instrument, should check if such instrument might already fall within the scope of any approved national scheme, including those under the Temporary Framework. Designing the financial instrument in line with an approved scheme could save time in making the new or modified ESIF financial instrument operational. Alternatively, Member States may notify their own schemes under the Temporary Framework.

Further information can be found on the Commission webpage 'State aid rules and coronavirus'[8].

5 Commission Regulation (EU) No 1407/2013 of 18 December 2013 on the application of Articles 107 and 108 of the Treaty on the Functioning of the European Union to *de minimis* aid the Commission Regulation (EU) No 1408/2013 of 18 December 2013 on the application of Articles 107 and 108 of the Treaty on the Functioning of the European Union to de minimis aid in the agriculture sector and the Commission Regulation (EU) No 717/2014 of 27 June 2014 on the application of Articles 107 and 108 of the Treaty on the Functioning of the European Union to de minimis aid in the fishery and aquaculture sector.

6 Communication from the Commission Temporary Framework for State Aid Measures to Support the Economy in the current Covid-19 Outbreak (Consolidated Version).

7 https://ec.europa.eu/competition/state_aid/what_is_new/covid_19.html.

8 https://ec.europa.eu/competition/state_aid/what_is_new/covid_19.html.

3. Use of the public procurement framework to respond to the COVID-19 crisis

When using financial instruments in response to the COVID-19 outbreak, managing authorities need to take into account the public procurement provisions that are applicable to the related contractual arrangements (i.e. funding agreement, between the managing authority and the fund of funds/financial intermediary and/or between the fund of funds and the financial intermediaries).

The European Commission has published a Communication[9] (the Communication) outlining the tools available to public procurers to respond to the COVID-19 crisis. The Communication does not introduce new rules or flexibilities with respect to the rules in the Public Procurement Directive[10] (the Directive), but **provides guidance as to the interpretation of the exceptions already provided for in the Directive, taking into account current crisis circumstances**. It features, amongst other measures, the potential application of the **accelerated open procedure** or **the negotiated procedure without prior publication of a notice,** to enable implementation of urgent measures.

When implementing COVID-19 response measures, public procurers must determine whether this can be done by a **modification of an existing funding agreement**, in accordance with **Article 72 of the Directive**, or through a **new procedure using the flexibilities highlighted in the Communication** and mentioned above. Managing authorities should undertake their own analysis and assessment of which procedure is appropriate, having regard to the nature of the proposed action. Given the unprecedented nature of the current crisis, and the severe potential impact on EU businesses, however, the need for immediate action justifies the consideration of appropriate measures to ensure actions are implemented with minimum delay.

Adopting a non-selective approach[11] to implementing a financial instrument provides **a further option** for the rapid implementation of financial instruments through a **'Call for Expressions of Interest' outside the scope of the public procurement rules**. This approach was recently adopted in Slovakia by the NPBI Slovak Investment Holding (SIH) and is featured in the **mini-case study at Appendix 1** of this factsheet. By designing the instrument to fall outside the scope of the Directive, SIH were able to implement the guarantee instrument so that the first guarantee agreements were signed with participating banks within a month of the Call for Expressions of Interest being issued.'

Managing authorities also have the possibility to **directly award contracts** to a body implementing financial instruments supported through ESIF. A direct award may be made if such body is either: the European Investment Bank (EIB), European Investment Fund (EIF) or other International Financial Institution (IFI) (and thus falls outside public procurement rules); or based on the exceptions of the Directive (Article 12), a National Promotional Bank or Institution (NPBI), based on the clarifications in Article 38(4) of the Omnibus Regulation.

9 Communication from the Commission, Guidance from the European Commission on using the public procurement framework in the emergency situation related to the COVID-19 crisis (2020/C 108 I/01).

10 Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC.

11 Following the decisions of the ECJ in *Falk Pharma*, Case C-410/14 and *Tirkkonen*, Case C-9/17.

4. Implementing options utilising ESIF to support financial instruments in response to the COVID-19 crisis

The flexibilities introduced by CRII/CRII Plus and the Temporary Framework provide managing authorities and their partners with a number of options to use ESIF financial instruments as part of their response to the COVID-19 outbreak. In the following sections, a number of the key opportunities are presented for consideration as follows:

- Section 5 – the **use of existing ESIF financial instruments** to quickly mobilise finance in support of businesses during the current crisis. This could include supporting companies experiencing liquidity and related financial difficulties or those companies in sectors where demand has significantly increased and are seeking finance to expand their capacity;
- Section 6 – the **implementation of new financial instruments** in response to the crisis. These could include either guarantee or risk sharing loan instruments that, in light of the regulatory novelties described in Section 1, could potentially be rapidly implemented;
- Section 7 – the **combination of existing or new financial instruments with grants**, including in the form of interest rate or guarantee fee subsidies and grants for working capital support; and
- Section 8 – other measures including the development of a **stand-alone grant support programme** to provide grants, including for interest rate subsidies and/or capital/investment grants to help alleviate liquidity and/or working capital constraints on non-ESIF funded loans (including those provided by EIB Group, other IFIs, NPBIs or private sector banks).

Each of these options is considered in further detail in the following sections.

5. The use of existing ESIF financial instruments to quickly mobilise additional financing

The **relaxation of the requirement to review and update the ex-ante assessment** prior to modifying financial instruments should allow managing authorities to **quickly adapt existing financial instruments** to respond to current financing needs in their local economy. In this way they may be able to take advantage of financial instrument structures already procured/set up. The package of support could include measures to support **existing and/or additional final recipients** that are experiencing liquidity and/or working capital constraints. Businesses in sectors such as medical supplies, logistics, tourism and research and development could also be targeted for support by extending the range/scope of existing instruments.

Additional ESIF resources may be contributed to financial instruments and funding agreements amended to respond to the crisis (subject to Article 72 of the Directive). Examples of how existing instruments might be re-purposed or expanded include:

- introducing **new eligible investments** not initially foreseen, but now needed and included in the funding agreements following the CPR legislative amendments (e.g. by now allowing for the funding of working capital or targeting new categories of final recipients);
- (re)designing financial products, such as:
  - loans that could provide **bridge financing** to SMEs, individual entrepreneurs and/or other targeted businesses (including micro enterprises, social enterprises and larger businesses), financing working capital and other short term liquidity needs;
  - amended guarantees with **increased coverage of risk** (for example with an increased portfolio cap rate) to enable financial intermediaries to provide more support to final recipients, for example through repayment holidays, extending repayment periods of current outstanding loans to final recipients and extending additional credit to include additional working capital needs of their borrowers; and
  - equity investments to enable businesses to increase their access to capital without taking on additional debt or for financing a new growth opportunity area of the business (including in health care, digitalisation or research and development);
- **combining a grant** with an existing financial instrument in one financial instrument operation or in two operations respecting the rules on combination in line with Articles 37(7)-37(9) of the CPR. Grants may take the form of either investment grants for non-revenue generation part of the investment or grants for working capital (as a stand-alone operation) or interest rate/guarantee fees subsidies or technical support;
- **modifying the terms and conditions of the financial instrument's products**, both to outstanding products and to newly disbursed ones, thus easing requirements and/or conditions attached to the financial product.

Using the above and other measures, managing authorities can develop a specific package of support tailored to meet the needs of the final recipients of existing ESIF financial instruments. In designing the measures, the **flexibilities under the Temporary Framework** may also be used, including **national crisis State aid schemes that have already been approved by the Commission**. Where a national scheme is not notified, the **fast track procedure** provided by the Commission in this regard may be used to secure approval to measures compatible with the Temporary Framework.

6. Implementation of new ESIF financial instruments

Additional ESIF resources may be used to set up **new financial instruments** in support of new loans and other financing of businesses during the current crisis period.

6.1 Guarantee financial instrument

Using the flexibilities in the Temporary Framework, a straightforward guarantee product could be developed and implemented relatively quickly to **mobilise additional resources from public and private banking institutions**. The managing authority's contribution to financial instruments like these can, in accordance with CRII Plus, be **funded entirely from ESIF resources, without the need for national co-financing**.

Examples of **flexible** financial products available in the market, that could also be supported by guarantees, to respond to the crisis conditions include:

- Loans with flexible/conditional duration, giving the possibility for the borrower to extend the loan duration depending on certain conditions.
- Loans with flexible repayment schedules (option to suspend instalments for a limited period, or to change the repayment frequency, e.g. from monthly to quarterly).

The implementation of the guarantee could follow one of the public procurement options outlined in the Communication on public procurement. Alternatively, where the guarantee is designed to be made available to all financial institutions that meet minimum criteria **on a non-selective basis**, the implementation may take place outside the scope of the Directive[12].

The Slovakia mini-case study at Appendix 1 shows how a guarantee instrument can be quickly implemented to respond to the COVID-19 outbreak. In this case the NPBI, Slovak Investment Holding (SIH), implemented the guarantee instrument before the CRII, CRII Plus and Temporary Framework were adopted. The additional flexibilities under recent legislation should increase the scope to rapidly implement this type of financial instrument to support businesses during the current crisis.

The Temporary Framework allows for two options for ensuring State aid compatibility, depending on the size of the underlying loan. For **guarantees on small loans, in the limit of EUR 800 000 in nominal value, section 3.1** of the Temporary Framework (as amended on 3 April 2020[13]) could be relied on for State aid clearance.

12 Following the decision of the European Court of Justice in the case Falk Pharma (Case C-410/14).
13 Communication from the Commission, Amendment to the Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak C(2020) 2215 final.

For **larger nominal amounts of loans, section 3.2** (applicable to guarantees on loans) of the Temporary Framework, completed by **Section 3.4 thereof** (applicable to guarantees and loans channelled through credit institutions or other financial institutions), provides for possibilities of both **a vertical guarantee and a first loss piece guarantee.** A vertical guarantee is a guarantee where risks are shared between the guarantor and the financial intermediary proportionately and under the same conditions, and where the public guarantee can cover maximum 90% of the underlying loans. A first loss piece guarantee to be absorbed by ESIF can be up to a maximum of 35% of the loan principal. Where the aid is provided in an intermediated manner the provisions of Section 3.4 of the Temporary Framework apply as well. In such a configuration a pass-on mechanism has to be put in place to ensure that the intermediaries are passing on the benefit of the measure to the final recipients to the largest extent possible (i.e. through higher volumes of financing, riskier portfolios, lower collateral requirements, lower guarantee premiums or lower interest rates).

Aid under the Temporary Framework, granted under the form of a guarantee, may be cumulated, in line with the cumulation rules, set out in the General Block Exemption Regulation[14] (GBER) and in the different *de minimis* Regulations, provided also that the cumulation as well as the other conditions of these regulations are fulfilled.

As with the previous examples, **grants might also be used in combination** with the guarantee to enhance/improve the affordability of the underlying loans. For instance, a short-term loan could serve the purpose of funding additional working capital requirements (for example to maintain production or supply of raw materials). At the same time, a grant might also be provided, alongside or together with the financial instrument, to support businesses with more immediate liquidity needs, for example to pay staff salaries (and other costs which cannot be supported by a company's capacity to borrow).

6.2 Risk sharing loan financial instrument

Funded loan schemes can help provide much needed liquidity to final recipients and leverage co-financing from financial intermediaries, while sharing with them the underlying risk on a portfolio of loans to final recipients. The level of co-financing from intermediary(ies), to ensure that interests of managing authorities and financial intermediaries are aligned, would depend on market financing conditions and the appetite of the intermediaries to provide this complementary financing.

In order to provide conditions that are even more favourable to final recipients, **the intermediary's co-financing component may also then benefit from an interest rate subsidy**, funded by ESIF resources, so as to make the overall funding package to final recipients effectively 'interest free'.

14 Commission Regulation (EU) No 651/2014 of 17 June 2014 declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty.

Practical example

A managing authority wants to support entrepreneurs and social enterprises that are providing increased healthcare services linked to the COVID-19 emergency. The aid package might be composed of:

- loans for EUR 100 000, 10-years tenor at 1% annual interest rate (composed of EUR 50 000 from ESIF resources at 0% interest rate and EUR 50 000 from financial intermediaries' own resources at 2% p.a. interest rate),
- a grant support of EUR 30 000 per final recipient for the purchase of healthcare equipment or for employing additional (or retaining existing) staff;

With EUR 10 000 000, the managing authority could support approximately 125 final recipients (being a financial instrument amount of EUR 6 250 000 and a capital grant element of EUR 3 750 000). The managing authority could provide an additional interest rate subsidy and cover the entire amount of the interest, for example, payable on the loan for first year. Assuming no capital repayment in that first year, this would amount to an interest rate subsidy of EUR 1 000 (EUR 50 000 * 2% p.a.) per final recipient (and EUR 125 000 in total for 125 final recipients).

All the other rules on combination between grants and financial instruments apply (e.g. distinct eligible expenditure, grants shall not be used to reimburse support received from financial instruments and vice-versa, etc.).

Regarding the selection process of the bodies implementing the financial instrument, the managing authority could also potentially benefit from the accelerated procedures outlined by the Communication on public procurement, namely:

- **shortened deadlines for open procedure and restricted procedure**, in case of urgency; or
- **negotiated procedure without prior publication of a notice**, in cases of extreme urgency.

The managing authority could implement the scheme under **Section 3.1** of the Temporary Framework for small loan amounts, **where the nominal value of the loan does not exceed EUR 800 000**. The Temporary Framework does not contain any restriction with respect to maturity, interest rate or collateral, so the loans can be provided at very preferential terms.

For **larger nominal amounts of loans, sections 3.3** of the Temporary Framework (applicable to subsidised interest rates for loans) **and 3.4 thereof** (applicable to guarantees and loans channelled through credit institutions or other financial institutions), could be relied on, aligning the interest rate to the rates at section 3.3 of the Temporary Framework. Where it is provided in an intermediated manner, in accordance with Section 3.4, applicable in relation to aid granted in the form of subsidised interest rate for loans, pursuant to Section 3.3, a pass-on mechanism has to ensure that the intermediary passes on the benefits to the final recipients to the largest extent possible.

Alternatively, the managing authority may consider implementing the scheme under **the *de minimis* Regulation**. In this case, the GGE of the discounted loan would need to be included in the calculation of the total amount of *de minimis* aid received per final recipient or the loan amount would need to comply with the maximum amount provided for in the regulation.

Aid under the Temporary Framework, granted in the form of a loan, may be cumulated, in line with the cumulation rules, set out in the GBER and in the different *de minimis* Regulations, provided also that the other conditions of these regulations are fulfilled, including those on cumulation.

For the same underlying loan principal, aid granted under section 3.2 and section 3.3 of the Temporary Framework cannot be cumulated. Aid granted under section 3.2 and section 3.3 may be cumulated for different loans provided the overall amount of loans per beneficiary does not exceed the ceilings set out in point 25(d) or in point 27 (d) of the Temporary Framework.

7. Combination of existing or new ESIF financial instruments with grants

Existing or new ESIF loan, guarantee or equity instruments set up to respond to the COVID-19 outbreak may also take advantage of the existing options under Articles 37(7) and (8) for **combining financial instrument support with grants**. As indicated in the examples given above grants in the form of interest rate or guarantee fees subsidies and/or grants for working capital and investment might be combined with loan, guarantee or equity instruments as part of a combined response to meet the needs of businesses in the Member State.

Table 1 shows the implementation options for managing authorities seeking to combine grants with existing or new ESIF financial instruments as part of their response to the COVID-19 outbreak.

Table 1: combination of grants with existing or new ESIF financial instruments

Type of support	Existing or new ESIF supported financial instruments	Implementation
Interest rate/ guarantee fee subsidies	√ Interest/guarantee fees payable for both existing and new loans or guarantee commitments respecting the conditions of State Aid notification under Temporary Framework if applicable	Implementation: • a combined financial instrument/grant operation under Art 37(7) CPR through amendment of existing funding agreement • separate grant operation (ERDF Regulation 3(1) CPR CRII amendment) based on Art. 125 CPR, being either: – an arrangement under which the financial intermediary would be the beneficiary of a grant on terms consistent with Article 2(10)(a) CPR (as amended by the Omnibus Regulation[14]) providing cash to or for the benefit of final recipients where the aid per undertaking is below EUR 200 000; or – individual grants to final recipients, managed by the MA or by the intermediate body.
Grants for Working capital	√ where the business had been affected by the public health crisis, as defined in national rules, when a given measure targets exclusively such expenditure in line with the amended Article 3(1) of the ERDF Regulation; expenditure eligible after date of grant agreement or as of the date of the crisis response package, or according to the date(s) in line with the State Aid notification under Temporary Framework.	Separate grant operation (ERDF Regulation 3(1) CPR CRII amendment) based on Art. 125 CPR, implemented through: • an arrangement under which the financial intermediary would be the beneficiary of a grant on terms consistent with Article 2(10)(a) CPR (as amended by the Omnibus Regulation) providing cash to or for the benefit of final recipients where the aid per undertaking is below EUR 200 000; or • individual grants to final recipients managed by the MA or by the intermediate body. In the context of grants for working capital, it has to be ensured that: › grants from ESI Funds are not used to reimburse support received from ESIF financial instruments › the related expenditure declared in a payment application is not declared for support from another Fund or Union instrument, or for support from the same Fund under another programme.

15 Regulation (EU, Euratom) 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union, amending Regulations (EU) No 1296/2013, (EU) No 1301/2013, (EU) No 1303/2013, (EU) No 1304/2013, (EU) No 1309/2013, (EU) No 1316/2013, (EU) No 223/2014, (EU) No 283/2014, and Decision No 541/2014/EU and repealing Regulation (EU, Euratom) No 966/2012.

Type of support	Existing or new ESIF supported financial instruments	Implementation
Investment grants	√ expenditure possible as a separate grant operation for example where a grant is needed for a non-revenue generating part of the investment; expenditure eligible after date of grant agreement or as of the date of the crisis response package.	Separate grant operation (ERDF Regulation 3(1) CPR CRII amendment) based on Art. 125 CPR implemented through: • an arrangement under which the financial intermediary would be the beneficiary of a grant on terms consistent with Article 2(10)(a) CPR (as amended by the Omnibus Regulation) providing cash to or for the benefit of final recipients where the aid per undertaking is below EUR 200 000; or • individual grants to final recipients managed by the MA or by the intermediate body. In the context of investment grants, it has to be ensured that: › grants from ESI Funds are not used to reimburse support received from ESIF financial instruments › the related expenditure declared in a payment application is not declared for support from another Fund or Union instrument, or for support from the same Fund under another programme.

8. Other measures – interest rate subsidies and grants for working capital or investment grants provided alongside non ESIF supported financial instruments

As an alternative to the direct use of ESIF resources as financial instruments, managing authorities may **support bigger, non ESIF supported loan portfolios of public and/or private financial institutions** (including EIB, NPBIs and other IFIs), **by providing grants in the form of either interest rate subsidies, grants for working capital or investment grants** to the existing loan recipients.

An interest rate subsidy and/or working capital or investment grant could be disbursed by the managing authority in two possible ways as follows:

- **a grant may be given to the financial institutions** for a scheme, for example to subsidise the interest payable on loans that have been (or will be) disbursed (and have to be paid back in the future). This can be done as a normal grant operation implemented by a beneficiary /beneficiaries selected by the managing authority in accordance with Article 2(10)(a) CPR (as amended by the Omnibus Regulation). The **financial institutions would be the grant beneficiaries** and they would have to demonstrate that they used the grant for the **purpose of writing off interest payment obligations of SME borrowers**; or
- **a grant scheme to fund final recipients** (SMEs) to enable them to pay, for example the interest on loans that have been (or will be) disbursed (and have to be paid back in the future). This can be done either as a grant operation by the managing authority where **the SME borrowers are grant beneficiaries,** or through a grant mechanism where a **fund of funds/NPBI is the grant beneficiary** in accordance with Article 2(10)(a) CPR (as amended by the Omnibus Regulation) and distributes small amounts of grants to the SME borrowers.

In all cases the implementation of the grant schemes should be implemented based on Article 125 CPR, in line with usual practice for grant schemes. For example, the grant beneficiaries may be required to reply to a Call issued by the managing authority for the grant and the grant will be distributed based on the selection criteria published in the Call. Table 2 shows the different implementation options for managing authorities seeking to use ESIF grant to support non ESIF/EU lending as part of their response to the COVID-19 outbreak.

Table 2: implementation options for ESIF grant in support of non-ESIF/EU lending

<table>
<tr><th></th><th>Existing and new non ESIF/EU supported loans/guarantees/equity</th><th>Implementation</th></tr>
<tr><td>Interest rate/ guarantee fee subsidies</td><td>√
Interest/guarantee fees payable for both existing and new loans or guarantee commitments respecting the conditions of State Aid notification under Temporary Framework if applicable</td><td rowspan="3">Separate grant operation (ERDF Regulation 3(1) CPR CRII amendment) based on Art. 125 CPR implemented through:
• an arrangement under which the financial intermediary would be the beneficiary of a grant on terms consistent with Article 2(10)(a) CPR (as amended by the Omnibus Regulation) providing cash to or for the benefit of final recipients where the aid per undertaking is below EUR 200 000; or
• individual grants to final recipients managed by the MA or by the intermediate body.

All the above support and their combination shall not lead to exceeding the applicable aid intensity under the relevant State aid frameworks or those set in Annex II to Regulation (EU) No 1305/2013.</td></tr>
<tr><td>Grants for Working capital</td><td>√
where the business had been affected by the public health crisis, as defined in national rules, when a given measure targets exclusively such expenditure in line with the amended Article 3(1) of the ERDF Regulation;

could also be used e.g. to finance payments of the principal part of a loan due or past due (current liabilities), where such a loan was not supported by EU budget in the past;

expenditure eligible after the date of grant agreement or as of the date of the crisis response package, or according to the date(s) in line with the State Aid notification under Temporary Framework</td></tr>
<tr><td>Investment grants</td><td>√
separate grant operation where a grant is needed for a non-revenue generating part of the investment;

expenditure eligible after date of grant agreement or as of the date of the crisis response package.</td></tr>
</table>

This type of support could be **combined with a targeted loan product**, including intermediated lending for example from the recently announced COVID-19 liquidity support package of the European Investment Bank Group. Supporting businesses by meeting the short-term borrowing costs would allow undertakings to access finance that would be designed to provide longer-term support as the economy recovers.

Appendix I – Mini Case Study: SIH Anti-Corona Guarantee

This mini case study focuses on the Financial Instrument 'SIH Anti-Corona Guarantee' recently launched in Slovakia to help alleviate economic hardships faced by SMEs as a result of the measures to contain the spread of COVID-19. It is one of the first products introduced by National Promotional Banks and Institutions (NPBIs) in the EU after the outbreak of COVID-19, which employs European Structural and Investment Funds (ESIF) and may also eventually make use of some of the innovative features enabled by the simplified regulatory framework for financial instruments. As such, it can hopefully serve as inspiration also for managing authorities (MAs) and NPBIs in other Member States too.

1. Introduction

Slovak Investment Holding (SIH) has recently launched a new financial instrument for small and medium-sized enterprises (SMEs), to help support them through the period of difficulties caused by the necessary health and safety measures to contain the spread of the coronavirus. The programme is funded using ESIF, from the Operational Programme 'Integrated Infrastructure' and the national budget of the Slovak Republic.

The purpose of the instrument is to enable financial institutions to extend favourable-term bridging loans to SMEs. The principal objective of the instrument is to help SMEs overcome financial difficulties caused by the COVID-19 crisis and help preserve existing jobs. All the benefits ensuing from this financial instrument (in particular reduced interest rates and reduced collateral requirements) must be fully passed onto the target SMEs.

The financial instrument consists of a portfolio guarantee for financial institutions and an interest subsidy of up to 4% p.a. for those enterprises that manage to preserve existing jobs. By means of said financial instrument, the SIH will shoulder a part of the financial institutions' credit risk resulting from a portfolio of new loans to the SMEs negatively affected by the current situation. The instrument is expected to facilitate the provision of new bridging loans with maturity of no more than four years (including a 12-month grace period on both the principal and interest) and up to almost EUR 1.2 million per loan. Thanks to the SIH Anti-Corona Guarantee, and the combined interest rate subsidy, it is expected that the loans may be provided interest-free to final recipients to cover both their investment and operating costs in order to preserve employment.

The total amount of funds currently allocated to the SIH Anti-Corona Guarantee is EUR 38 million; however, with a view to the ongoing negotiations between the SIH and the Ministry of Economy, as well as the measures recently announced by the Slovak Government, a significant growth in the overall volume of funds allocated to this financial instrument is expected[16]. For this reason, the financial instrument was designed in a way to enable possible increases to the allocation to the participating financial institutions. Draft guarantee agreements contain clauses enabling the participating financial institutions to request a guarantee top-up in the event that 70% of the loan portfolio covered by the guarantee has been created, and subject to SIH having secured additional financial resources.

16 As of the end of April, SIH has secured additional EUR 57 million for this financial instrument and a soft commitment from the relevant managing authority that further resources will be made available if needed.

2. Key parameters of the financial instrument

2.1 Development of the financial instrument

The SIH Anti-Corona Guarantee was rapidly prepared in March 2020 with ESIF from the 2014-2020 programming period. The design of the instrument therefore pre-dated amendments to the Common Provisions Regulation (Regulation (EU) No 1303/2013) that were adopted on 2 April[17]. The need for a formal ex-ante assessment was therefore taken into account and the CPR requirements in this respect were met by the ex-ante assessment contracted by the Slovak Ministry of Finance (prepared by EIB in 2014, and updated in 2017). The gap identified at the time was deemed further exacerbated by the economic difficulties resulting from the measures adopted in Q1 2020 to contain the spread of COVID-19.

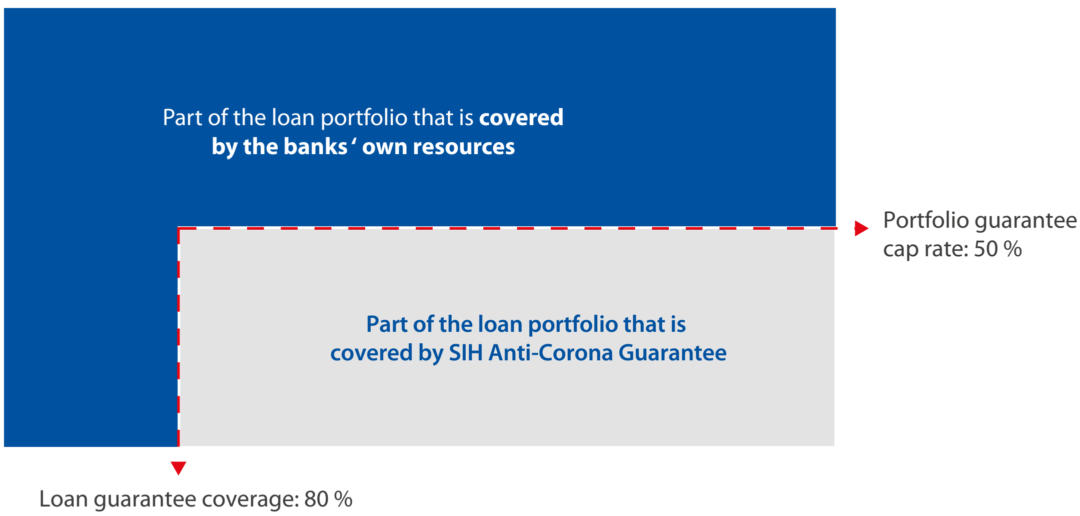
2.2 Description of the financial instrument

The instrument includes two components structured as a single operation:

- SIH Anti-Corona Guarantee (First Loss Portfolio Guarantee); and
- Interest rate subsidy, i.e. partial or full interest refund on loans provided by participating financial institutions.

Guarantee parameters: An 80 % guarantee coverage on individual loans (with maturities between 3 and 4 years) and a 50 % guarantee cap rate on the portfolio of underlying loans.

Figure 2: the SIH Anti-Corona Portfolio Guarantee



Setup of the guarantee: The SIH provides the guarantee in line with the parameters described above. Based on the guarantee, each financial institution shall create and administer a portfolio of new loans guaranteed by SIH. The guarantee shall cover credit risk at the level of individual loans as well as at the level of the entire loan portfolio. This allows for more favourable financing conditions to be provided by the financial institutions to the target SMEs. Throughout the entire loan period, loans that are covered by the guarantee must comply, *inter alia*, with the following eligibility criteria:

17 https://ec.europa.eu/info/sites/info/files/european_structural_and_investments_funds.pdf.

- The loans must be new, i.e. it is not permitted to refinance or restructure existing loans;
- The loans must not be used to finance operations/investments that have been physically completed or fully implemented before submitting a loan application;
- The loans must not be used to finance financial activities, the development of real estate property as a financial investment, or to provide consumer loans.

Funds shall be earmarked and deposited in an escrow account with the State Treasury (Štátna pokladnica), for the sole use of settling guarantee claims from the participating financial institutions. In case of an individual loan default, the participating financial institution shall receive funds in the amount of the guaranteed portion of the defaulted loan, while simultaneously commencing recovery of the defaulted loan from the liable SME. The transfer of the guarantee payment shall be executed by SIH to the financial institution within 30 days of delivering an authorised settlement request.

Interest rate subsidy: Up to 4% p. a.

Setup of the interest rate subsidy: The interest rate subsidy shall reduce the interest paid by SMEs to participating financial institutions. This form of the support is designed for the benefit of SMEs, but it shall not be disbursed to them directly.

The SME's claim to the interest rate subsidy arises after the financial institution verifies that the beneficiary SME has met the following conditions:

- The beneficiary SME's workforce was not reduced, compared to the previous period;
- The beneficiary SME is not or did not fall in arrears on its social and healthcare contributions, or has reduced the arrears as a result of the loan being used for other eligible activities.[18]

The conditions must be complied with by the beneficiary SME and verified by the financial institution 12 months after the first drawing of the loan. If the conditions are met, the subsidy applies to the entire loan period, including for the initial 12 months. In such case, SIH makes a payment to the financial institution to cover the interest rate subsidy. If conditions are not met, the interest rate subsidy is not applied to the SME and the financial institution charges the relevant part of the interest rate to the SME, including for the initial 12 months period.

2.3 Description of the combined financial product for SMEs

Combined financial product: Provision of low- to zero-interest rate loans to SMEs (interest rates between 0% and 2% p.a. are envisaged). The loans shall take the form of a fixed amortisation instalment schedule or a revolving loan. The loans must not take the form of a mezzanine loan, subordinated debt or quasi equity.

Maximum amount of each loan: EUR 1 180 000.
Minimum maturity: 3 years (36 months), including the grace period.[19]
Maximum maturity: 4 years (48 months), including the grace period.
Grace period for the principal and interest payments: 12 months from the date of the loan first being drawn.[20]
Collateral requirements: None.

18 For the avoidance of doubt, the guaranteed loans cannot be used directly to settle such arrears.
19 In case of revolving loans, the minimum maturity is 12 months.
20 In case of revolving loans, grace period on principal and interest payments is not applicable. Neither is the interest rate subsidy.

Interest rate: The financial institutions' loan margins shall be reduced by 50% based on the provided guarantee. Subsequently, the interest rate is reduced by up to 4% p. a. (limited to the interest rate applied taking account of the guarantee). The subsidy is applied only to the extent that a 0% interest rate is achieved. SIH expects that overall, this financial instrument should help bring the final interest rate charged to target SMEs down to between 0% and 2% p. a.

The fees for providing the loan, increases, prepayments and loan guarantee should not be charged. Other fees are to be charged and determined in accordance with the standard fee schedules of the particular financial institution.

Expected leverage effect[21]: Minimum of 2.5 : 1

2.4 Distribution key for allocation to individual financial institution applicants:

The total resources available will be distributed between the participating financial institutions in accordance with the following formula:

(a/b)*c

Where:
a = Outstanding principal balance for SMEs loans of the particular financial institution as at 31 December 2019,
b = Cumulative outstanding principal balance for SMEs loans of all participating financial institutions as at 31 December 2019,
c = Total allocation for the cash collateral to cover losses from defaulted loans, i.e. the guarantee amount.

The minimum possible allocation per individual financial institution is EUR 1 million[22].

Draft guarantee agreements leave room open for additional guarantee allocations to participating financial institutions, in line with the 'distribution key' outlined above.[23]

2.5 Eligible SMEs

- Must be incorporated in the Slovak Republic and pursue their business activities on its territory;
- Must comply with the definition of 'small and medium-sized enterprises' as defined in applicable EU legislation;[24]
- Must pursue their business activities in the territory of the Slovak Republic, in any of its regions;

21 Being the ratio between the total amount of newly-extended, guaranteed loans and the amount of the guarantee (which employs both the ESIF and the state budget funds); in other words, every EUR 1 of provided guarantee should lead to the extension of at least EUR 2.5 in new loans.

22 If the formula indicates less than EUR 1 million for financial institution(s), then allocation in a minimum amount of EUR 1 million is made to such institution(s). As a next step, the formula is applied again, this time ignoring the SMEs loan volumes from financial institution(s) with EUR 1 million allocation(s) and the guarantee amount (c) being reduced by the minimum allocation(s) made in the previous step.

23 Once a financial institution absorbs 70% of the initially allocated guarantee, it can request an additional allocation. SIH, subject to having secured additional resources at that point, may allocate additional funding to such a financial institution in the amount, which represents the larger of: 50% of the financial institution's initial allocation; and EUR 1 million.

24 As defined by Commission Recommendation 2003/361/EC on micro, small and medium-sized enterprises.

- Must not belong to the strongest credit risk rating category according to the participating financial institution's internal rating evaluation;[25]
- Must not be subject to any procedure initiated by the European Commission aimed at returning previously provided support on the grounds of irregularities;
- Must not have any history of being convicted for crimes related to their professional conduct, including fraud, corruption, participation in an organised crime group or any other illegal activities that are harmful to EU financial interests;
- Must not be subject to any lawful decision that would sanction them for violating any legal statutes forbidding illegal hiring of third country nationals.

2.6 Eligible use of extended loans

- Procurement of material and non-material property required to maintain or increase the number of jobs, including transfer of ownership rights in SMEs (e.g. purchase of new machinery/technologies/licences, renovation of buildings, etc.) as well as working capital complementary to such procurement;
- Working capital required to preserve or increase the number of jobs and to establish, strengthen or extend business activities of the beneficiary SME (e.g. purchase of supplies/ goods/services/utilities, etc.);
- Working capital required to preserve or increase the number of jobs in order to support special treatment of disadvantaged social groups and implement socially oriented measures (e.g. preservation of jobs, etc.);
- Working capital necessary to support SMEs with limited access to capital due to events and developments that are outside of their control.

2.7 State aid scheme

The aid provided within this financial instrument will be in compliance with *de minimis* conditions as set out in Regulation (EU) No. 1407/2013 and Articles 107 and 108 of the Treaty on the Functioning of the European Union with respect to *de minimis* aid. The *de minimis* aid scheme that governs this financial instrument was published on SIH website[26] after having been approved by the Antimonopoly Office of the Slovak Republic.

This State aid scheme was selected as SIH has implemented a First Loss Portfolio Guarantee instrument in the past and had an existing applicable and approved *de minimis* scheme. As a result, SIH decided to prepare a new *de minimis* scheme, which would be similar to the previously approved one, in order to speed up the process of having the new scheme approved by the Antimonopoly Office.

The scheme was already prepared and under review by the Antimonopoly Office by the time the Communication from the European Commission - Temporary Framework for State aid measures to support the economy in the current COVID-19 outbreak - was published. Furthermore, given that the ESIF resources used to implement the SIH Anti-Corona Guarantee were restricted for SMEs, the decision was taken to implement the financial instrument with the *de minimis* scheme under preparation. The Temporary Framework for State Aid was identified as a possible state aid regime to be used in the event SIH receives additional funding and increases the size of the guarantee amount.

25 The instrument is not designed to support lower risk/safest SMEs.

26 https://www.sih.sk/en/aktuality/sih-anti-corona-guarantee-to-help-small-and-medium-sized-businesses.

2.8 Participation of financial institutions

The SIH Anti-Corona Guarantee is designed to be a remuneration-free financial instrument. This means that SIH will not pay any management or performance fees to the financial institutions that will participate in this instrument. Moreover, the participating financial institutions are not providing a service to the SIH, as the guarantee is used to support SME lending operations in line with standard banking practice. SIH has provided access to this financial instrument to every eligible financial institution and there is no rating of individual applications, nor selection from among them. Every financial institution that submits an expression of interest, which SIH assesses to be in compliance with the Call requirements, including with requirements stipulated in Article 7 of the Commission Delegated Regulation (EU) No. 480/2014, is offered an opportunity to sign the guarantee agreement and participate in the implementation of the financial instrument. No contractual negotiations are to be held before signing of the guarantee agreements. For these reasons, SIH has, with the support of their legal advisers, concluded that the implementation of this financial instrument is not subject to the public procurement rules.

2.9 SIH verification of the financial institutions' eligibility criteria

SIH checks whether the expressions of interest from financial institutions are compliant with the Call and in line with the requirements stipulated in Commission Delegated Regulation (EU) No. 480/2014 of March 3, 2014. Every financial institution that meets the criteria, receives a portion of the guarantee in line with the distribution methodology for allocation to individual financial institutions described earlier. There is no rating of individual expressions of interest, nor selection of the applicants. Every compliant applicant is offered an opportunity to sign the guarantee agreement and participate in the implementation of the financial instrument. Eligibility criteria against which the expressions of interest from financial institutions are assessed, include:

- Expression of interest is delivered on time, in a prescribed form, with complete documents and declarations, and dully signed;
- The candidate financial institution is in compliance with EU's internationally agreed tax standards;
- The candidate financial institution has no conflict of interest to the object of the financial instrument and has appropriate mechanisms to resolve potential conflicts of interest;
- The candidate financial institution is legally authorised to implement the financial instrument and has an appropriate economic and financial capacity, an efficient and effective internal control system, an appropriate management and system capacity and an appropriate accounting system to implement the financial instrument;
- The candidate financial institution demonstrates preferential financing conditions (e.g. lower interest rate, reduction of collateral requirements) for SMEs as compared to its standard operations and the extension of its basic product line as a result of the guarantee financial instrument;
- The candidate financial institution demonstrates a robust and credible methodology for the identification of the final recipients (SMEs);
- The candidate financial institution makes use of its own resources to implement the financial instrument.

Appendix II – ESF financial instruments in response to COVID-19

This Appendix targets ESF managing authorities and, by way of complementing this factsheet, aims at providing practical hints on the potential for ESF to respond to COVID-19 outbreak through financial instruments, exploiting the flexibilities introduced by CRII/CRII Plus and the Temporary Framework.

ESF managing authorities are encouraged to adjust existing financial instruments or to set up new ones to respond to current financing needs in their local economy, in line with the guidance in this factsheet.

When repurposing **existing financial instruments**, various sections of this factsheet shed light on the options available at this stage. The adjustment of a financial instrument can be carried out by introducing modifications of an existing funding agreement or by setting up a new procedure to select the fund of funds manager and /or the financial intermediaries (Section 3 and Section 5, above). This could be complemented by a grant scheme for the benefit of the final recipients, alongside the financial instrument (Section 7, above).

When managing authorities decide to set up **new ESF financial instruments** to respond to COVID-19 outbreak, Section 6 above provides relevant information.

This Appendix intends to provide further inspiration to ESF managing authorities:

- by describing how an ESF managing authority in Poland is using financial instruments to tackle the COVID-19 effects on social economy;
- by outlining an ESF financial instrument model.

1. Mini Case Study: ESF financial instruments against COVID-19 in Poland

This mini case study focuses on the measures adopted in Poland by the managing authority of the 2014-2020 ESF National OP 'Knowledge, Education, Development' in response to financial problems faced by social enterprises following the outbreak of COVID-19. Particularly, this mini case study briefly presents:

- *the adjustments introduced to the financial instrument 'National Fund for Social Entrepreneurship' in order to improve the borrowing and repayment conditions for final recipients;*
- *the set-up of a new countrywide financial instrument, by the use of 2007-2013 reflows, to meet the increased liquidity needs of the social sector.*

As such, it could serve as an inspiration for managing authorities and for NPBIs in other Member States.

1.1 The National Fund for Social Entrepreneurship financial instrument

The *National Fund for Social Entrepreneurship* is a financial instrument operating in Poland, financed by the 2014-2020 ESF OP 'Knowledge, Education, Development', Thematic Objective 9 (Promoting social inclusion, combating poverty and any discrimination). The Polish National Promotional Bank, Bank Gospodarstwa Krajowego (BGK) is acting as the fund of funds manager.

The financial instrument, which is a follow-up of a loan scheme implemented under the national 2007-2013 ESF-funded OP Human Capital[27], aims at increasing the set-up of Social Economy Enterprises (SEE), improving SEEs' access to finance and supporting their growth.

The financial instrument foresees a total budget of over EUR 37 million. Alongside the provision of loans, business development services are offered to final recipients by the Social Economy Support Units[28].

The Funding Agreement between the managing authority and BGK was signed in April 2016; in December 2016, BGK completed the public procurement procedure and retained two financial intermediaries to deploy the financial instrument: TISE (Towarzystwo Inicjatyw Społeczno Ekonomicznych) and FRW (Fundusz Regionu Wałbrzyskiego). Retained financial intermediaries started to build the loan portfolios in March 2017. Following the complete disbursement of the amount initially allocated to the financial intermediaries, BGK carried out a new public procurement procedure in 2019, retaining the following financial intermediaries: TISE and FRP (Fundacja Rozwoju Przedsiębiorczości).

The financial intermediaries were requested to contribute with own resources for at least 15% of the ESF amount.

1.2 Key parameters of the existing financial instrument

The features of the loans provided under the *National Fund for Social Entrepreneurship* include the following:

- Start-up loans
  - for SEEs operating no longer than 12 months;
  - up to EUR 23 600 per loan, and up to EUR 47 200 per SEE (each SEE can apply twice);
  - 5-years maturity, with a grace period of up to 6 months;
  - interest rate at the promissory note (bill of exchange) rediscount rate of Polish Central Bank (currently 1.05%); reduced by half if a new job is created;
  - interest rate subsidy provided by the MA when the loan is provided via financial intermediary's own funds;
  - no commission fees;
  - although no collateral was recommended, collateral requirements depend on each financial intermediary's terms, but zero collateral encouraged;
  - the MA covers up to 30% of the first portfolio piece losses. The financial intermediary bears the exceeding losses; in case of loan default, financial intermediary has a priority on the recovered amounts;

27 For more information, see the fi-compass case study: https://www.fi-compass.eu/publication/case-studies/case-study-financing-social-economy.

28 Social Economy Support Units are a countrywide network of entities, mostly operated by NGOs, financed by the ESF within Regional OPs. They are based in sub-regions (NUTS3), are subjected to an accreditation process and offer business advisory services to SEEs, also related to the FI's application.

- Development loans
  - for established SEEs, operating for longer than 12 months;
  - up to EUR 117 900 per loan, and up to EUR 235 800 per SEE (each SEE can apply twice);
  - 7-years maturity, with a grace period of up to 6 months;
  - interest rate negotiated according to the loan amount, and reduced according to the number of new jobs created;
  - no commission fees;
  - although no collateral was recommended, collateral requirements depend on each financial intermediary's terms, but zero collateral encouraged;
  - the MA covers up to 20% of the first portfolio piece losses. The financial intermediary bears the exceeding losses; in case of loan default, financial intermediary has a priority on the recovered amounts.

Eligible final recipients include social enterprises; reintegration agencies, providing social and occupational reintegration services for people at risk of social exclusion; NGOs and business entities created to achieve social goals. Working capital is eligible under this financial instrument. In terms of State aid, the *de minimis* regime is applied to final recipients (as they benefit from reduced interest rates or interest rate subsidy).

1.3 COVID-19 related amendments to the financial instrument

In March 2020, following the COVID-19 outbreak and in order to minimise its negative socio-economic impact in the social economy sector, the following more favourable conditions for final recipients were introduced:

- further loan interest rate reduction, up to 0%, for social enterprises in financial difficulties and for a maximum period of 12 months;
- six-month repayment holiday (interests or principal);
- additional six months of grace period (up to 12 months in total) for new loans and the loans for which grace period has not finished yet;
- extension of the loan maturity by up to 12 months (up to 6 years in start-up loans and up to 8 years in development loans);
- extension of the period for new job creations (up to 12 months) for both outstanding and new loans.

The changes in the outstanding loans are introduced upon request of a SEE only if – according to the assessment of the financial intermediary – it is proven that the COVID-19 situation caused financial problems during the loan maturity or if similar problems could clearly materialise, in the future.

These 'ad hoc' features are introduced for a defined period only, i.e. until 31 December 2020. Starting from 1 January 2021, pre-COVID-19 conditions will apply again.

The above-mentioned changes and the investment strategy of the financial instrument were the object of an amendment of the Funding Agreement between the managing authority and BGK. Thereafter, BGK engaged with retained financial intermediaries through a negotiated procedure without prior publication of a notice. At this stage, all retained financial intermediaries apply the improved conditions of the financial instrument to the final recipients.

The financial instrument has recently extended a loan to a social cooperative in the Wrocław area. The social cooperative, which used to sew tote bags, backpacks, sacks and gadgets, has recently converted its production into sewing protective masks for local hospitals, following the epidemic breakout. The loan has provided the social enterprise with the funding necessary to purchase the raw material.

Following the adjustment to the financial instrument, 33 contracts related to SEEs' outstanding loans were modified at 30 April 2020, out of which:

- 78% involved the introduction of repayment holidays;
- 67% involved the extension of the loan maturity.

1.4 Set up of a new financial instrument to meet liquidity needs

With a view to provide a comprehensive response to the financial constraints of the social sector, the managing authority set-up a new financial instrument aimed at deploying micro-loans to tackle liquidity issues faced by SEEs. This additional financial instrument, operating countrywide as of May 2020, is funded by the reflows generated from the 2007-2013 Human Capital OP's legacy funds (loan repayments from the pilot financial instrument) and has a budget of around EUR 5 million.

The features of the loans provided under the new financial instrument include the following:

- only working capital as eligible expenditure;
- for social enterprises operating longer than 12 months;
- maximum loan amount of EUR 23 600 (only one loan per SEE);
- no commission fees;
- 48-months maturity, with a grace period of up to 12 months;
- interest rate – 0.1% annually;
- promissory note recommended, collateral requirements depend on each financial intermediary's terms.

To set-up the financial instrument, the managing authority retained BGK on the basis of an inter-administrative cooperation procedure. Thereafter, BGK entered into negotiated procedure without prior publication of a notice[29] with all three retained financial intermediaries already involved in the implementation of the *National Fund for Social Entrepreneurship* financial instrument.

2. ESF financial instrument model

This model financial instrument has been prepared to illustrate how ESF resources could be used within a new financial instrument. The proposed scheme includes a loan programme, financed under the TO8 and/or the TO9, developed to support businesses that are active in or are able to provide an increase in the quality of the service in sectors including healthcare and social services. Working capital is included in the eligible expenditures.

29 Under the Public Procurement Directive (see Section 3 above), recalled at paragraph *2.3. In cases of extreme urgency – negotiated procedure without publication* of the Communication.

2.1 Introduction

The financial instrument consists of a risk sharing loan financial instrument that is implemented through a National Promotional Bank or Institution (NPBI), although a similar financial instrument could be implemented directly by a managing authority, if desired. Similarly, if the financial instrument operates at local level, the role of the NPBI could be played by regional promotional agencies.

The ESF contribution could be complemented by additional resources of the NPBI. This could contribute to create a critical mass that could be the basis of a fund of funds, managed by the NPBI. Loans to final recipients will be made available via a number of selected financial intermediaries (typically local banks) appointed by the fund of funds manager following a Call for Expression of Interest. All participating financial intermediaries are required (as a minimum) to match the Fund of funds' contribution with the objective to create a portfolio of loans of eligible enterprises.

2.2 Set up and design of the financial instrument

As a new financial instrument, the managing authority has first to undertake a focused and short ex-ante assessment, relying on existing EC publications and its own estimates of demand, as a result of the COVID-19 outbreak, which could be prepared in-house by the managing authority and/or with the help of the NPBI.

The NPBI is entrusted with managing the fund of funds by direct award under Article 12 CPR. As a working hypothesis, it is assumed that the managing authority commits EUR 35 million of ESF programme resources. The programme contribution includes co-financing. For the purposes of this example, the managing authority decides not to take advantage of the new flexibility allowing 100% ESIF participation. Under the funding agreement, the NPBI commits to provide from its own resources complementary financing of EUR 15 million, creating a fund of funds totalling of EUR 50 million. Participating financial intermediaries are then required to match the fund of funds' contribution by deploying an aggregate volume of loans to underlying businesses of EUR 100 million.

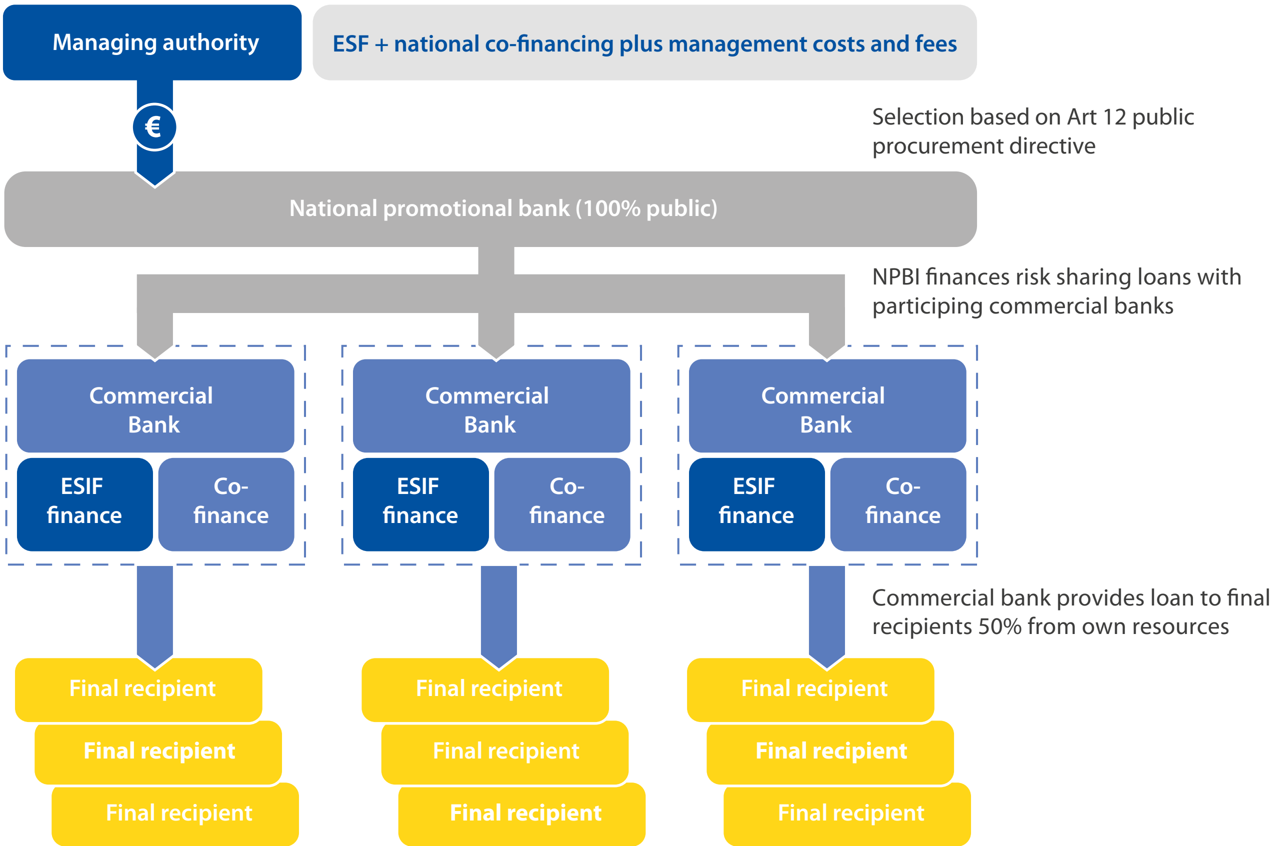
The funding agreement between the managing authority and the NPBI contributes the ESF resources by way of a contingent loan. In this way, the NPBI is obliged to repay the resources to the managing authority by the end of the N+3 period only to the extent that there are resources remaining following repayment of the contribution from the NPBI's resources. The NPBI retains the risk of loan defaults in the portfolio in excess of the ESF contribution.

The NPBI selects financial intermediaries using the accelerated open procedure[30]. As described in the Communication on public procurement, the deadline for receipt of proposals can be reduced to 15 days in cases of urgency. The managing authority can consider the use of a non-selective 'Call' procedure or a short selection process. The latter is particularly indicated to ensure the financial intermediaries have the appropriate skills and experience to support the targeted sector. The 'non-public procurement' model may be more suitable for a general financial instrument targeting SMEs in financial difficulty.

30 Under the Public Procurement Directive (see Section 3 above), recalled at paragraph *2.2. In cases of urgency – shortened deadlines* of the Communication.

The design of the financial instrument is shown in figure 3 below.

Figure 3: Design of the financial instrument



2.3 Support to final recipients

The financial intermediaries are expected to use ESF resources to provide loans to eligible enterprises as part of the managing authority's initiative to support its local economy recover following the COVID-19 outbreak. Under this financial instrument, loans could be offered to final recipients on the following beneficial terms:

- Loans between EUR 10 000 and EUR 300 000
- Maximum duration of ten years
- With a two year grace period before the final recipient must start repaying the principal
- Zero interest payable on the ESF/NPBI 50% contribution to the loan
- No collateral required from borrowers

Eligible businesses to participate in the programme are businesses with a substantial presence in the territory covered by the OP and that have been established for at least one year and are not in financial difficulties at the end of 2019. This recognises that notwithstanding continued or increased demand on health and social care services, undertakings in this sector may nevertheless be experiencing short- term cash flow and financing challenges.

The programme is designed to be implemented under the State aid Temporary Framework, relying on the EUR 800 000 allowance per business for grant and/or other types of support (including through financial instruments). As the maximum loan is EUR 300 000 this allowance is considered sufficient, even if combined with additional measures such as interest rate subsidy described below. If a national State aid notification is not in place to cover this action, the managing authority can notify the scheme for rapid approval by the European Commission under the fast track notification procedure. In order to comply with the Temporary Framework all eligible loans must be committed before the end of 2020.

2.4 Other measures

In order to further adapt the scheme to meet the short-term needs of businesses facing difficulties, because of the COVID-19 outbreak, the managing authority might establish an interest rate subsidy of up to 50% financial intermediary contribution to the loans. This can be done either:

- via a stand-alone grant operation, where the NPBI is regarded as the beneficiary of a grant operation to be used to meet the interest costs;
- via a combined financial instrument/grant operation under Art 37(7) CPR.

In order to best target resources, the interest rate subsidy could be made available only for the initial two years of the loan period, to coincide with the grace period for repayment of capital. Requests for payment of the subsidy are made, with accompanying evidence by the financial intermediary to the NPBI, which confer the subsidy directly to the financial intermediary on behalf of the final recipients to meet their interest costs.

www.fi-compass.eu
contact@fi-compass.eu

European Commission
Directorate-General
Regional and Urban Policy
Unit B.3 "Financial Instruments and IFIs' Relations"
B-1049 Brussels

European Investment Bank
Advisory Services
fi-compass
98-100, boulevard Konrad Adenauer
L-2950 Luxembourg