Preliminary and Complementary Financing for EU-Funded Environmental Projects

Prepared by
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Dusan Sevic and Venelina Varbova
2007

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<th>Abbreviation</th>
<th>Full Form</th>
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<tr>
<td>BMLFUW</td>
<td>Austrian Federal Ministry for Agriculture, Forestry, Environment and Water Management</td>
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<td>BNG</td>
<td>Bank Nederländse Gemeenter, the Netherlands</td>
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<td>BOS</td>
<td>Bank Ochrony Srodowiska S.A., Poland</td>
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<td>CBA</td>
<td>Cost-benefit analysis</td>
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<td>CCF</td>
<td>Carbon credit funds</td>
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<td>CDM</td>
<td>Clean development mechanism</td>
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<td>CEB</td>
<td>Council of Europe Development Bank</td>
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<td>CEE</td>
<td>Central and Eastern Europe</td>
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<td>CF</td>
<td>Cohesion Fund</td>
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<td>CP</td>
<td>Cohesion Policy</td>
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<td>DG</td>
<td>Directorate General</td>
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<td>DG REGIO</td>
<td>Directorate General for Regional Policy</td>
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<td>EBRD</td>
<td>European Bank for Reconstruction and Development</td>
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<td>EC</td>
<td>European Commission</td>
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<td>EEB</td>
<td>European Environmental Bureau</td>
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<td>EIA</td>
<td>Environmental impact assessment</td>
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<td>EIB</td>
<td>European Investment Bank</td>
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<td>EIC</td>
<td>Environmental Investment Center (Estonia)</td>
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<td>EIF</td>
<td>European Investment Fund</td>
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<td>ERDF</td>
<td>European Regional Development Fund</td>
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<td>ESF</td>
<td>European Social Fund</td>
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<td>ESG</td>
<td>Environmental, social and governance</td>
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<td>ETS</td>
<td>Emission Trading Scheme</td>
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<td>EU</td>
<td>European Union</td>
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<td>EUR</td>
<td>Euro</td>
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<td>FLAG</td>
<td>Fund for Local Authorities and Governments (Bulgaria)</td>
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<td>GDP</td>
<td>Gross domestic product</td>
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<tr>
<td>ICT</td>
<td>Information and communication technologies</td>
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<td>IFC</td>
<td>International Finance Corporation</td>
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<td>IFI</td>
<td>International financing institution</td>
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<td>IPO</td>
<td>Initial public offering</td>
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<td>ISPA</td>
<td>Instrument for Structural Policy for Pre-Accession</td>
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<td>JASPERS</td>
<td>Joint Assistance to Support Projects in the European Regions</td>
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<tr>
<td>JEREMIE</td>
<td>Joint European Resources for Micro to Medium-Sized Enterprises</td>
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<td>JESSICA</td>
<td>Joint European Support for Sustainable Investment in City Areas</td>
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<td>JI</td>
<td>Joint implementation</td>
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<tr>
<td>KK</td>
<td>Kommunalkredit Austria AG</td>
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<td>KPC</td>
<td>Kommunalkredit Public Consulting GmbH</td>
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<tr>
<td>MEPA</td>
<td>Malta Environment and Planning Authority</td>
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<td>MoE</td>
<td>Ministry of Environment</td>
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<td>MSMEs</td>
<td>Micro, small and medium-sized enterprises</td>
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<td>NEP</td>
<td>National environmental programme</td>
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<td>NFOSIGW</td>
<td>National Fund for Environmental Protection and Water Resource Management (Poland)</td>
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<td>NFP</td>
<td>National framework programme</td>
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<td>NGO</td>
<td>Non-governmental organisation</td>
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<td>NIB</td>
<td>Nordic Investment Bank</td>
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<td>OP</td>
<td>Operational programme</td>
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<td>PPP</td>
<td>Public-private partnership</td>
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<td>REEE</td>
<td>Renewable energy and energy efficiency</td>
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<td>RSFF</td>
<td>Risk Sharing Finance Facility</td>
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<tr>
<td>SAPARD</td>
<td>Special Accession Programme for Agriculture and Rural Development</td>
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<tr>
<td>SEA</td>
<td>Strategic environmental assessment</td>
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<tr>
<td>SF</td>
<td>Structural Funds</td>
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<tr>
<td>SFF</td>
<td>Structured Finance Facility</td>
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<tr>
<td>SMEs</td>
<td>Small and medium-sized enterprises</td>
</tr>
<tr>
<td>UAPME</td>
<td>European Association of Craft, Small and Medium-Sized Enterprises</td>
</tr>
<tr>
<td>UFI</td>
<td>Austrian Environmental Fund (Umweltfoerderung in Inland)</td>
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<tr>
<td>UK</td>
<td>United Kingdom</td>
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<tr>
<td>UN</td>
<td>United Nations</td>
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<td>UNEP</td>
<td>United Nations Environmental Programme</td>
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<tr>
<td>USD</td>
<td>United States dollar</td>
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<tr>
<td>VAT</td>
<td>Value-added tax</td>
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<td>VCF</td>
<td>Venture capital funds</td>
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This document was prepared with the main objective of providing an overview of sources of complementary and preliminary financing (hereinafter “co-financing” and “pre-financing”) for EU-funded environmental projects in the EU-27 countries. Specific topics include public schemes for pre-financing and co-financing; the role of international financing institutions (IFIs) in providing such funds; and the involvement of the commercial banking sector in financing environmental projects. Two other matters with bearing on the subject — state aid regulation and cost-benefit analysis — are presented. The EU funds considered in this report are the European Regional Development Fund, the European Social Fund and the Cohesion Fund under the Cohesion Policy. The report was prepared based on data gathered during 2006 and the document provides an outlook for the 2007-2013 programming period. This publication targets managers of EU funds and the ultimate beneficiaries of EU support in the EU-27 countries.

With the new programming period the community funding priorities and funding structure have changed. A larger financial envelope is available for EU member states, and this is expected to increase the need for sources of co-financing and pre-financing. The Lisbon goals have become a priority, which places financing for the environmental sector in a different light. Increased focus has been given to environmental areas with direct impacts on economic growth and employment, such as eco-innovation, environmental technologies, energy efficiency and renewable energies. It is expected that more co- and pre-funding will be available for those areas. As the Lisbon process emphasises the enhancement of entrepreneurship, it can be assumed that more co-financing and pre-financing will be available for the private sector, in particular for small and medium-sized enterprises (SMEs). For the new programming period financial resources have been earmarked to support the Lisbon agenda while those earmarked for the environment have been removed. As a result, environmental projects will have to compete more strenuously against projects from other sectors for funding.

Many EU countries have developed functioning public co-financing mechanisms to assist beneficiaries of EU-funded projects. There is an increasing tendency to involve IFIs in public co-financing schemes. The success of the public co-financing systems depends largely on a clear division of responsibilities between institutions, clear procedures for determining the co-financing rate, clear and simple co-financing rules and accurately assessed funding capacities of the proponents (liquidity). Several countries have procedures to ensure that, in the overall system of financing, only the best projects are submitted for EU funding.

Despite the fact that public pre-financing mechanisms can play a crucial role in preventing delays and cost overruns, only a few examples exist in old EU member states (e.g., in Ireland, Spain and Portugal). Most new EU member states have indicated that the main constraints in setting up such systems are the difficulty in getting approval from their finance ministries and the capitalisation of the funds. Pre-financing systems can operate as revolving funds and can be direct lenders and grant providers to final beneficiaries. Public institutions involved in pre-financing systems can range from departments of ministries to independent funds. In some cases public banks are involved in providing pre-financing for municipalities for EU-funded environmental projects (such as BNG in the Netherlands, Kommuninvest in Sweden and BOS Bank in Poland).

IFIs are important sources of co- and pre-financing for environmental projects. There is an increasing tendency of harmonising their support activities among themselves and the European Commission. As a result of this cooperation three facilities have emerged: JESICA, JEREMIE and JASPERS. By pooling together funding capacities and applying expertise for financial engineering and project preparation, these facilities are expected to improve the availability of co-financing and pre-financing for environmental projects.

Commercial banks have begun to pay more
attention to the environment, social issues and governance while taking decisions about investments. In addition, they are increasingly involved in financing environment-related projects. As a result, the range of financial products available to provide co- and pre-financing for environmental projects is growing. This tendency is particularly visible in providing pre-financing, as commercial banks view it as a business niche. They are also diversifying their services with technical assistance for beneficiaries of EU projects ranging from project preparation to finding the most suitable financial products and matching subsidy programmes.

The reform process of the state aid regulations and changes in the methodology of cost-benefit analysis can influence co- and pre-financing. State aid rules, including the one for environment-related projects, are under revision. Proposed reforms include increasing the maximum state aid intensity, the expansion of eligible costs and the widening of tax reductions and exemptions for environmental protection activities. The need for co-financing and pre-financing for private sector environmental projects is anticipated to grow, provided the proposed reforms are implemented. Concerning the changed methodology for cost-benefit analysis, the amount of EU grants is expected to be lower for revenue-generating projects, which can result in an increased need for co-financing.

In summary, we can see a general shift in support priorities and finance mechanisms toward activities that advance the Lisbon goals. New finance facilities are emerging with the cooperation of IFIs and the EC that provide co- and pre-financing for issues identified as Lisbon priorities, including climate change, innovation and enhancement of entrepreneurship. Private sector financing for the environment is growing in scale with the increasing involvement of commercial banks in the co- and pre-financing of EU-funded environmental projects.
This report was prepared by Eniko Artim (project manager), Joanna Fiedler-Morotz (project director), Venelina Varbova (project team member), and Dusan Sevic (project team member) of the Regional Environmental Center for Central and Eastern Europe (REC). The report was prepared in close cooperation with environmental authorities and various public and private institutions in the EU. For their active involvement in information gathering and cross-checking, the authors wish to give special thanks to (in alphabetical order):

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From the start of the new EU funding period of 2007–2013, new EU member states will receive a significantly larger financial envelope than before. The higher EU allocation means not only a great opportunity to finance more projects but also a significant challenge to come up with a pipeline of mature projects to absorb the funds, to build the institutional capacity to cope with the administrative burden and, last but not least, to ensure the availability of required co-financing. For the ultimate beneficiaries, it is crucial to find other sources of finance to complement EU funding. This is a prerequisite for EU support. In addition, EU grants are paid out later in the form of reimbursement of eligible costs to the final beneficiaries. This implies that in order to begin project implementation in a timely fashion, final beneficiaries will often have to secure bridging funding until the subsidy arrives. This raises the need for pre-financing. In new EU member states, due to limited own-resources of applicants, ensuring co- and pre-financing is often a difficult task.

The main objective of this document is to address the issue of the increased demand for project co-financing and pre-financing by providing an overview of such sources.

Specific objectives of the document are:

- to present selected pre-financing and co-financing schemes available from national funds and national banks from which final beneficiaries of EU funds can receive funding for environmental projects;
- to provide an overview of the role of IFIs in co- and pre-financing environmental projects submitted for EU funds support;
- to present an overview of co- and pre-financing options offered by commercial banks in this context;
- to describe certain factors that affect the need and availability of co- and pre-financing;
- to formulate conclusions on available and planned co- and pre-financing schemes.

Scope of the document

The report provides an overview of co- and pre-financing schemes for EU-funded environmental projects available in 2006 and offers an outlook for the 2007-2013 programming period. The EU funds covered in this report are the European Regional Development Fund, the European Social Fund and the Cohesion Fund under the Cohesion policy. The geographical scope is the EU-27 member states.

Target groups

This report targets managers of EU funds and final beneficiaries of EU support, primarily in the new member states of Bulgaria and Romania. However, the report’s findings could be useful for old member states as well.

Structure of the report

The report is organised according to the following structure:

Chapter 1 presents the background and objectives of the report.

Chapter 2 describes the changes in the new programming period of 2007-2013 in the Cohesion Policy and also presents the Lisbon Agenda as the new community focus.

Chapter 3 presents an overview of co- and pre-financing mechanisms developed by public bodies.

Chapter 4 describes the involvement of IFIs in providing co- and pre-financing for EU-funded environmental projects.

Chapter 5 provides an overview of commercial
banks’ involvement in environmental financing.

Chapter 6 describes two factors that can influence the need and availability for co- and pre-financing: the state aid regulation and the new regulation on cost-benefit analysis for infrastructure projects.

Chapter 7 presents conclusions.

Methodology

For the development of the report the following methodology was applied:

- For data collection on national pre- and co-financing systems, a questionnaire was developed and sent to contacts in ministries of environment, ministries of finance, environmental funds and other funding agencies in the EU-27 member states. A list of responding countries and a brief description of the questionnaires are presented in the annex. In addition to this, the authors conducted desk research of available information and made phone interviews.

- For data collection from IFIs, a questionnaire was sent to the European Bank for Reconstruction and Development (EBRD), the European Investment Bank (EIB) and the Council of Europe Development Bank (CEB) on financing mechanisms to complement EU funds. In addition, phone interviews and desk research were conducted.

- For data collection from the commercial banking sector, selected private banks were approached with a questionnaire on financial products offered for co- and pre-financing to beneficiaries of EU projects. Desk research was also conducted in this area.

- The sections on state aid and cost-benefit analysis were developed through desk research and interviews with relevant institutions and expert groups.

In this document, complementary financing (hereinafter “co-financing”) is understood as funding to cover costs of EU projects which are not covered by EU subsidies or by the client’s own sources. Preliminary financing (hereinafter “pre-financing”) is the finance that beneficiaries receive to cover the costs of EU projects before EU funds arrive.
Chapter 2
Introduction — The New Cohesion Policy

The new Cohesion Policy (CP) for the 2007–2013 period introduces a re-prioritisation of areas of support as well as in the setup of EU financial support mechanisms. These changes have an impact on the need and availability of co- and pre-financing. This chapter describes briefly the new CP and highlights the changes that can influence co- and pre-financing for EU-funded projects.

The CP for the 2007–2013 period focuses on increasing growth, competitiveness, innovation and employment in line with the renewed Lisbon Strategy\(^1\). It promotes decentralisation of responsibilities to national and regional levels. In addition, the new CP strives to be simpler and more transparent than the previous one by requiring unified programming for cohesion and structural support into a single programming document (2007–2013 National Strategic Reference Framework) and related operational programmes (OPs).

Financing tools have been reduced to three: the European Regional Development Fund (ERDF), the Cohesion Fund (CF) and the European Social Fund (ESF). These funds support three principal objectives (see box 2.1).

**Larger financial envelope**

The total Cohesion Policy budget amounts to EUR 307.6 billion\(^2\) for 2007–2013. This amount is 22 percent more than during the previous period (EUR 241 billion\(^3\)). This huge increase in available funding means a greater challenge to absorb the funds. It raises the need for EU member states to enhance administrative capacities and project preparation skills. It also presents a challenge to EU member states to provide more complementary funds and mechanisms for co- and pre-financing EU projects.

**New Community policy focus: The Lisbon Strategy**

The Lisbon Strategy\(^4\) focuses on EU competitiveness and cohesion within an increasingly innovative economy in order to create more and better jobs, improve opportunities for all members of society, and, at the same time, protect the environment. The Lisbon Strategy highlights the need to increase investment in research and development (R\&D) to a minimum of 3 percent of GDP and to promote entrepreneurship\(^5\). The Lisbon Strategy rests on three pillars:

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**Objectives of the 2007–2013 programming period**

- The **Convergence objective** concerns EU member states and regions whose GDP per capita is less than 75 percent of the Community average. It seeks to promote growth-enhancing conditions leading to convergence with more developed member states and regions through long-term competitiveness and job creation. The Convergence Objective receives EUR 251.33 billion — 81.7 percent of the total CP funding — through the ERDF, ESF and CF.

- The **Regional Competitiveness and Employment objective** concerns other EU member states and regions (NUTS I and II, and “Phasing-in” regions) and it helps them to anticipate and promote economic change by strengthening their competitiveness and attractiveness and to foster job creation and shift skills towards market needs and changes. This objective receives around 15.8 percent of CP funding (EUR 48.79 billion) through the ERDF and ESF.

- The **European Territorial Cooperation objective** supports cooperation between regions at the cross-border, transnational and interregional levels for a balanced integration of the EU’s territory. Around 2.44 percent of CP funding (EUR 7.5 billion) will be spent on this objective through the ERDF.
the economy, society and environment. After the mid-term review, the Lisbon Agenda was re-launched in 2005 with a reiterated focus on research and development, innovations and entrepreneurship and employment. With regard to environment, environmental technology, renewable energy and energy efficiency have been prioritised.

For the new financing period an emphasis is placed on the attainment of the Lisbon Agenda’s goals. This shift in focus will have an effect on allocations and on the scope of projects that need co-financing and pre-financing. As the Lisbon Strategy emphasises the development of entrepreneurship and employment and the prioritisation of knowledge and innovation, energy and climate issues, it is anticipated that more pre- and co-financing will be available for supporting these areas. In addition, new financing vehicles are expected to be established to provide finance to SMEs in the prioritised areas.

**Earmarked financing for Lisbon**

Community financial resources are earmarked for measures that support the Lisbon goals. Sixty-two percent of the new CP budget is earmarked for Lisbon priorities, where:

- 60 percent of expenditures are earmarked for Lisbon priorities under the Convergence objective;
- 75 percent under the Regional Competitiveness and Employment objective; and
- the European Territorial Cooperation objective is earmarked with respect to geographical scope: 77.6 percent for cross-border projects, 18.5 percent for transnational projects, and 3.9 percent for interregional projects.

Within these limits, the EU member states can decide how to distribute funds among different programmes, priorities and measures. Thus, they can influence how much the environment will be integrated into programmes and individual projects. The earmarking can create competitive advantage for fields of environment that have a direct link to the Lisbon Agenda. The earmarking for Lisbon is not obligatory for new EU member states.

**Earmarked sectors for Lisbon**

There are sectors that are earmarked as contributors to the Lisbon Agenda. These sectors are listed in the CP Funding Regulation as categories of expenditure (see details in box 2.2).

The earmarked sectors linked to environment have been reduced in number and are now confined to the fields of renewable energy and energy efficiency (REEE) and clean transport. Some other categories (such as transport: railways, multimodal transport; and human capital: research and innovation) have potential to be used for successful integration of environmental priorities. However, this potential depends on the conditions within a given project, region or EU member state. It is expected that EU funds will focus on supporting environment-related projects.

**BOX 2.2**

**Expenditure categories related to environment in the CP Funding Regulation**

The CP Funding Regulation provides a list of categories of expenditure, grouped within priority themes. There are seven priority themes:

- Research and technology, innovation and entrepreneurship
- Information society
- Energy
- Environmental protection and risk prevention
- Employment and sustainability
- Social inclusion
- Human capital

Within these seven priority themes there are 49 expenditure categories. Out of these 49 categories, only 6 are strictly environmental. These are all in the areas of renewable energy, energy efficiency, and clean urban transport. Under the environmental protection and risk prevention priority theme there is only one category: clean urban transport.
under the given expenditure categories. As a result, there is a risk that less financing will be available for projects that fall outside these categories.

**No earmarking for environment**

Even though the CP financial envelope is larger in the new programming period, the share for the environment will not necessarily grow, despite increasing environmental financing needs. Furthermore, the new Cohesion Policy does not set earmarks for the environment. Environment-related activities are eligible to receive support from all three instruments, and they can be horizontally integrated into all three CP objectives. In the previous period, for instance, 50 percent of the CF was earmarked for environmental projects.

This implies the possibility that environmental projects will face tougher competition for funding with other priority sectors. It can be expected that co- and pre-financing mechanisms will follow the shift in Community policy focus, and adjust to the eligible project scope and funding availability accordingly. It is anticipated that new options of co- and pre-financing will open up for projects with clear links to the Lisbon Agenda, such as innovation and technological development. It can be assumed that traditional CF environmental projects (such as waste and water infrastructures) will compete with other projects (e.g. in the field of transport, renewable energy and energy efficiency) for co- and pre-financing. In this case there is a risk that unless adequate funding is ensured through political will and the quality of projects enhanced for environmental projects, there will be less capacity to absorb funds.

**Challenges for EU member states**

Some EU member states have a shortage of people with skills in environmental project development and management, a problem remaining from the previous programming period. In addition, the majority of new EU member states still have many unresolved pollution problems from the distant and not so distant past as well as gaps in institutional capacity for allocating resources for the environment. The integration of environmental issues into Lisbon priorities is necessary to ensure adequate funding for the environment. These challenges could affect the ability of EU member states to set up and successfully operate co- and pre-financing mechanisms supporting EU-funded environmental projects.

**Conclusions**

- The larger financing envelope in the new programming period means EU member states need to ensure greater availability of co- and pre-financing.
- The new focus of the Community policy is the Lisbon Agenda. It is expected that the scope of co- and pre-financing will follow this shift and as a result more funding will be available for eco-innovation, environmental technologies, energy efficiency and renewables, climate change issues and the private sector.
- Since there is no earmarking specifically for environmental projects, stiffer competition for co- and pre-funding can be expected between the environment and projects from other sectors.
- As EU funds are earmarked for Lisbon priorities, it is anticipated that more co- and pre-financing will be available for environmental projects directly supporting Lisbon goals (e.g. energy efficiency and renewable energy, eco-innovation, development of environmental technologies) than for environmental projects falling outside the Lisbon priority areas (e.g. waste and water infrastructures).
- It will be a challenge for some member states, especially new ones, to absorb EU funds for the environment. The ability to attract EU funds affects the need and capacity for co- and pre-financing.
Chapter 3
Public Co- and Pre-financing Mechanisms

This chapter presents an overview of selected co-financing mechanisms developed by public bodies in order to support beneficiaries of EU-funded projects. Interesting examples of national co-financing systems are presented from EU-27 member states; however, the list is not exhaustive. This chapter also presents an overview of pre-financing sources in the EU and provides examples of such mechanisms.

Public co-financing mechanisms

Mechanisms for channelling co-financing are present in many EU countries. In this document co-financing is understood as funding to pay for those costs of EU projects which are not covered by EU subsidies or by the client’s own sources. Co-financing can be provided from national sources such as from the state budget, environmental funds or other national purpose funds, regional, sub-regional and local budgets.

In Austria the federal environmental fund is the main source of co-financing of grants. The fund is managed through Kommunalkredit Public Consulting GmbH (KPC). Beneficiaries can also receive co-financing at the regional level (federal state). See more information in box 3.1.

BOX 3.1

Case study on the Austrian co-financing mechanism

The Austrian environmental funding system of the Federal Ministry for Agriculture, Forestry, Environment and Water Management (BMLFUW) comprises the following elements: water management fund (water supply and wastewater treatment); environmental fund (greenhouse gases, air pollution, hazardous waste); rehabilitation of old dumping sites; and joint implementation (JI) / clean development mechanisms (CDM). All funds are managed on behalf of the BMLFUW by Kommunalkredit Public Consulting GmbH (KPC), a daughter company of Kommunalkredit Austria AG (KK).

The Austrian Environmental Fund (UFI) receives money to support environmental projects from two sources: the federal state budget and EU Structural Funds. The legal basis for both subsidies is the national guidelines for environmental subsidies, managed by KK. Due to the Structural Funds regulation, the contracting and the payment of the SF is done separately. Therefore, there are two types of subsidy contract: one is for grants from the state, and the second is for EU subsidies. The Environmental Fund provides direct grants to final beneficiaries (private and municipal enterprises) according to existing national funding guidelines. The total amount of available federal funds for environmental financing is currently about EUR 80 million per year. The EU funding will be approximately EUR 32 million for seven years or EUR 4.5 million per year.

According to the funding guidelines, only enterprises (private and municipal) are eligible. Municipalities themselves are not eligible. The maximum total grant (calculated on the basis of additional environmental costs) is 30 percent of the investment, 50 percent of which can derive from EU funds. The minimum project size is EUR 10,000 (grants of approximately EUR 3,000). The maximum grant is EUR 3.75 million. It is important to note that, in the case of environmental projects, the beneficiaries have no advantage in getting EU funds aside from being eligible for an additional supplement of up to 5 percent (no more than EUR 10,000) of the above calculated subsidy.

There are no sequenced calls for projects and therefore no deadlines in the national funding scheme. EU co-financing is only taken for the best projects. After exhausting the EU funds, funding depends on national means. This means that only the best projects (in terms of innovation and in terms of compliance with EU criteria) get EU funding. The projects have to comply with technical criteria, laid down in the UFI guidance, as well as with sound financial management criteria and innovative concept criteria. The competition rules of the EU also apply, as well as EU restrictions on the aid intensity, pay-back conditions and eligible costs (state aid regulations and cost-benefit analysis regulations). Costs are limited to the environmental component of a project. These costs are determined by comparing the projects with similar projects without environmental investments. The amortisation of the first five years must also be taken into account.
In Belgium, project proponents can receive co-financing from sources that are regional (Flemish level), sub-regional or local. No specific institutions or funds have been created for co-financing. No fixed limit on grants has been determined; proposals are reviewed on a case-by-case basis. Eligible applicants include any public or private proponent which presents a project proposal in accordance with the priorities and measures of the programme. In the case of the ERDF, for example, co-financing from the Flemish budget can be as high as 85 percent.

In Bulgaria, according to plan, 15 percent of the total public costs of a project will be eligible for co-financing through the state budget. National co-financing for the years 2007 to 2009 has been earmarked in the state budget and is set in the budgetary forecast for the respective period. For the rest of the programming period, national co-financing of project costs can come from other sources. It is expected that municipalities may have difficulty covering non-eligible costs. In order to overcome these difficulties, a special fund — the Fund for Local Authorities and Governments (FLAG) — was created with the participation of the EBRD. Among other things, FLAG is meant to ensure co-financing of non-eligible costs (e.g. VAT costs); provide pre-financing which is subsequently reimbursed from the EU funds and the state budget; and provide resources for the preparation of projects to be funded by the EU. Considering that the Operational Programme (OP) “Environment” focuses mainly on municipalities as final beneficiaries, FLAG is envisaged to be accessible for environmental projects as well. See details in box 3.2.

In the Czech Republic, the final beneficiary may ask for co-financing of projects in the form of grants from national and regional sources (regional authorities), as well as from the State Environmental Fund (SEF). The SEF can also provide loans. The maximum amount in the frame of the OP “Environment” (allocation period 2007–2013) is 1 percent of eligible costs for an individual project from state sources and 4 percent from SEF. The amount of the fund available to co-financing beneficiaries is around EUR 4.9 million for the allocation period 2007–2013. The grant beneficiaries can be public institutions, municipalities, municipal enterprises, and the private sector, depending on the priority concerned (water, air, waste, etc.).

In Cyprus, beneficiaries can receive co-financing from the state budget in the form of a grant. There are plans to involve the EIB in the co-financing of projects.
In Cyprus, municipalities are too small to manage large-scale infrastructure projects, therefore most public institutions of agglomerations of municipalities are eligible for grants. The maximum rate for co-financing is 15 percent.

In Estonia, co-financing is provided through the Estonian Environmental Investment Center and via the state budget through the Ministry of Environment. See more information in box 3.3.

In Latvia, co-financing comes mainly from national

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**BOX 3.3**

**Case study on the Estonian Environmental Investment Center (EIC)**

Financing for environmental projects in Estonia is provided by the state budget through the Ministry of Environment of Estonia and the Estonian Environmental Investment Centre. The Ministry evaluates the applications for grants, while the EIC finances and coordinates the implementation of projects. The priority task of the EIC, a foundation established in 2000, is to provide financial support for international, national, regional and local projects that follow the environmental strategy of the country, and to offer complex, in-house service (consulting to applicants, payments management, supervision and audit) at measure level and to improve cooperation with other implementing agencies. In addition, in November 2006, the EIC opened county offices (with one employee in each of the 15 counties).

Total funds available through the EIC between 2000 and 2006 were EUR 176.58 million. The majority of funds (96.6 percent) came from the state budget through the National Environmental Programme (NEP). The ERDF (since 2005), ISPA and CF (since 2003) contributed the rest of the funds (3.4 percent). The EIC estimates that for the period 2007–2013, more than EUR 224 million of public money is needed for environmental measures alone. This estimate includes mainly investment needs for fulfilling directive requirements. During the 2000–2006 period, co-financing for EU-funded projects mostly came in the form of grants and rarely in the form of loans. Loans were also provided by commercial banks.

Domestic funding sources of the EIC include pollution charges, usage fees for transboundary water bodies, fees for mining permits, fees for hunting and fishing licences, and fines for environmental damage. These resources are collected by tax authorities and directed to the state budget. The Treasury then (as stipulated in the budget law and other relevant laws) transfers these funds back to the EIC’s bank account. The EIC disburses money to funding applicants or directly to contractors implementing the projects if so agreed with the grant applicant. The EIC fills the role of an implementing agency of EU funds in the system. For projects supported by the ERDF, the decision maker is the Ministry of Environment. For nationally supported projects, the decision-making body is the Council of the EIC. Technical reviews of project applications are carried out by the EIC, while environmental impact assessments of project applications are handled by the Ministry of Environment.

In 2002 the Nordic Investment Bank (NIB) lent Estonia EUR 14 million for investing in the environmental sector. The government of Estonia and the NIB agreed that project selection and on-lending would be carried out by EIC (in cooperation with the NIB). In 2002–2005, the EIC managed to use EUR 9 million of the loan for funding selected projects. The EIC paid, on behalf of the state, the full amount (EUR 14 million) back to the NIB in 2006, and it continues to serve the loans provided via the on-lending scheme. As of 2006, the EIC’s own credit-line capacity from the domestic budget was EUR 10 million for long-term loans. Up to 2007, loans had not been used for the co-financing of CF and/or ERDF-supported projects (with a few exceptions involving small amounts), because project beneficiaries of the CF/ERDF were not able to afford credit.

Commercial banks can act as lenders in co-financing schemes. However, their share in the overall co-financing of environmental projects is negligible. Municipally owned projects are of low financial risk, therefore commercial banks are willing to finance such projects provided that the municipalities do not exceed the legal ceiling for borrowing. The rate of national co-financing varies from 5 to 50 percent, depending on how EU funding procedures are set up and the financing requirements for applicants. It is assumed that the applicant must secure at least 10 percent of project costs. For the previous period, the ERDF required that at least 25 percent of the funding be secured by the borrower from his own resources.

One of the challenges in Estonia is that the current demand for construction work and services is double the supply, which puts continuous upward pressure on prices. At the same time, the Estonian construction market is too small to attract construction companies from other countries.

The co-financing system for national environmental projects in Estonia during 2000–2006 worked well for all types of projects (CF, ERDF and NEP). It is more flexible than the EU funding schemes and it provides a good opportunity to solve environmental problems. The EIC’s funding mechanisms and procedures have been flexible enough to respond quickly and secure smooth payment of project invoices. This success stems from the EIC’s high degree of independence from political influences and the high availability of information for beneficiaries concerning opportunities for funding-related conditions. Every year a legally fixed amount of money is available for investments for the environmental sector. To ensure the applicants’ ownership and commitment to solve their own problems through the proposed projects, a certain level of financing needs to be provided.
banks and the state treasury. International financing institutions are involved in co-financing through loans.

In *Lithuania*, co-financing is provided from the national budget and national and international banks. Through the national budget, grants are indirectly provided to the final beneficiaries through payments to contractors who implement EU-funded projects. IFIs provide direct lending to the final beneficiaries.

In *Malta*, depending on the particular EU financing source (SF, CF, etc.), beneficiaries may receive co-financing from national funds through either budgetary subvention from the government consolidated fund (when the borrower is a public entity) or through a grant sponsored by a public entity (when the borrower is from the private sector, such as an NGO [subject to state aid rules]). Co-financing may also be provided by private financial institutions and banks. The Malta Environment and Planning Authority (MEPA) is involved in the co-financing of environmental projects in two ways: as a direct beneficiary of the funds, in which case it provides matching funding from its own resources; and as a sponsor of projects implemented by other entities. In the latter case, funding is subject to conditions designed to ensure that the project’s results help MEPA to achieve its business plan objectives. Typically, MEPA receives and evaluates project proposals from NGOs and makes its sponsorship decision on a case-by-case basis. In either instance, there is an established mechanism for the provision of co-financing. Decisions are made on the basis of the organisational strategy for implementing internationally funded projects. Although not financed by EU funds, MEPA also administers an environment fund through the Environmental Initiatives in Partnership Scheme (EIPPP). The fund is financed through contributions collected as “planning gain” and financial guarantees attached to the implementation of certain development projects. Currently, MEPA is exploring a possibility of utilising EIPP funds to provide co-financing for environmental projects that receive EU support.

In *Greece*, public and private entities may receive co-financing from national subsidy programmes, most of which goes to infrastructure projects. Co-financing support varies from 25 to 75 percent depending on the type of project. Private banks are normally involved in providing a loan for the beneficiary’s own contribution, which is required. Typically, the financing breaks down as follows: EU contribution, 50 percent; own contribution, 25 percent; and bank loan, 25 percent. With the signing of the award contract between the beneficiary and the government, the beneficiary receives the first installment of the bank loan straight away in order to get the project started. In a few cases, the beneficiary can give the award contract to a bank and receive an amount of credit equal to his own contribution or, in some cases, even an amount equal to the total project budget. Beneficiaries who are small companies have the option of getting a special low-interest loan from the Credit Guarantee Fund for Small and Very Small Enterprises (which belongs to the government and is subsidised by the EU). Some calls for proposals are publicised directly by banks, which means that applications must be submitted to and evaluated by the banks. In this case, after the signing of the award contract, the company immediately receives the loan from the bank to implement the project.

In *Poland*, beneficiaries get support mainly in the form of grants and loans. The main provider of co-financing is the National Fund for Environmental Protection and Water Management. IFIs are involved in co-financing large infrastructure projects. Commercial banks are very active and a very popular source of project co-financing. Almost half of beneficiaries use commercial banks. Loans are given on commercial terms. The most active commercial banks are: PKO BP, PKO SA and BPH. Banks have quickly mastered the system of EU funding and have found their niche in the market. It is expected that in the future programming period, cooperation with commercial banks will even be strengthened.

In *Portugal*, public entities belonging to the government receive co-financing from the government budget. Municipalities and associations of municipalities receive co-financing from their own budget. Municipalities get their own revenues from local taxes and also receive money from the national budget. The autonomous governments of Madeira and the Azores have a regional budget. The government, local and regional entities can ask for loans, but they must get authorisation from the Ministry of Finance and adhere to certain regulations, as such borrowing affects the budget deficit. Public enterprises have their own financial resources, through their shareholders, and they also have revenues from their own activities. They can take out loans as long as they can prove the ability to repay. Some municipalities and groups of municipalities create public utility enterprises with private entities. The municipalities own more than 50 percent of the capital of the enterprise, so they retain control over the enterprise. Such enterprises are eligi-
ble for loans. Commercial banks are often involved in the co-financing of EU-funded projects.

In Romania, beneficiaries can receive co-financing for EU projects from the state budget and local funds in the form of grants. The main institution providing co-financing is the National Fund. IFIs and commercial banks may also be involved in co-financing EU projects. The estimated demand for co-financing for the 2007–2013 period is EUR 943 million (EUR 846 million from the state budget and EUR 97 million from local budgets). The beneficiaries include municipalities, associations of municipalities, state organisations, NGOs and private entities. For projects financed by the ERDF, the maximum rate of co-financing is 20 percent.

In Slovakia, beneficiaries can obtain co-financing from the state budget. This type of support is disbursed to the beneficiary under the same conditions as the EU grant. In the programming period 2004–2006, the EIB provided EUR 95 million in funding for ERDF measures for the public sector through a framework loan facility.

In Slovenia, EU-supported projects, on average, are funded 65 percent by the EU and 35 percent by national co-financing. A quarter of this co-financing comes from the state budget and 10 percent comes from municipal budgets. Grants are provided directly to final beneficiaries. The total funds available for co-financing are EUR 230 million. Types of projects supported include wastewater collection and treatment, potable water supply, waste management, energy efficiency and water infrastructure for risk prevention. The minimum size of projects for CF support is EUR 10 million and the maximum size is EUR 130 million. There are no limits for SF projects.

**Public pre-financing mechanisms**

This section overviews pre-financing sources in the EU and provides examples of such mechanisms. Pre-financing is finance that the beneficiary receives to cover the costs of EU projects until the EU funds arrive. Sources of public pre-financing can be public funds at national, regional or local levels and public banks. As beneficiaries of EU funds often face difficulties in financing the start-up of projects, pre-financing from other sources can play a crucial role in project success.

Access to pre-financing by final beneficiaries is an important factor in avoiding costly delays in project implementation. For large infrastructure projects, delays at the beginning of implementation can stretch over two years or even more. A well-designed system of pre-financing by the EU member states can make it possible to get approvals for projects which are close to tendering or have completed tendering procedures.

Public pre-financing systems in the EU

Pre-financing systems from public budgets such as state funds, regional funds, local funds or public banks are not common in Europe. Among the old
EU member states, Ireland, Spain and Portugal operate central pre-financing systems dedicated to CF projects. These systems provide help at the beginning of projects and help avoid delays in implementation. In Ireland, for instance, pre-financing for EU projects is secured through the Exchequer (see box 3.4). This mechanism successfully buffers cost increases due to high inflation. During 1995–2002, by way of illustration, prices in the construction sector increased by 95 percent in Ireland.

In some new EU member states, pre-financing is available to beneficiaries from the central fund (as in Poland) and regional development funds (as in Slovenia). In Poland there is an option to acquire bridging loans for CF projects, a resource often used by municipalities. There is no similar public pre-financing mechanism for SF, so in this case, borrowers must turn to commercial banks. In Slovenia, the Governmental Office for Local Self-Management and Regional Policy provides grants directly to municipalities.

Several other new EU member states have plans — or at least intentions — to set up public pre-financing systems. However, there are obstacles, including complex changes in the administration system, the need for approval from ministries of finance and the difficulty of capitalising the funds. To address this final issue, the accession countries are designing central pre-financing systems with the involvement of IFIs.

In Romania, there are plans for the establishment of a revolving fund to be operated by the Ministry of Economy and Finance with the possible involvement of IFIs such as the EIB and EBRD, based on financing agreements. The fund would provide pre-financing loans to beneficiaries. The planned rolling fund would set the following conditions for giving pre-financing:

- The contract must be signed between the beneficiary and a work contractor / services provider / goods supplier.
- Public procurement rules (tendering and contracting) must be followed.
- Conditions for state aid must be fulfilled.
- The beneficiary must have an open treasury account for pre-financing.

In Bulgaria it is envisaged that part of the resources of the Fund for Local Authorities and Governments (FLAG), with the possible involvement of the EBRD, will be allocated for pre-financing in the form of short-term loans with low interest rates (see the discussion of FLAG in the section on co-financing).

General characteristics of public pre-financing systems

Pre-financing systems can operate as revolving funds and can be direct lenders and grant providers to final beneficiaries. For instance, Portugal operates a revolving fund that is replenished by transferring half of the advance payment to the fund. In Slovenia, grants are provided directly to municipalities by a regional fund; and in Bulgaria, according to plan, short-term loans of up to 12 months will be provided to municipalities to cover the time period necessary for the verification, certification and reimbursement of project costs.

Eligible projects are generally in line with the environmental priorities of national development plans and related operational programmes (including those for waste, wastewater, drinking water, nature protection, energy, etc.). Project sizes vary by country. In Portugal, for instance, limits mirror the EUR 10 million minimum of the Cohesion Fund. Since Portugal’s is a rolling fund, there is no predefined ceiling. The maximum amount depends on the total value of qualifying projects in a given period. There are other eligibility criteria, as well, such as approval by the EC, clarification of ownership issues, the project being part of national strategic programmes, the contribution of own share resources, etc.

The form of support in most cases is credit. Only a few governmental institutions provide grants (such

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**BOX 3.4**

**Irish national pre-financing scheme**

In Ireland, environmental and road projects are financed entirely by the Exchequer, the Irish central budget. When a project receives co-funding from the CF, the amount drawn down from the EU fund by the Department of Finance is transferred to the Exchequer. As for port, airport and rail projects, financing is secured by the implementing bodies. In this case, the Department of Finance transfers the CF support to the implementing body in coordination with the related government department. In this way, continuous financing of the project is ensured even if there are delays in receiving EU payments.

In Ireland, environmental and road projects are financed entirely by the Exchequer, the Irish central budget. When a project receives co-funding from the CF, the amount drawn down from the EU fund by the Department of Finance is transferred to the Exchequer. As for port, airport and rail projects, financing is secured by the implementing bodies. In this case, the Department of Finance transfers the CF support to the implementing body in coordination with the related government department. In this way, continuous financing of the project is ensured even if there are delays in receiving EU payments.

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as the pre-financing schemes for CF projects in Ireland and Portugal).

The primary beneficiaries are municipalities. Some pre-financing systems restrict such assistance to particular kinds of public entities, such as public institutions, municipalities and public enterprises including municipal associations (e.g. in Portugal). Others are open to the private sector, as well.

Public institutions involved in the pre-financing system can range from departments of ministries to independent funds or public banks. As examples, in Slovenia the Governmental Office for Local Self-Management and Regional Policy provides grants directly to final beneficiaries. In Poland, besides the Ministry of Public Finance, the National Fund provides pre-financing. In Ireland, the Exchequer is in charge of providing bridge finance for beneficiaries. In Austria the federal-level environmental funding system, including public pre-funding, is outsourced to KPC, a daughter company of KK (see also the section on co-financing). The rights and duties of KK are laid down in the contract with the finance ministry (for more information see box 3.5).

Public banks providing pre-financing

Some public banks specialise in local self-government financing, funding municipal projects based on joint or sovereign credit enhancement. BNG in the Netherlands, for instance, is owned by public authorities and supports municipalities and public sector institutions (see box 3.6).

Such publicly owned local government financing vehicles are well established in northern Europe. Examples can be found in Norway (Kommunalkreditt AS, a government funding agency for local governments) and Sweden (Kommuninvest, the Swedish local government debt office). Only limited examples exist in Eastern Europe. These include Dextra Banka Slovensko (the former Slovak PKB), which is jointly owned by municipalities. There are also examples of public banks specialising in financing environmentally friendly undertakings (see box 3.7).

Conclusions

- Despite the fact that pre-financing can tide a project over until EU funds arrive, thus avoiding significant delays in project implementation, public pre-financing mechanisms are not widely available in Europe.
- In old EU member states, there are some examples of successful public pre-financing schemes, such as in Ireland, Spain, and Portugal.
Only a few new member states have public co- and pre-financing options either from central or regional budgets (such as Poland and Slovenia). Some of the key challenges to setting up such systems are the need for finance ministry approval and the capitalisation of the funds.

In newly acceded countries (Bulgaria and Romania), there are plans to set up pre-financing systems with the involvement of IFIs.

Pre-financing systems can operate as revolving funds and can be direct lenders and grant providers to final beneficiaries, which, in the majority of cases, are municipalities. The main form of support is credit, with only few government institutions providing grants. Eligible projects are generally in line with the environmental priorities of national development plans and related operational programmes.

Public institutions involved in pre-financing systems range from departments of ministries to independent funds.

There are also examples of public banks providing finance for local governments (such as BNG in the Netherlands or Kommuninvest in Sweden), and even specialised public banks for environmental protection (such as BOS in Poland).

BOX 3.7

Bank Ochrony Środowiska S.A. (BOS), the Polish public bank for environmental protection

BOS specialises in providing financial services to public and private entities conducting environmentally friendly undertakings. The bank is a public company whose largest shareholder (with an 83.29 percent stake) is the National Fund for Environmental Protection and Water Resource Management (NFOSiGW). The Provincial Environmental Protection and Water Management Fund in Katowice holds 5.6 percent of the shares, and the remaining stock is held by corporations and individuals.

The bank’s key activity is the financing of environmental activities in line with its development strategy. It also provides bridge loans and supplementary financing for investment projects supported by European Union funds (SAPARD). The bank cooperates with several funds supporting the environment, such as the NFOSiGW, regional-level funds (wojewódzkie funds) of the NFOSiGW, the M. Rataj Foundation for the Polish Countryside 2000, and the Counterpart Fund of the European Fund for the Development of Polish Villages. BOS offers a wide range of standard banking services (deposit and loan products) to local government bodies, retail and corporate segments. It is interesting to note that the bank offers eco-deposits, in which a part of its charges are channelled to help protect endangered animal species.
International financing institutions (IFIs) are considered important agents in providing co- and pre-financing for environmental projects, mainly infrastructure ones. Such financial assistance can be provided directly in the form of soft loans with payback conditions that are more favourable than those offered for commercial loans, or indirectly, e.g. via different on-lending schemes. Activities of selected IFIs, namely the European Bank for Reconstruction and Development (EBRD), the European Investment Bank (EIB) and the Council of Europe Development Bank (CEB) are presented below. New initiatives for providing financing for beneficiaries of EU projects between the European Commission and the mentioned IFIs are described in this section as well.

**International financing institutions providing co- and pre-financing**

**European Bank for Reconstruction and Development**

The EBRD provides co-financing to EU-funded projects in the form of loans which are used for either eligible or ineligible expenditures under EU rules. The EBRD also provides funding on a facility basis via financial intermediaries. Examples include the SME Facility or Municipal Finance Facility (MFF). The bank does not normally make global loans to governments to co-finance entire programmes. The EBRD supports project preparation activities with technical cooperation sourced from its donor technical cooperation funds, and from (limited) consultancy funds under EBRD’s own internal budget. The bank also provides direct input to project preparation with its own staff, and via its contribution to Joint Assistance to Support Projects in the European Regions (JASPERS). (For more on JASPERS, see below.)

It is estimated that during the period 2007–2013, the demand for direct EBRD financing will be limited to very large infrastructure projects or projects in which grant funding is modest due to high revenue generation or the presence of state aid (e.g. in the energy sector). It is expected that the demand for EBRD financing may be highest in sectors which have received less EU funding in the past but where EBRD expertise is strong – such as energy efficiency, district heating, public transport, and different public-private partnerships. With regard to lending via finance facilities, energy efficiency appears to be a strong area of potential demand, and also one in which the EBRD has strong capacity and expertise. Key constraints for beneficiaries to access EBRD’s financial sources are presented in box 4.1.

**BOX 4.1**

**Key difficulties for beneficiaries to access EBRD’s financial sources**

- Proving creditworthiness and being able to improve governance, innovative (re)structuring, commercialisation and private sector involvement.
- Accessing funding for smaller municipalities or utilities on a grouped basis, and the difficulties of blending grant and private funding, both of which are complex and pose difficulties with regard to EU funding.
- Availability of technical assistance to support project preparation, especially as EBRD has limited own funds to spend in EU member states following their accession. The EBRD often helps beneficiaries to make the best use of their own technical assistance funds, including helping write terms of reference or providing supervising consultants, either directly or via JASPERS.
Council of Europe Development Bank

The CEB currently operates in 39 member states. It provides loans and guarantees to its member states, to local authorities or to financial institutions (on-lending) for the implementation of social projects. It also provides, in special cases, interest rate subsidies and donations via trust accounts for the purpose of financing projects or technical assistance. CEB’s most frequently used financial instrument is long-term loans with low interest rates and repayment schedules adapted to meet borrowers’ requirements.

The CEB can also provide technical assistance for project preparation. Direct lending at the sub-sovereign level is also possible subject to the evaluation of risks. The CEB also uses on-lending through intermediary local banks covered by adequate guarantees, to better serve beneficiaries in relevant countries. In the period 2007–2013 the bank intends to increase cooperation in terms of co-financing with other IFIs and the EC. Greater complementarity is expected between the European Union’s Structural and Cohesion Funds. This goes along with the CEB’s latest development strategy, which envisages 50 percent of loan disbursements going to the target countries (CEE countries, Turkey and Georgia).

European Investment Bank

The EIB is the European Union’s long-term lending institution. It provides loans, technical assistance, guarantees and venture capitals. Co-financing is mostly channelled through loan agreements to public or private borrowers in support of projects in all sectors of the economy. Clients range from large corporations to municipalities as well as small and medium-sized enterprises. Loans cover up to 50 percent of total investment costs and they can be individual or intermediated loans:

- Individual loans are offered for proponents of projects of more than EUR 25 million in the public and private sectors, including banks, under fixed, revisable fixed or convertible rates. The project or programme must be financially viable, sound and in line with EIB lending objectives;
- Intermediated loans are provided to banks and financial institutions so that they can lend on to SMEs and local authorities carrying out projects costing less than EUR 25 million (see example in box 4.2). In some countries, microfinancing is provided as well. Conditions of the loan are set by the partner banks, and loan maturity ranges from 5 to 12 years.

The EIB also operates special instruments, such as the Structured Finance Facility (SFF), the Risk Sharing Finance Facility (RSFF) and the Carbon Credit Funds (CCF).

- The SFF was set up to provide funding for high-risk projects as well as to pursue equity financing and guarantee operations for large-scale infrastructure schemes. The facility provides a range of financial products such as senior loans and guarantees (incorporating pre-completion and early operational risk); subordinated loans and guarantees, mezzanine finance, etc.
- The RSFF was set up in cooperation with the EC to provide higher-risk financing for innovative

**BOX 4.2**

**EIB, an example of on-lending for environmental projects**

In December 2006, a EUR 50 million loan agreement was signed between the EIB and BNP Paribas SA in Poland to support small and medium-scale projects promoted by either public or private entities in the field of environmental protection. This includes the rational use of energy, diversification of energy sources and improvements in environmental infrastructure. Since 1990, the EIB has provided loans in Poland amounting to some EUR 13 billion. The bank has provided about EUR 2.1 billion for implementation of smaller projects by SMEs and municipalities in Poland. This represents 15 percent of the overall EIB lending to the country. A large share of EIB lending in Poland — approximately 40 percent — has been focused on the transport sector. BNP Paribas SA in Poland has a profound knowledge of the Polish market and an extensive network of branches in the country.

In addition, regional and municipal authorities, to whom the loan is devoted, are customers of the bank and they will profit from better access to long-term finance provided by the loan. EIB loans to partner banks have been developed as a successful tool for providing long-term funding for smaller projects (EUR 0.04 to 25 million). They represent credit lines to financial intermediaries that on-lend EIB funds under their own management, at their own risk and under their own conditions. The EIB will finance environmental projects that contribute to Poland’s efforts to implement EU environmental legislation.
R&D and technology platform projects. This facility is based on credit risk sharing between the European Community and the EIB.

- The CCF was set up in cooperation with the EBRD and the World Bank to develop the carbon market in transition countries and to encourage private sector participation.

Technical assistance is a complementary service of the bank for project preparation by a pool of experts. In the EU, the EIB performs due diligence prior to investments. In addition, the EIB, in cooperation with the EBRD and the EC, launched JASPERS to provide project preparation assistance for large infrastructure projects financed under Cohesion and Structural Funds in 12 new EU member states. (Detailed information on JASPERS is presented below.)

Conclusions

- IFIs are relevant sources of co- and pre-financing for environmental projects, traditionally for large-scale infrastructure, mainly in the form of soft loans.
- For smaller projects finance is channelled via financial intermediaries to SMEs and local governments.
- As a response to the new Cohesion Policy objectives, special facilities have been developed to provide finance for projects of high relevance, such as research and development, climate change and risk sharing.
- IFIs are striving to harmonise funding priorities with the European Commission and cooperate with other IFIs. Several joint facilities have been developed to pool together funding capacities and complement technical assistance.

New initiatives: JASPERS, JEREMIE and JESSICA

JASPERS, JEREMIE and JESSICA are major new joint policy initiatives of the EC, the EBRD, the EIB and the CEB for the budgetary planning period 2007–2013. These assistance mechanisms are meant to provide additional loan resources for business formation and development in the regions of the EU; to improve access to finance to encourage more business start-ups and new ventures; to assist the beneficiary countries in the preparation of mature large-scale infrastructure projects; and to expedite the achievement of cohesion policy goals. Detailed descriptions of the activities and functions of the three instruments are presented below. These facilities will have an effect on the availability of co- and pre-financing for environmental projects as well, either by the provision of finance or technical assistance for project preparation.

JASPERS

JASPERS stands for Joint Assistance to Support Projects in the European Regions, and it emerged through cooperation between the EC, the EIB and the EBRD (see structure in box 4.3). Its main objective is to provide project preparation assistance to national authorities. This involves upstream technical expertise on technical, economic and financial matters throughout the project cycle.

JASPERS targets its support on the preparation of large-scale projects, especially in CEE, for support from Structural and Cohesion Funds under the convergence objective, which includes the environment among many other sectors. The key areas of support

The structure of JASPERS

Requesting assistance from JASPERS is voluntary and free of charge for EU member states. It does not entail the obligation to borrow from either the EIB or EBRD, nor are banks obliged to finance projects prepared under JASPERS. Priorities and objectives will be drawn up within the framework of country-specific annual action plans. The action plans will be developed in cooperation with the beneficiary country and the EC Directorate General for Regional Policy (DG REGIO). In each beneficiary country the managing authority will take the role of JASPERS coordination and will have the right to request project preparation assistance. All assistance will be offered free of charge. Assistance may be given to prepare individual projects or horizontal studies that cover more than one project or more than one country.

The JASPERS head office is located in the EIB headquarters, with regional offices to be opened and staffed with engineers, economists, financial specialists and other experts. The majority of the JASPERS experts will be based in regional offices so that they can work closely with the beneficiaries. Implementation of JASPERS is supervised by a steering committee consisting of two members appointed by the EC, two members appointed by the EBRD, and two by the EIB.
include: trans-European networks (TENs); rail, river and sea transport; inter-modal transport systems; management of road and air traffic; clean urban and public transport; environment, including energy efficiency and renewable energy; and private-public partnerships. In addition to increasing project preparation efficiency, JASPERS is expected to assist in resolving horizontal issues such as rolling stock financing, energy efficiency financing, public-private partnership (PPP) co-financing and state aid. Addressing such issues and bringing them to the attention of the European Commission can potentially contribute to project funding across sub-sectors. It is anticipated that with JASPERS, a higher number of environmental projects will be prepared, which will increase the need for co- and pre-financing.

**JEREMIE**

**JEREMIE** stands for **Joint European Resources for Micro to Medium Enterprises**. The EC DG REGIO, the EIB and the European Investment Fund (EIF) have launched a joint initiative to improve the access of micro, small and medium-sized enterprises (MSMEs) to finance in the framework of European Regions. JEREMIE became operational on January 1, 2007.

Its aim is to enable EU member states and regions to use part of their SF support to obtain a set of financial instruments that are specifically designed for MSMEs support, such as equity, venture capital, guarantees, loans and technical assistance. It is meant to contribute to growth and employment in line with the renewed Lisbon Agenda (see box 4.4).

JEREMIE facilitates a process in which the EIF as the managing authority enables EU member states and regions to use the part of funds from the ERDF that are allocated to MSMEs (see the example of JEREMIE implementation in box 4.5). From the ERDF, the financing is available through the OP holding fund, and then through financial intermediaries, to beneficiary SMEs.

Under the JEREMIE facility, the EIF contributes with financial engineering, while EIB co-finances the holding fund with loan capital. Beneficiary MSMEs will be able to receive equity and venture capital, mezzanine financing, guarantees, loans, advice and assistance from financial intermediaries. Supported projects range from the modernisation or expansion of existing businesses within sectors such as the environment, life sciences, manufacturing, agribusiness, services, ICT, etc. Special emphasis will be given to projects supporting the Lisbon Agenda by emphasising technology transfer, start-ups or innovation.

**JESSICA**

**JESSICA** stands for **Joint European Support for Sustainable Investment in City Areas**, and is an initiative of the EC in cooperation with the EIB and the CEB (see box 4.6). The main goal of the facility is to promote sustainable investment, growth and jobs in European urban areas.

JESSICA provides the managing authorities of SF programmes outside expertise and greater access to loan capital for the purpose of promoting urban development. If a managing authority wishes to participate under the JESSICA framework, it must contribute resources from the operational programme, while the EIB, other international financial institutions, the EC DG REGIO, the CEB and the EIB.

**BOX 4.4**

**The structure of JEREMIE**

Participation in the JEREMIE scheme is voluntary for EU member states. The EIF is involved with the support of the EIB and its lending capacity. The EIF will work with national and local authorities to design each local scheme “à la carte”, taking into account and adapting to local conditions. It will also support EU member states in evaluating or rating its financial intermediaries. The EIF’s role as manager of funds simplifies the administrative process of funds disbursed from the ERDF and the management of the operational programmes (OPs).

If an OP managing authority decides to join the JEREMIE framework, it has to designate a holding fund, which can be any suitably qualified financial institution at national level. The holding fund will manage the OP’s own resources as well as additional loan capital from the EIB.

The holding fund organises calls for expressions of interest addressed to all interested financial intermediaries and then evaluates, selects and accredits them. The holding fund can then provide them with equity, loans or guarantees, as well as technical assistance. The selected financial intermediaries are responsible for making funds available on competitive terms to MSMEs.
private banks and investors can contribute additional loan or equity capital as appropriate. Since projects will not be supported through grants, programme contributions to urban development will be in the form of revolving funds.

There are two possible approaches in JESSICA: establishing a direct relationship with urban development funds, and organising JESSICA through holding funds (see box 4.7).

Under the JESSICA facility, co-financing is provided directly to the urban development funds by IFIs, private banks and private investors. Beneficiaries can receive
loans from these funds which are backed by guarantee schemes established by the funds and the participating banks themselves. No state guarantee for these loans is involved; hence they would not aggravate public finance and debt. Since JESSICA supports urban projects within the scope of ERDF interventions, it can finance environmental projects in urban areas and sustainable urban investments including social housing.

Conclusions

- The new initiatives involve closer cooperation among the EC, the EIB, the EIF, the EBRD and the CEB.
- It is expected that the initiatives will contribute to the Lisbon goals by encouraging business development, including highly innovative activities.
- It is also expected that the facilities will help create stronger incentives for the successful preparation and implementation of projects by combining financial and managerial expertise.
- The initiatives will increase the efficiency of various financing mechanisms by combining grants with loans and other financing instruments.
- With the new JESSICA and JEREMIE facilities it is anticipated that more funding will be available for co- and pre-financing environmental projects both for private and public beneficiaries of the ERDF.
- With the support of JASPERS, it is expected that higher numbers of environmental projects will be prepared, which can increase the need for co- and pre-financing.
The commercial banking sector is an important potential source of co- and pre-financing, primarily by providing loans as bridge finance (pre-financing) or complementary finance (co-financing) to EU grants. The commercial banking sector is becoming increasingly involved with environmental financing. It has two aspects: putting more focus on socially and environmentally responsible investment, and introducing financial products that are accessible to environmental projects.

Socially and environmentally responsible investment

During recent years, private asset owners, including commercial banks, began paying more attention to environmental, social and governance (ESG) issues while taking decisions about investments. The main reason for this is growing evidence that considering ESG issues has a positive impact on the financial performance of investments. This changing approach can be seen at the international level with the development of initiatives (see box 5.1).

Investors are divided up into three groups, according to their interest in ESG issues:

- financially focused investors who wish to include ESG issues for the sole purpose of enhancing financial return;
- blended investors seeking an investment that makes a competitive return but that also delivers a certain degree of environmental or social return; and
- social investors wishing to deliver environmental or social outcomes through their investments even if the investment does not bring an adequate profit. Examples include community investments and microfinance.

BOX 5.1

International initiatives for commercial banks for socially and environmentally responsible investments

- The United Nations Principles for Responsible Investment (UN PRI) were announced in April 2006. The banks commit themselves to the integration of ESG issues (known as “ESG-inclusive investment”) into their investment decision making and ownership principles.
- The United Nations Environment Programme Finance Initiative (UNEP FI) is a global partnership between UNEP and the private financial sector. It was established with the purpose of developing and promoting linkages between the environment, sustainability and financial performance. The mission of the initiative is to identify, promote and realise the adoption of best environmental and sustainability practice at all levels of financial institution operations.
- The Equator Principles were developed in 2003 and brokered by the International Finance Corporation (IFC), the private sector arm of the World Bank Group, with a number of leading commercial banks. They apply to projects financed with USD 50 million or more. For projects that are considered riskier according to IFC environmental and social criteria, an environmental assessment which satisfactorily addresses a number of social and environmental concerns must be prepared. A revised set of guidelines, Equator II, was approved in 2006; the principles were enlarged to include requirements for labour conditions, community health, safety and security, and pollution prevention and abatement. The project threshold was also lowered to USD 10 million.
- The European Principles for the Environment for international financing institutions.
CHAPTER 5: THE INVOLVEMENT OF THE COMMERCIAL FINANCIAL SECTOR

Commercial bank involvement in co- and pre-financing for environmental projects

Commercial banks are becoming increasingly interested in financing environmental and environment-related projects. As a result, the financial products offered by commercial banks for such projects have been gradually expanding in number (see examples in box 5.2).

This tendency is clearly visible in the new EU member states as the EU financial resources for the environment are available for longer periods and the accompanying administrative structures are being developed. Usually the same bank offers both co-financing and bridge finance to beneficiaries of EU funds. It is increasingly considered a business niche and examples can be listed in each country as this market is rapidly developing.

Since the accession to the EU of Romania and Bulgaria, commercial banks in these countries have started to provide co- and pre-financing as well. An example from Bulgaria is presented in box 5.3.

The commercial banking sector participates in co- and pre-financing in many ways, offering short- and long-term loans, guarantees and other financial products. (See examples of such products in box 5.4.)

It is important to note that, in several cases, commercial banks extend their range of service with project preparation activities and consultancy services to find subsidy programmes and suitable financial products (see case study in box 5.5).

Conclusions

- Commercial banks have begun to pay more attention to environmental, social and governance issues while taking decisions about investments and they offer more financial products for environment-related projects.

BOX 5.2

Products of commercial financial institutions

- Loans, which can be programmes lending to a government, public agency or utility; corporate finance to a private company or commercialised utility; or project finance for a specific project;
- Retail and relationship banking, which includes typical banking services such as offers of deposits and current accounts to individuals and small businesses, overdraft and loan facilities, and advice on financial affairs;
- Bond purchases, either through the purchase of existing stock via market transactions, participation in initial public offerings (IPOs), or syndications (including those led by international banks enjoying preferred creditor status);
- Equity holdings, i.e. open market purchases, portfolio or direct investments, taking up or guaranteeing IPOs, and/or participation in venture capital and private equity funds;
- Mezzanine finance, including convertibles and junior debt;
- Guarantees, options and other derivatives;
- Innovative products, such as microfinancing and ecosystem services;
- Socially responsible and philanthropic activities such as community projects or funds that invest according to environmental or other ethics-based principles.

BOX 5.3

HVB Bank Biochim AD — a private Bulgarian bank that provides co- and pre-financing

HVB Bank Biochim AD and Hebrov Bank AD provide the necessary co-financing for the preparation and implementation of projects by clients of both banks. HVB Bank Biochim AD provides EU co-financing and bridge finance to corporate and public entities. In addition, the bank offers tailor-made solutions to public-private partnerships (PPPs) which meet the national and Eurostat criteria for a PPP and comply with the bank’s lending conditions. The bank also provides loans for environmental infrastructure projects. The loans are usually tailor-made and the maximum amount of the loan and payback period depend on the borrower’s cash flow, creditworthiness and ability to repay.
Examples of financial products offered by commercial banks to beneficiaries of EU projects

HVB Bank Biochim AD, Bulgaria

- Issuance of letters of intent — indicative and firm offers for co-financing of projects;
- Bridge financing — to tide over projects until EU funds arrive. EU support is paid retroactively after the project or a part thereof is completed. The bridging loan is designed to provide the client with financial funds until the customer actually receives the support;
- Investment loans – loans meant to cover project expenses that are not financed by the EU subsidy. An investment loan complements the client’s own sources and it is in the form of co-financing;
- Bonds – tender guarantees, advanced payment guarantees and performance guarantees;
- Loans for continuing or extending projects.

OTP Bank PLC, Hungary provides proponents with a wide variety of financial support, especially:

- Financing project planning costs (such as feasibility studies);
- Financing non-eligible costs, VAT;
- Project co-financing and bridging loans;
- Bank guarantees (if listed among EU funding requirements).

Case study of a commercial bank offering technical assistance to beneficiaries of EU-funded projects — OTP Hungaro-Projekt Ltd.

OTP Hungaro-Projekt Ltd. is a member of the OTP Group. It offers a complete set of additional support for project developers. This service portfolio ranges from project development and management to project consultancy, training and strategic planning. OTP Hungaro-Projekt Ltd. primarily gives advice in identifying, generating, preparing and managing EU-funded projects. As a complementary activity, the bank also focuses on the dissemination of knowledge and best practices in the field of EU-funded programmes and projects.

Project generation services: for clients who are just about, or have just begun, to identify their problems and want to find solutions in the form of a series of development projects. Project development activities focus on the identification, collection and classification of project ideas based upon the problems identified and the available development concepts. The focus is on developing projects to be funded by Hungary’s National Development Plan and its operative programmes.

Preparation of project proposals services: the examination of the feasibility of the project, outlining possible alternatives and preparing the budget and financing plan. Afterwards the documentation package for the relevant call for proposals is prepared including the elaboration of the application form and all necessary supporting documents.

Project financing consultancy: outlining the financing structure of the project, coordinating the various grants available, and finding the most appropriate banking products to facilitate project implementation.

Quality control: performing quality checks of the whole project documentation to ensure formal compliance, eligibility and feasibility.

Project management services: from project approval to the closure of project activities, including assistance in outlining work flows and time schedules; preparation of progress reports; assistance in public procurement procedures; as well as financial project management. It includes preparation of the final report and taking part in technical and financial project monitoring until project closure.

Liability insurance of OTP Hungaro-Projekt Ltd.’s project management activities: all incidental damages incurred by the clients due to the company’s activities during the project are to be compensated by an insurance company.

Organisation of training programmes: tailor-made training modules and consultancy services are aimed at providing expertise on various themes and topics related to EU-funded programmes and projects. Trainings focus on improving project development skills through providing information on the structural and regional policies of the EU; project generation and development according to EU standards; and local and regional economic development.
Commercial banks are becoming increasingly involved in providing loans and other financial products for beneficiaries of EU-funded environmental projects.

This tendency is particularly visible in terms of providing pre-financing. Commercial banks view it as a business niche, as pre-financing from public financial sources is not widespread.

Such bridging funding is normally accompanied by financial products offered as co-financing.

Commercial banks can also provide technical assistance services for beneficiaries of EU projects ranging from project preparation to finding the most suitable financial products and matching subsidy programmes.
Chapter 6
Factors Influencing Co- and Pre-Financing

In this section, two emerging factors are described which can have an influence on the receipt of co- and pre-financing for EU-funded projects. These are the new state aid regulation and the new rules for cost-benefit analysis.

State aid regulation

An important source of support for EU-funded projects is the government budget. Governmental support for the private sector is regulated at the EC level by the state aid rules. This set of rules also regulates environmental state aid for the private sector. The reform of the state aid rules commenced in 2005 and the new rules were due to come into force on January 1, 2008. The reforms will affect the scope and overall availability of state aid for the co- and pre-financing of environment-related projects in the private sector. The state aid rules revision process is ongoing and includes consultation with stakeholders15 (see case study on the consultation process in box 6.1).
Conclusions

The Lisbon Agenda places great emphasis on the promotion of entrepreneurship and increasing the competitiveness of the private sector. State aid can be an important means of such private sector support; however, it is restricted by state aid regulation. The reform process attempts to relieve this tension by streamlining state aid regulation to fit Lisbon priorities. As the new regulations on state aid have not yet been finalised, the key points of the proposal have been summarised below with reference to their potential effect on the availability and scope of co- and pre-financing for environmental projects promoted by the private sector.

- The state aid rules should be simpler and more transparent in order to prevent abuse and misinterpretations.
- The current maximum allowed state aid intensity (i.e. the maximum allowable share of state funds in an investment) for the environment should be augmented.
- The eligible types of costs should be expanded, both in terms of direct costs and costs for consulting and environmental project preparation management services.
- Tax reductions and exemptions should be widened for environmental protection activities.
- The currently eligible environmental sub-sectors, including eco-innovation and energy efficiency, should be eligible for more state support than they are now.
- The rules should allow aid for other environmental sub-sectors such as waste management.
- The rules should permit state aid for activities that can achieve higher environmental standards, not just ones that comply with existing standards.
- The rules should take into account new financing methods such as JI, CDM, and emission trading schemes.

New EU methodology for cost-benefit analyses

The methodology for carrying out cost-benefit analyses (CBAs) for projects has been modified for the new programming period 2007-2013. As a consequence, the process of determining the EU grant for all projects has changed. This will influence the level of co-financing needed to supplement the EU grants. This section describes the methodological changes.

For the new period, the EC has published Guidance on the Methodology for Carrying out Cost-Benefit Analysis, a document that presents a set of working rules intended to introduce greater consistency in future cost-benefit analyses for ERDF and CF applications. The working document clarifies some general principles of CBA for major projects and the process of determining the EU grant for all projects.

The rate of EU grant is determined by the funding-gap method. With regard to revenue-generating projects, the Commission has proposed simplifying and realigning this method for determining the rate of assistance from the funds. The funding gap refers to the share of the discounted cost of the initial investment not covered by the discounted net revenue of the project.

In contrast to the 2000-2006 period, the eligible expenditure and not the co-financing rate is modulated for revenue-generating projects. This is meant to align the contribution from the EU funds with the revenues generated by the project. It should be noted that Article 55 applies to all projects and not explicitly to major projects. However, "member states may adopt procedures proportionate to the amounts concerned for monitoring revenues generated by operations whose total cost is below EUR 200,000" (Art. 55[5]). According to the modification, the revenues generated by the project need to be deducted when calculating the eligible expenditure. This implies that for such projects the size of the EU grant will be lower.

The new rule applies to investment operations which generate net revenues through charges borne directly by users. It does not apply to the following cases:

- projects that do not generate revenues (e.g. roads without tolls);
- projects whose revenues do not fully cover the operating costs (e.g. some railways); or
- projects subject to state aid rules (Art. 55[6]).

Conclusions

- The method of calculating the size of the EU grant has been modified in the new programming period for revenue-generating projects.
• Due to these changes, the level of EU granting is reduced for revenue-generating projects and, as a result, the need for co-financing will increase for such projects.

• For the environment, the method affects a wide range of projects, including those involving user charges such as waste and wastewater treatment services, remuneration for services or the sale or renting of buildings and land.
• The new programming period 2007–2013 introduces significant changes to the new Cohesion Policy. The Community focus has shifted to the attainment of the Lisbon goal of increasing economic growth and employment. Financial earmarks were set to allocate resources for supporting the Lisbon Agenda, and at the same time earmarks for the environment were abolished. As a result, the environmental sector now faces tougher competition from other sectors for funding. In addition, environmental areas with direct impacts on economic growth were prioritised, such as eco-innovation, environmental technologies, energy efficiency and renewable energies. This change in accent will have a significant impact on the scope of projects for which co- and pre-financing are needed.

• The new programming period introduced several simplifications of the programming and funding system, e.g. the reduction of the number of financial instruments to three, and the introduction of unified programming for Cohesion and Structural Funds. In addition, there is a greater level of decentralisation in programme management. These measures have affected the organisation and management of public co- and pre-financing schemes and, as a result, integrated financing mechanisms are now preferred. The new structure also provides more flexibility for EU member states in choosing projects for EU financing.

• A larger financial envelope has become available, one with high relevance to new EU member states. The challenge to absorb the higher amount of allocated funds has increased the need for co- and pre-financing.

• As the Lisbon Agenda emphasises the need to support the private sector, it is expected that more co- and pre-financing will be available for the private sector.

• Many EU countries have developed a smoothly functioning co-financing system to assist beneficiaries in co-financing EU-funded projects. The co-financing mechanisms that have been created are mostly in the form of programmes, funds and centres with varying degrees of independence from the government.

• More and more EU member states are involving IFIs in the national co-financing schemes, such as the EIB in Cyprus, the EBRD in Bulgaria and the NIB in Estonia.

• The success of public co-financing systems depends largely on the clear division of responsibilities among the institutions; clear procedures for determining the co-financing rate; clear and simple co-financing rules; and accurately assessed funding capacity of proponents (liquidity).

• Many countries have self-protecting procedures that are meant to ensure that only the best projects are submitted for EU funding in order to increase the absorption capacity.

• Public pre-financing mechanisms are not common across Europe although they can play a crucial role in preventing delays and cost overruns during project implementation. In some old EU member states there are examples of successful public pre-financing schemes, such as in Ireland, Spain and Portugal. In new member states, only a few such mechanisms exist (such as Poland and Slovenia). In newly acceded countries (Bulgaria and Romania), pre-financing systems are planned to be set up with the involvement of IFIs. Some of the key challenges to setting up such systems are getting approval from ministries of finance, and the capitalisation of the funds.

• Pre-financing systems can operate as revolving funds and be direct lenders and grant providers to final beneficiaries, which, in the majority of cases, are municipalities. The form of support is mainly loans, with only few governmental institutions providing grants. Eligible projects are generally in line with the environmental priorities of the
national development plans and related operational programmes. Public institutions involved in the pre-financing system can range from departments of ministries to independent funds.

- There are examples of public banks providing finance for local governments (such as BNG in the Netherlands and Kommuninvest in Sweden), and even public banks specialised in environmental protection (such as BOS in Poland).
- IFIs can provide co- and pre-financing for environmental projects, mainly through soft loans. For smaller projects, co- and pre-funding is made available through financial on-lending.
- There is a tendency for IFIs to harmonise their support activities with each other and with the EC. This includes developing special facilities to support targeted areas (such as research and development) or addressing specific issues (such as risk sharing and financial planning).
- The new initiatives (JESSICA, JEREMIE and JASPER) are the result of cooperation among IFIs and the European Commission. By pooling funding capacities and applying expertise for financial engineering and project preparation, these facilities are expected to increase the availability of co- and pre-financing for environmental projects as well. With the new JESSICA and JEREMIE facilities, it is anticipated that more funding will be available to co- and pre-financing environmental projects, both for private and public beneficiaries of the ERDF. With the support of JASPER, it is expected that higher numbers of environmental infrastructure projects will be prepared, which can increase the need for co- and pre-financing.
- Commercial banks have begun to pay more attention to environmental, social and governance issues while taking decisions about investments. In addition, they are increasingly involved in financing environment-related projects. As a result, the range of financial products that are available for co- and pre-financing environmental projects is widening. This tendency is particularly visible in the provision of pre-financing. Commercial banks view it as a business niche. Commercial banks are also diversifying their services with technical assistance for beneficiaries of EU projects. The new services range from project preparation to finding the most suitable financial products and matching subsidy programmes.
- The regulations under the state aid regime, including state aid for environment-related projects in the private sector, are being reformed. This means that the modified rules will affect the level of demand of the private sector for co- and pre-financing as well as the scope of projects eligible for such funding. During the consultation process, it was requested that eligible environmental areas be extended, and that they accommodate new financing methods such as JI, CDM and emissions trading. This means that the scope for the co- and pre-financing of private sector projects from public sources would be extended accordingly. The need for co- and pre-financing for private sector environmental projects is anticipated to grow, provided that the proposals on the increase of maximum state aid intensity, the expansion of eligible costs and the widening of the tax reductions/exemptions for environmental protection activities are implemented.
- The method of calculating the size of EU grants has been modified in the new programming period for revenue-generating projects. Eligible expenses will be reduced in direct proportion to the amount of revenue that can be generated. This means that the level of EU grants will be lower for such projects and, as a result, the need for complementary co-financing will be increased. This change affects a wide range of environmental projects, including those involving any user charges. This includes, for example, waste and wastewater treatment services, remuneration for services or the sale or renting of buildings and land.
- In summary, a general shift in support priorities and finance mechanisms to the Lisbon goals is envisaged. New finance facilities are emerging with IFI and EC cooperation that provide co- and pre-financing for issues indentified as Lisbon priorities. These include climate change, innovation and the enhancement of entrepreneurship. Private sector financing for the environment is growing with the increasing involvement of commercial banks in the co- and pre-financing of EU-funded environmental projects.
Survey methodology

In order to collect information on pre- and co-financing systems available from national funds, private banks and international financing institutions (IFIs), a questionnaire was developed and sent to contacts in ministries of environment, ministries of finance, environmental funds and other funding agencies, selected private banks and IFIs in EU-27 countries. The questionnaire referred to co- and pre-financing systems for supporting EU-funded environmental projects that were available in 2006.

The questionnaire covered the following issues:

• possibilities of receiving co- and pre-financing for EU-funded environmental projects from national sources (e.g. state funds, regional funds, local funds and national banks);
• characteristics of the financing mechanisms;
• institutions involved in the financing system;
• forms of co- and pre-financing (grant, loan or equity finance, etc.) and the total amount available;
• conditions for receiving co- and pre-financing (eligible applicants from the public and private sectors, eligible types of projects);
• loans for co- and pre-financing (conditions for taking up the loans, minimum and maximum amounts of loans);
• means of applying for co- and pre-financing; and
• procedures for applying for co- and pre-financing.

Respondents were also asked for their personal views regarding the reform process of the EU state aid regulations, and the methodology changes in cost-benefit analysis and the involvement of commercial banks in co- and pre-financing EU-funded environmental projects. In addition they were asked how the co- and pre-financing systems were to be modified for the 2007-2013 period and what changes would make these financial systems more efficient.

Replies to the questionnaires were received from the following countries:

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The Strategy for Growth and Jobs ("Lisbon Strategy") applies to the 2001–2010 period, and it was revised in 2005, according to the findings of its mid-term review.

During the meeting of the European Council in Lisbon, Portugal (March 2000), the heads of state or government launched the Strategy for Growth and Jobs (Lisbon Strategy) aimed at making the European Union (EU) “the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion” by 2010.


Apart from the UFI, which is financed from the federal budget, EU SF, and occasionally by provinces, there is the Water and Wastewater Fund, financed from a dedicated percentage of income taxes, as defined at federal and provincial levels for several years; and the Contaminated Sites Fund, financed from earmarked levies on depositing and exporting waste. JI/CDM is also financed by the federal budget.

Direct EU instruments for the environment (such as LIFE, CIP) are managed within the Ministry itself.

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EIC in Estonian: KIK. Website: www.kik.ee


That is, projects costing more than EUR 25 million for environment projects and more than EUR 50 million in transport and other fields, although these thresholds can be smaller for smaller countries.

Financial intermediaries include: banks, guarantee funds, loan and mezzanine funds, microcredit providers, technology transfer organisations, as well as venture capital funds (VCFs) that can include start-ups and seed capital funds (“business angels”) and technology and innovation funds.

The eligibility criteria for MSMEs include: a maximum of 249 employees, a maximum annual turnover of EUR 50 million and/or a maximum annual balance sheet of EUR 43 million. Preference should be given to small (fewer than 50 staff; balance sheet/annual turnover less than EUR 10 million) and microenterprises (fewer than 10 staff; balance sheet/annual turnover less than EUR 2 million). Eligible SMEs must have majority private ownership and control or be in the final stage of the process of privatisation. They must not conduct business in gambling, real estate, banking, insurance or financial intermediation, or the manufacture, supply or trade in arms, or activities on the EIF’s or EIB’s exclusion lists.

The New

Endnotes
References


