



European Economic and Social Committee

TEN/472
Europe 2020 Project Bond
Initiative for infrastructure
projects

Brussels, 23 February 2012

OPINION

of the

European Economic and Social Committee

on the

Proposal for a Regulation of the European Parliament and of the Council amending Decision No 1639/2006/EC establishing a Competitiveness and Innovation Framework Programme (2007-2013) and Regulation (EC) No 680/2007 laying down general rules for the granting of Community financial aid in the field of the trans-European transport and energy networks COM(2011) 659 final - 2011/0301 (COD)

Rapporteur: **Armin Duttine**

On 17 November and 12 December 2011, respectively, the European Parliament and the Council decided to consult the European Economic and Social Committee, under Articles 172, 173(3) and 304 of the Treaty on the Functioning of the European Union, on the

Proposal for a Regulation of the European Parliament and of the Council amending Decision No 1639/2006/EC establishing a Competitiveness and Innovation Framework Programme (2007-2013) and Regulation (EC) No 680/2007 laying down general rules for the granting of Community financial aid in the field of the trans-European transport and energy networks.
COM(2011) 659 final - 2011/0301 (COD).

The Section for Transport, Energy, Infrastructure and the Information Society, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 3 February 2012.

At its 478th plenary session, held on 22 and 23 February 2012 (meeting of 23 February), the European Economic and Social Committee adopted the following opinion by 161 votes to 2 with 10 abstentions.

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*This opinion is part of a 5-opinion package prepared by the EESC on the "**Connecting Europe Facility**" (CEF) and its guidelines which were issued by the European Commission in October 2011. This package contains opinions **TEN/468** on the CEF (rapporteur Mr Hencks), **TEN/469** on the Guidelines for **Telecom** Networks (rapporteur Mr Longo), **TEN/470** on the Guidelines for **Energy** Infrastructure (rapporteur Mr Biermann), **TEN/471** on the Guidelines for **Transport** Infrastructure (rapporteur Mr Back) and **TEN/472** on the Project **Bond** Initiative (rapporteur Mr Duttine).*

1. **Conclusions and recommendations**

- 1.1 The EESC welcomes, in principle, the European Commission's proposal to establish a risk-sharing instrument for issuing project bonds for the envisaged pilot phase in 2012 and 2013, but points out that there are risks associated with the instrument. Before this instrument is extended for the new EU budgetary period 2014-2020, the evaluation should first be continued and deepened as part of wide-ranging public discussions, and undertaken with particular care. These discussions should be informed in particular by lessons learned from experience with public-private partnership (PPP) projects.
- 1.2 The opportunities presented by the proposed instrument reside primarily in the mobilisation of significant investment funding for transport, telecommunications and energy infrastructure

projects, which will be vital in boosting growth, innovation and competitiveness and in creating jobs. Executing the planned projects will help to make the benefits of European integration a tangible reality for the general public and thus strengthen the idea of Europe.

- 1.3 However, the EESC also sees risks in the proposal, arising in particular from the possibility of having to absorb losses from the investment projects launched. While the Commission's legislative proposal puts a clear cap on the EU budget's exposure to risk, it assumes that, due to the individual contracts concluded between the EIB and the investors for each project and the EIB's distribution of risk between all the projects, the EIB's exposure to risk will not increase. In order to ensure that, should a risk materialise, it does not under any circumstances compromise the EIB's credit rating or reputation, or the establishment and implementation of its conventional projects, the EESC feels that the EIB should also apply its conservative project risk evaluation criteria to project bonds. In particular, the EIB's exposure to risk should be clearly set out¹ and, if appropriate, should be limited. This possibility should be taken into particular consideration in connection with extending the instrument for the new EU budgetary period 2014-2020 having evaluated the experience gained during the pilot phase.
- 1.4 The EESC notes that the Commission's proposal makes too little mention of issues concerning the repayment of privately financed infrastructure projects. Particularly with regard to transport projects, there is a need for a broad-based public debate on the possible consequences of introducing user financing. The Committee also notes that the proposed instrument must not counteract policy decisions and social agreements aimed at sustainable economic, environmental and social goals. Perverse incentives for launching PPP projects must be avoided. The Committee therefore reiterates its position that the debt criteria for PPP projects must be equivalent to those for conventional public procurement projects.
- 1.5 The Committee takes the view that the proposed risk-sharing instrument for issuing project bonds will not be able to mobilise all of the investment required for urgent infrastructure projects. It therefore notes that it is necessary to mobilise additional sources of revenue for public budgets for public investments, referring in particular to the proposals to introduce a financial transaction tax.

2. **Introduction**

- 2.1 On 19 October 2011, the European Commission presented a number of legislative and non-legislative proposals for developing trans-European transport, energy and telecommunications networks and infrastructure, under the umbrella of the "Connecting Europe Facility" The proposals focus on the new budgetary period from 2014 to 2020, and relate in particular to eligibility guidelines, project selection, the amount of investment needed and new financing

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See also European Commission, Impact Assessment Board, DG ECFIN – Impact Assessment on a proposal for a regulation on the Europe 2020 Project Bond Initiative (draft version of 15 September 2011), point C 2 (Ref. Ares(2011) 1012531 - 23/09/2011), which calls for the risks for the EIB to be explained more clearly.

instruments in the areas mentioned. This opinion focuses on the financing aspects; the EESC is issuing further opinions covering the other elements².

- 2.2 The legislative proposal under discussion includes the following elements: extending the scope of the Competitiveness and Innovation Framework Programme for the current EU budgetary period (2007-2013) to include investments in broadband infrastructure; and launching a risk-sharing instrument for project bonds for investment in information and communications technology (ICT) and broadband, and in the trans-European transport and energy networks (TEN-T and TEN-E).
- 2.3 In light of the problems caused by the financial and economic crisis, the aim of the proposed instrument is to finance long-term investment using private capital. The intention is for additional funds to be raised on the capital markets for long-term infrastructure projects. The proposed instrument is a risk-sharing instrument for project bonds, which, by means of a contribution from the EU budget to the European Investment Bank, will enable the bank to reduce the credit risk for bond holders by means of subordinated loan capital or subordinated guarantees.
- 2.4 The legislative measure relates to a pilot phase in 2012 and 2013, during which the risk-sharing instrument's effectiveness in mobilising private investment will be tested.
- 2.5 The risk is shared between the EU and the EIB, with the financial contribution from the EU's budget being capped at EUR 230 million. The intention is that, in 2012 and 2013, up to EUR 200 million will be available for TEN-T projects and up to EUR 10 million for TEN-E projects, while up to EUR 20 million will be available in 2013 for investment in ICT and broadband infrastructure.
- 2.6 It is assumed that the subsidy from the EU budget will enable to EIB to cover the "first loss" over all implemented projects. The exact cap on the EIB's exposure to risk will be established contractually for each individual project. In theory, the maximum risk for the EIB is the sum of the contracts entered into minus the contribution from the EU budget. The Commission's legislative proposal does not, however, provide a nominal cap on the EIB's risk across all projects as it does for the EU budget: it states that "the residual risk inherent in all operations shall be borne by the EIB". It is up to the EIB to establish the residual risk as part of its risk analysis.
- 2.7 The Commission's aim with this instrument is to mobilise additional investment, particularly from private investors, and thus to produce a leverage effect. This is targeted primarily at investors such as insurance companies, pension funds and sovereign wealth funds that are looking for a secure, long-term investment opportunity.

² EESC opinion on the Connecting Europe Facility, EESC opinion on guidelines for trans-European telecommunication networks, and EESC opinion on guidelines for the trans-European transport network (not yet published in the Official Journal).

- 2.8 During the pilot phase, funding from the EU budget will be raised solely through redeployment, primarily of as-yet uncommitted funds from the existing Loan Guarantee Instrument for TEN-Transport Projects (LGTT).
- 2.9 Whereas the existing risk-sharing instrument LGTT involves the EIB covering risks for commercial creditors (banks), the legislative proposal under discussion involves the EIB covering risks for investors in project bonds. Both involve covering the debts of special purpose entities that undertake infrastructure projects, which in practice particularly relates to investment in the form of project financing and other public-private partnerships (PPPs). In such cases, it is usually project sponsors such as construction companies, infrastructure funds, operating companies and, in some cases, public companies who take responsibility not only for the construction but also for the operation, planning and, in particular, financing of investment projects.
- 2.10 The projects to be supported in the pilot phase have yet to be selected; three to eleven TEN-T projects, one TEN-E project and one or two ICT/broadband projects will be chosen. The experience gained from the pilot phase will be used to draw conclusions for the new EU budgetary period 2014-2020.
- 2.11 The Commission makes only passing reference to repayment issues in the legislative proposal and accompanying documents, but it is clear from an EIB paper on experience with the LGTT that this risk-sharing instrument is considered to be particularly suitable for user-financed projects³. The same is expected to apply to the projects targeted by this legislative proposal.

3. **General comments**

- 3.1 The EESC welcomes, in principle, the European Commission's proposal to establish a risk-sharing instrument for issuing project bonds for the envisaged pilot phase in 2012 and 2013. It would highlight both the opportunities and risks set out below, as well as the suggestions and conditions described, in particular for the continued use of the instrument following the pilot phase.
- 3.2 The opportunities reside primarily in the possibility of mobilising additional investment, thus increasing the impact of the EU budget. This could play a major part in generating growth and innovation, making the European economy more competitive, achieving the goals of the Europe 2020 strategy, and safeguarding and creating jobs. Executing the planned projects will help to make the benefits of European integration a tangible reality for the general public and thus strengthen the idea of Europe.

³ See European Investment Bank, Loan Guarantee Instrument for TEN-T Projects – Mid-term Review (2011), Luxembourg, 14 July 2011, p. 4.

- 3.3 The Committee nonetheless sees risks in the proposal, noting that there is an inherent link between the extent of the leverage effect and the risk taken on by the public authorities. These risks arise in particular from the possibility of having to absorb losses from the investment projects launched. While the Commission's legislative proposal puts a clear cap on the EU budget's exposure to risk, it assumes that, due to the individual contracts concluded between the EIB and the investors for each project and the EIB's distribution of risk between all the projects, the EIB's exposure to risk will not increase. In order to ensure that, should a risk materialise, it does not under any circumstances harm the EIB's credit rating or reputation, or the establishment and implementation of its conventional projects, it would be advisable to put reasonable limits on the use of the risk-sharing instrument in terms of the degree of risk assumed by the EIB on the basis of a clear assessment of its exposure to risk. In particular, the EIB's exposure to risk should be clearly set out⁴ and, if appropriate, should be limited. This possibility should be taken into particular consideration in connection with extending the instrument for the new EU budgetary period 2014-2020 having evaluated the experience gained during the pilot phase.
- 3.4 The evaluation of the Commission's proposal depends on the various policy goals pursued by the public authorities in representing the interests of the public, and on the financial interests of purchasers of project bonds; these may coincide, but may equally well contradict each other. The EESC recommends continuing and intensifying the public discussions on opportunities and risks before launching the new instrument, particularly for the 2014-2020 budgetary period. These discussions should be informed in particular by lessons learned from experience with project financing and PPP projects.
- 3.5 The EESC points out that the implementation of project financing makes it necessary for the project debt to be paid back through project-related income, in which context the issue of user financing takes on particular relevance. While the energy and telecommunications sectors are already characterised by this kind of financing, due to liberalisation and privatisation, in the transport sector, especially motorised private transport, it has so far been used in only a few Member States, mainly on motorways. This possible consequence needs to be discussed as part of a broad public debate prior to implementing planned transport projects.
- 3.6 The EESC calls for consideration to be given to denominating project bonds such that small savers can also buy them, so that the instrument is not only available to institutional investors.
- 3.7 The objective in launching the planned risk-sharing instrument should not simply be to achieve the greatest possible leverage effect to mobilise additional investment funds from private sources; it must also be ensured that the proposed instrument does not counteract policy decisions and social agreements aimed at sustainable economic, environmental and

⁴ See also European Commission, Impact Assessment Board, DG ECFIN, point C 2, *op. cit.* (see footnote 1).

social goals⁵. The investment projects launched by project bonds must not, for example, be based on disregarding social, environmental and quality standards. Execution of these projects must take due account of the quality of construction and maintenance, environmental sustainability, compliance with collective agreements and the place-of-employment principle, the need to support small and medium-sized enterprises, to promote innovation and to calculate costs on the basis of lifecycle costs, the social and environmental conditions of the drafting process⁶, and the need to guarantee accessibility for people with disabilities, provided these factors can be objectively verified and are based on non-discriminatory criteria. It must be ensured that users are not burdened with excessive fees, particularly those who need to make frequent, or even daily, use of certain transport infrastructure, and especially if no alternative infrastructure is available.

- 3.8 Based on these requirements, the EESC calls for the evaluation of the pilot phase of the project bond initiative to be continued and deepened on a broad social basis in good time before the political decision is taken to implement the risk-sharing instrument for project bonds for the new 2014-2020 EU budgetary period. This evaluation should also be informed by experience gained with the LGTT. There must, in particular, be transparency regarding the projects supported, the allocation of funds and the investment flows thus initiated; this will require ongoing follow-up and real time monitoring so that conclusions can be drawn in good time. The evaluation should involve political decision-makers at European, national, regional and local level, the social partners and civil society organisations, scientific, environmental and consumer protection organisations and social movements, and also the EESC and the Committee of the Regions. The European legislator should take a decision prior to the new budgetary period. The suggestion implicit in the Commission's documentation that an evaluation would not be undertaken until 2016/2017 is too late, in the EESC's view.
- 3.9 In terms of refinancing investment projects, the financial obligations imposed on the public authorities by project financing and PPP projects where repayment of the debt is guaranteed by public payments are equivalent to those for conventionally financed projects under public procurement. In order to guarantee adequate budgetary transparency, avoid additional budgetary risks and perverse incentives for launching PPP projects, and ensure that competent authorities have freedom of choice between PPP projects and conventionally financed projects, the EESC reiterates that the debt criteria for PPP projects must be equivalent to those for conventional public procurement projects⁷.

⁵ The CER made similar sceptical comments on the implementation of the proposed risk-sharing instrument for rail; see Stakeholder Consultation on the Europe 2020 Project Bond Initiative, Response of the Community of European Railway and Infrastructure Companies (CER), 6 May 2011, available at: http://ec.europa.eu/economy_finance/consultation/pdf/community_of_european_railway_and_infrastructure_companies_cer_en.pdf.

⁶ See also the EESC opinion on the *European Procurement Market*, OJ C 318, 29.10.2011, p. 113.

⁷ EESC opinion on *Private and public investment*, OJ C 51, 17.2.2011, p. 59; see also House of Commons, Treasury Select Committee, Private Finance Initiative, Seventeenth Report of Session 2010-2012, London 18 July 2011. This report notes that the fact that PFI/PPP projects are not included in the public debt results in perverse incentives that run counter to the objective of "best value for money". The Chairman of the House of Commons Treasury Select Committee, Andrew Tyrie MP (Conservative), clearly calls for such projects to be included in the fiscal rules (cf. <http://www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/news/pfi-report/>).

3.10 Unlike certain transport projects, many energy and telecommunications infrastructure projects in the EU are generally privately funded, and are refinanced via usage fees, which are regulated. This includes the overall network infrastructure. In this connection, the EESC wonders what additional projects the European legislator is hoping to promote under the proposed financing instrument that apparently cannot be fully refinanced through regulated usage fees. In the Committee's view, a detailed justification should be provided for every proposed energy or telecommunications project, explaining why it is necessary for EU development, despite the lack of refinancing opportunities. It is absolutely vital for such projects to be verified by the European legislator.

4. **Specific comments**

4.1 The proposed risk-sharing instrument is a potential solution to the problems set out by the European Commission – i.e. inadequate public investment and the existence of as-yet-uninvested capital, particularly among institutional investors. It does, however, also raise various technical questions that need to be answered along with the policy requirements set out in section 3. The Committee recommends that these questions be clarified before the proposed risk-sharing instrument is created, or at the latest by the time it is introduced, as intended, in the new EU budgetary period 2014-2020.

4.2 Overall, the EESC takes the view that the EIB and the EU budget should not just cover risks, but also be entitled to an appropriate share of the profits ("fair risk sharing"). This should be ensured by systematically applying the EIB's risk and pricing policy and the other measures proposed here to limit the EIB's exposure to risk.

4.3 The exact roles of the stakeholders are also not entirely clear, in particular who will replace the bond insurers (monolines) as single controlling creditor, or how this will happen. It is particularly unclear what role the EIB will play here. This is to be determined in future agreements with the investors and a contract between the Commission and the EIB. The EESC therefore calls on the European legislator to clarify the technical details of the risk regime and the extent of the EIB's operation as controlling creditor as part of the pending legislative process, at least before the instrument is extended for the new EU budgetary period 2014-2020, in order to provide certainty for investors and the public authorities. The planned risk-sharing instrument must under no circumstances lead to the EIB's credit rating and reputation being put at risk.

4.4 Experience gained from LGTT projects should be systematically assessed against the criteria set out in section 3, with a view to drawing conclusions regarding appropriate project design for the risk-sharing instrument for project bonds and helping to avoid negative consequences⁸.

⁸ In this connection, see also European Investment Bank, *op. cit.* (see footnote 3), although this document does not examine a number of the criteria listed in section 3.

It is, however, also necessary in this connection to clear up the differences of opinion that have arisen in the assessment of PPP projects by the various parties involved.

- 4.5 In view of both positive and, in many cases, negative experiences with and risks involved in project financing and PPP projects – in terms of the length of contract negotiations, the complexity of contract provisions and relationships between parties and the uncertainty regarding the impact on demand – the EESC wonders whether the best solution might be to provide public budgets with the resources they need to launch investment projects in the context of conventional public procurement⁹. In this connection, the Committee welcomes the Commission's proposal to introduce a financial transaction tax and reiterates its support for the introduction of this type of revenue source for public budgets¹⁰.
- 4.6 The EESC would also point out in this connection that the issuing of project bonds will not on its own be able to guarantee the levels of investment that the Commission has determined as necessary for the "Connecting Europe Facility". It therefore recommends mobilising additional sources of revenue for public investments.

Brussels, 23 February 2012.

The President
of the
European Economic and Social Committee

Staffan Nilsson

⁹ This concept of a best and second-best solution can also be found in the response of the Community of European Railway and Infrastructure Companies (CER) to the consultation on the legislative proposal under discussion. Cf. CER, *op. cit.* (see footnote 5).

¹⁰ EESC opinion on *Financial transaction tax*, OJ C 44, 11.2.2011, p. 81, and EESC opinion on the *Report of the de Larosière Group*, OJ C 318, 23.12.2009, p. 57.