



JESSICA

***JOINT EUROPEAN SUPPORT FOR
SUSTAINABLE INVESTMENT IN CITY AREAS***

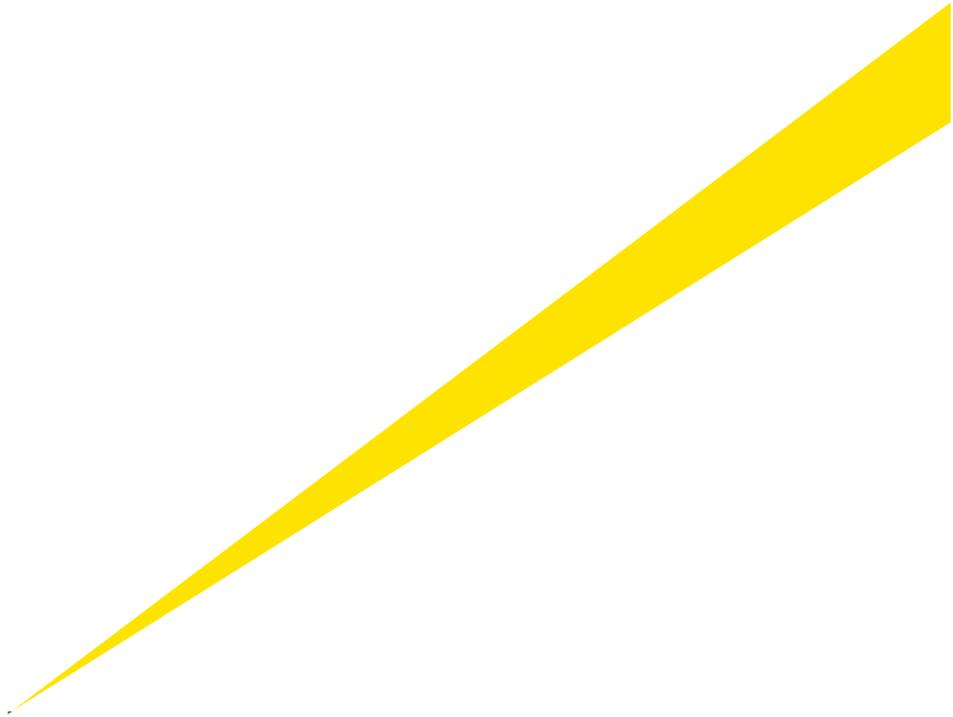
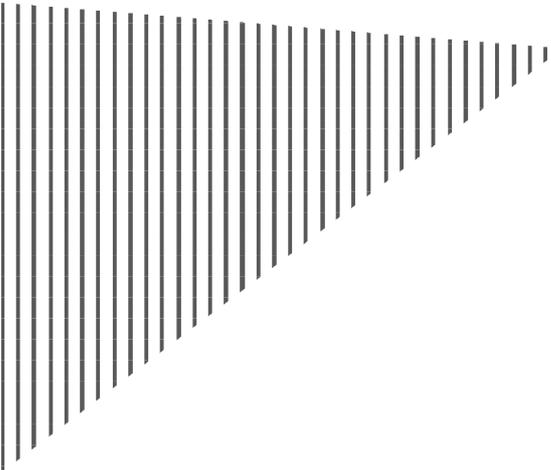
***Implementing JESSICA in the North-East
Cohesion Region, Czech Republic***

EVALUATION STUDY

English version

September 2010

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Implementation of the JESSICA financial instrument in the Northeast Cohesion Region, Czech Republic

Final Report

September 2010

Christos Kontogeorgos
European Investment Bank
JESSICA Task Force
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14 September 2010

Dear Mr Kontogeorgos,

In accordance with our contractual agreement dated 19 April 2010, we are pleased to present you with our final report (the Report) as part of the evaluation study "Implementation JESSICA in the Northeast Cohesion Region in the Czech Republic" (the Project).

The European Investment Bank (the EIB) has selected Ernst & Young s.r.o. (EY) for the implementation of the Project. The objectives of this Report are to produce a document through which it will be possible to initiate discussion on the implementation of the JESSICA instruments with NUTS II in the Northeast cities and regions.

This final report includes:

- ▶ Brief situational analysis containing a summary of the Regional Operational Programme, NUTS II, in the Northeast region and its funding availability;
- ▶ Analysis of the urban development plans and their equivalents;
- ▶ Funding model of the JESSICA instrument based on selected projects;
- ▶ Draft implementation structures of the JESSICA instrument and a draft action plan.

The data and information contained in this report were obtained from representatives of regional institutions between 19 April 2010 and 7 July 2010. Therefore, this report can not take into account any circumstances that occurred after that date. EY has not verified the accuracy of this data. Economic assumptions and calculations introduced in this report are valid only for the period in which they were created and are subject to change at any time.

The Report is designed for your purposes and EY does not assume any responsibility for any third party to whom the Report may be presented or who may become otherwise familiar with the Report.

If you have any questions, please contact me by phone (+420 225 335 582) or by mail (petr.knap@cz.ey.com).

Yours sincerely

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1. Executive Summary

A key task of EU structural funds is to lay the groundwork for long-term urban development. The subsidy-based instruments in place to distribute ERDF resources cannot alone be relied upon to meet this objective due, inter alia, to the attendant financial demands. Hence, the Joint European Support for Sustainable Investment in City Areas (JESSICA) instrument was launched based on an initiative of the European Commission (“EC”) and EIB in collaboration with the Council of the European Development Bank – CEB. As designed, the instrument respects existing regional operational programme conditions while introducing a new opportunity to secure assistance for long-term urban development via preferential repayable funding, which should not only provide for the use of allocated financial resources multiple times, but also for private investor involvement in long-term urban development. JESSICA funding, which may take the form of equity investments, loans or guarantees, would be provided through Urban Development Funds. Successful JESSICA application is contingent on setting up project requirements in the sense of financial repayability, the preference for repayable funding over subsidies, where appropriate, or a favourable approach to closer cooperation between regions and cities, on one hand, and private investors, on the other.

While this report was being developed, emphasis was placed not only on analytical work using available information and documents at the European and national levels, but also on specific local requirements of the Northeast Region. A key specific is the existence of three centres with differing regional features and needs, which were discussed with representatives of these cities and with the representatives of regions.

We can at present state that sufficient financial resources continue to be available in the ROP for the pilot phase of JESSICA implementation in the Northeast Cohesion Region, e.g. in comparison with the size of some existing JESSICA funds in Europe. This conclusion holds even though the remaining ROP NE allocation is not definitive, for it must be understood in the context of the fulfillment to date of ROP NE indicators or over-use by some support areas, as well as the plan for future calls for submissions.

The following areas of support were identified as potentially suitable for the utilization of the JESSICA instrument in the context of the Regional Operational Programme NUTS 2 Northeast (ROP NE): 2.1 Development of Regional Centres, 2.2 Development of Cities, 3.1 Development of Basic Infrastructure and Supporting Activities in the Field of Tourism and 4.1 Support for Development of Entrepreneurial Infrastructure (for more information, see Chapter 3).

To evaluate existing projects suitable for JESSICA funding, this study selected a total of 14 potentially suitable projects from a list of 569 projects submitted with grant funding applications for Support areas 2.2, 3.1 and 4.1 (using criteria determined by EY, which respect the basic implementation characteristics of JESSICA). Support area 2.1 was examined separately, as were any other project proposals in the region that met JESSICA requirements. An analysis was also performed of certain individual projects identified during study execution, some of which had sought grant funding in the past and some of which had not. The study yielded 3 projects to which a JESSICA funding application model was applied in the form of a loan from UDF. The results indicate that we may not expect JESSICA financing to be used across the board, but to be applied to specific, carefully selected projects that generate socio-economic benefits while guaranteeing certain financial return. Such projects can be found, for example, in the fields of tourism, sports & leisure, hospital infrastructure or urban brownfield revitalization.

The main advantages (added value) of implementing JESSICA in the region are expected to be as follows: (i) regional and local authorities will acquire practical experience with utilizing EU structural funds through revolving instruments and will be better prepared for the next EU financial period; (ii) resources returned to UDFs will be available for reinvestment in the region; (iii) more private investment will enter regional development projects (e.g. through co-investment into UDF-financed projects); (iv) realization of revenue-generating projects which have socio-economic benefits but currently are not fully commercially viable; and (v) unlocking of the region's latent capital for future investment.

We shall consider three different variants for JESSICA implementation, which may be combined in various combinations. When selecting the most suitable implementation variant for the Northeast Region, we bore in mind regional specifics, timing and key subsidy allocation requirements. Taking the foregoing perspectives into account, the application of the “Holding Fund” variant, where the respective entity serves as an intermediary between the RC NE and a sole UDF, represents the implementation variant best suited to the stated goal. The UDF would invest directly in projects in the Northeast Region. This

variant which involves a Holding Fund provides for a faster transfer of financial resources from the ERDF to a JESSICA Fund. This timely transfer could incentivise potential UDF administrators to draft business plans and potential implementers of financially repayable projects to prepare such projects. Moreover, the speedy creation of a Holding Fund facilitates the allocation of unused operational programme resources (for which no future calls for submissions are planned) in the form of repayable financial resources from subsidy recipients. From a timing perspective, then, this assures adherence to the N+2 (N+3) rule. Other benefits of this variant include a simplified Urban Development Fund selection and monitoring process from the point of view of the RC NE (for more information, including the implementation variants under consideration, see Chapter 5).

It must be noted that the creation of the JESSICA Fund, establishment of its investment strategy, selection of a manager and preparation of any related changes in the ROP would be more easily implementable in the case of the clear appropriation of resources for transfer to the JESSICA Fund than in a case where questions of the amount and source of resources to be transferred to the JESSICA Fund were to be left open. Aside from the administrative demands of implementation based on an unspecified amount of resources, we must consider the fact that the use of resources allocated to the JESSICA Fund as part of the ROP will be tied to the specific requirements of the support areas from which resources are transferred to the Fund (e.g. types of projects and costs that may be funded in a given support area).

The decision on JESSICA implementation should be made as soon as possible, not only due to the diminishing allocation in the ROP NE, but also in connection with possible under-use in some support areas, the return of subsidy resources for failure to adhere to the relevant requirements and the reallocation of unused resources from thematic operational programmes. Moreover, JESSICA implementation could serve as grounds for the allocation of additional resources from structural funds that would provide for a bridging period between the end of one operational programme and start of another. Of further significant benefit here is the use of the RC NE Authority apparatus already in place for implementation of this instrument (for information on the implementation procedure in the form of a skeleton action plan, refer to Chapter 6).

2. Introduction

Joint European Support for Sustainable Investment in City Areas (“JESSICA”) is an initiative of the European Commission (EC) and the EIB, supported by the Council of the European Development Bank (CEB). The objective of this initiative is to support the realization of revenue-generating and sustainable urban development projects within the framework of Operational Programmes of EU structural funds. These projects can be funded through loans, guarantees or equity investments from Urban Development Funds (UDFs).

Although JESSICA does not represent a new source of funding, it allows existing resources to be used in a manner that is innovative as compared to current practice in the Czech Republic. The key principle when using resources through JESSICA is an emphasis on the return of resources to JESSICA funds (the “revolving” principle). This stands in contrast to the traditional use of Operational Programme resources through one-off grants.

This principle should help to increase the overall quality of approved projects, and allows repeated investment into new urban development projects of resources returned to the UDF from previous projects. Depending on the financial return of a given project, it may be funded either entirely through repayable funding (including JESSICA funding) or by a combination of grants and JESSICA funding.

2.1. JESSICA and its basic characteristics

As a project funding instrument, JESSICA represents a new method of using existing allocations of financial resources available under Operational Programmes. The *raison d’être* of JESSICA includes the need for more efficient and effective use of European Regional Development Fund resources and the need to develop regional investment structures that are more financially sustainable than grants.

JESSICA funding, which may take the form of equity, loans and/or guarantees, is delivered to projects via Urban Development Funds. Managing Authorities can either create UDFs directly (by selecting a UDF manager and entering into a Funding Agreement with it) or can use the services of a JESSICA Holding Fund, which helps to select the UDF manager and set the contractual obligations of the UDF (through an Operational Agreement between the HF and the UDF).

For regions, cities and other actors involved in urban development in the Northeast Cohesion Region, JESSICA can enable the implementation of projects which (either as they are or after partial re-working) fulfil the following terms and conditions:

- ▶ The project or its part reports financial returns, albeit not in an amount that would be attractive for the private sector. As an urban development policy instrument, however, JESSICA should not support projects with a combination of risks and financial return, where the project in and of itself would be of financial interest to the business sector (investment made through JESSICA should attract, not drive away, private investment).
- ▶ The project is (or, subject to certain modifications, could be) eligible for funding under the Regional Operational Programme NUTS II Northeast (ROP NUTS II NE).
- ▶ The project is a part of an Integrated Urban Development Plan (IUDP) or of a document of the same nature.

JESSICA is a project funding mechanism that may be successfully implemented when certain investment management conditions are met by cities or regions. The key conditions are:

- ▶ Sufficient quantity of project concepts suitable for JESSICA funding by means of clearly identified conditions and appropriate publicity.
- ▶ Systematic efforts focused on structured project preparation with regard to the development of the city and the possibility of achieving certain financial return on investment, i.e. efforts focused on searching for activities/services/products generating financial flows;

- ▶ Readiness of city or region representatives to take on the (new) role of entrepreneur. This new role will place greater demands on city and regional leaders. In the event of JESSICA project funding, emphasis will be placed on repayable funding rather than subsidies. At the same time, the “right instrument for the right investment” shall have to be created, i.e. a system for active asset management and strategic planning that is further reflected when drafting calls for project submissions targeted at private entities.
- ▶ Strengthening of regions’ or cities’ cooperation with business, which may be assisted by the EIB or other specialized institutions or consultants and could help not only with setting up project funding via JESSICA, but also with training staff to administer these financial resources.

2.2. Project design approach

2.2.1. Implementation approach and procedure (methodology)

This project was carried out from March 2010 to July 2010; therefore, the information provided in this report is current as of the project implementation period. Given the scope of the mandate from the EIB, the timing and subject matter, the following project implementation procedure was selected:

- ▶ Gathering of available data sources and identification of key project implementation stakeholders.
- ▶ Documentation of key region characteristics and an evaluation of Northeast Region project readiness for JESSICA implementation. This included an analysis of the region, an analysis of support to cities under ROP NUTS II NE and an analysis of urban development support under ROP NUTS II NE (Support area 2.1). In this phase, we also analysed documents of regional municipalities that were related to sustainable urban development. This information is summarised in Chapter 3.
- ▶ Options for the JESSICA funding of selected projects were analysed in Chapter 4. The analysis included a selection of projects already submitted to the ROP NE based on criteria rendering them suitable for the JESSICA financial instrument.
- ▶ Three implementation structures are presented and evaluated in Chapter 5.
- ▶ An action plan for JESSICA implementation in the ROP NE region is proposed in Chapter 6.

2.2.2. Background documents and literature

Project implementation necessitated a review of extensive documentation. Some key documents were:

- ▶ Regional Operational Programme NUTS II NE, ROP NE Implementation Document, guides, calls for submission;
- ▶ Monthly ROP NE Resource Use Analyses (February, March, April and May 2010);
- ▶ Integrated Urban Development Plans submitted within the ROP NE (IUDP Pardubice Attractive City, IUDP Hradec Králové City Centre = Pole of Growth and Development, IUDP Liberec Lidové sady Park), sub-projects;
- ▶ Working documents of IUDP Liberec An Attractive and Quality Life in Liberec;
- ▶ Integrated Urban Development Plans submitted within the IOP (IUDP Hradec Králové – Edvard Beneš Avenue, IUDP Chrudim, IUDP Jablonec nad Nisou, IUDP Liberec – Regeneration of Rochlice Housing Estate, IUDP Náchod – Problem Area near the Hospital, IUDP Pardubice – Dukla and Višňovka Housing Estates.
- ▶ Strategic and conceptual documents at the regional level:
 - ▶ Liberec region: Liberec Region Development Strategy 2006-2020, Liberec Region Development Programme 2007-2013, Ongoing monitoring 2007, 2008;

- ▶ Hradec Králové region: Hradec Králové Region Development Strategy 2007- 2015, Hradec Králové Region Development Programme 2008-2010, Evaluation reports and monitoring;
- ▶ Pardubice region: Pardubice region Development Programme;
- ▶ Strategic and conceptual documents at the city level (Statutory City of Liberec Development Strategy 2007-2020, City of Hradec Králové Strategic Development Plan through 2020, City of Pardubice Strategic Development Plan for the Further Planning Period 2007-2014, City of Jablonec nad Nisou Strategic Plan 2003-2015, City of Česká Lípa Strategic Development Plan, Trutnov Strategic Plan – 2008-2009 update, Náchod Strategic Development Plan through 2020, City of Chrudim Strategic Development Plan including Action Plans and others);
- ▶ Draft Pardubice Region Territorial Development Principles, Draft Hradec Králové Region Territorial Development Principles, working material derived from the Liberec Region Territorial Development Principles;
- ▶ Operational programmes and implementing documents (Integrated Operational Programme, Operational Programme Business and Innovation, Operational Programme Research and Development for Innovation, Operational Programme Environment and others);
- ▶ Working documents provided by the ROP NE Regional Council Authority;
- ▶ Methodological Directive issued by the Ministry for Local Development on the main principles for Integrated Urban Development Plan preparation, evaluation and approval (pursuant to Czech Government Resolution No. 883 of 13 August 2007);
- ▶ EU legislation, in particular Council Regulation (EC) 1083/2006, as amended, Council Regulation (EC) 1080/2006, as amended, and Commission Regulation (EC) 1828/2006, as amended;
- ▶ Public databases and information from the Czech Statistics Office.

2.2.3. Communication with key stakeholders

The EIB, with the assistance of EY and other key organisations, organized two presentations with the aim of introducing the project and then presenting its results.

The introductory presentation took place on 19 March 2010 at the Pardubice Regional Authority offices with the participation of key representatives from all 3 regions comprising the NUTS II NE region. At this presentation, EIB staff introduced past experience with JESSICA funding implementation while EY discussed the basic approach to the project, its timeline and objectives.

This was followed on 14 June 2010 by an EY presentation (at the same location) of the original proposal for JESSICA implementation in the NUTS II NE region. The presentation further included a model for JESSICA use on a selected project from this region. Pardubice Region Commissioner Radko Martínek, who also serves as Northeast Cohesion Region Council Chair, took part in the presentation, which was followed by a discussion whose outcome is incorporated into this report.

Project implementation further required face-to-face meetings with key stakeholders. These meetings served not only as a source of information, but also as an opportunity to familiarise key stakeholders with the JESSICA financial engineering instrument. During project preparation, meetings were held with:

- ▶ Bc. Stanislav Eichler, Liberec Region Commissioner;
- ▶ Bc. Lubomír Franc, Hradec Králové Region Commissioner;
- ▶ Mgr. Zdeněk Semorád, Director of the Office of the RC NE (on behalf of Mgr. Radko Martínek, Pardubice Region Commissioner and RC NE Chair);
- ▶ Ing. Pavel Kalivoda, Director, Department of Strategic Development of the Region and European Funds, Office of the Pardubice Region;
- ▶ Mgr. Miroslav Smejkal, Director, Regional Development and Tourism Department;

- ▶ Mgr. Michael Otta, Director, Department of Strategic Development of the Region and European Projects, Regional Agenda of the Liberec Region;
- ▶ Ing. Klára Dostálová, Director, European Projecting Centre, Hradec Králové Region;
- ▶ Ing. Oldřich Čtvrtečka, Mayor of the City of Náchod;
- ▶ Ing. Stanislav Klik, Ph.D., Bursar, Hradec Králové University.

During project preparation, we could not have conducted suggested interviews with following important regional bodies:

- ▶ Ing. Jiří Kittner, City mayor of Liberec;
- ▶ Ing. Jiří Klepsa, Mayor of Jaroměř;
- ▶ CzechInvest, regional agencies (Hradec Králové, Pardubice, Liberec).

3. Situation Analysis

3.1. NUTS II Northeast Cohesion Region and its position within the Czech Republic

The NUTS II Northeast Cohesion Region (NUTS II NE) consists of the Hradec Králové Region (with the city of Hradec Králové as its centre), the Pardubice Region (with the city of Pardubice as its centre), and the Liberec Region (with the city of Liberec as its centre). The centres of all three regions are situated some 100 km from Prague. The area of NUTS II NE is 12,440 km², i.e. 15.8% of the total area of the Czech Republic. At 1 January 2009, the region had 1,507,000 inhabitants (15% of the total population of the Czech Republic), with 70% of these living in cities. All three regional centres have approximately the same population (100,000). The following towns in the region have a population of 20,000 to 50,000: Jablonec nad Nisou, Česká Lípa, Trutnov, Chrudim and Náchod. The following tables show basic characteristics and comparisons of the NUTS II NE region.

Table No. 1

Basic characteristics of the NUTS II NE region

	Population 31 December 2009	Gross salary (1st quarter 2010)	Unemployment rate 31 May 2010
Hradec Králové Region	554,251	CZK 19,689	7.37%
Pardubice Region	516,471	CZK 19,340	8.7%
Liberec Region	439,012	CZK 20,445	10.67%

Source: CSO

Table No. 2

Urban areas in the NUTS II NE region with more than 20,000 inhabitants

City	Population (1 January 2010)	Region
Liberec	101,625	Liberec
Hradec Králové	94,493	Hradec Králové
Pardubice	90,077	Pardubice
Jablonec nad Nisou	45,328	Liberec
Česká Lípa	38,104	Liberec
Trutnov	31,005	Hradec Králové
Chrudim	23,323	Pardubice
Náchod	20,760	Hradec Králové

Source: CSO

3.2. Urban space problems in the NUTS II NE region

Market failures on a regional level can have a host of manifestations and causes. In both economic theory and subsequent decision-making practices affecting financial assistance from EU public funds, two usual sources of market failure are defined – externalities and asymmetric information. Public institutions may initiate changes in these problematic areas, most often in the form of financial benefits.

By their nature, problematic areas concerning the urban space of the NUTS II NE region correspond to those problems experienced in other parts of the Czech Republic. Past urban development in the region's cities has been greatly influenced, inter alia, by industrial production (textile and glass production) and military history. The 2007 document "Regional Operational Programme NUTS II Northeast for the Period 2007-2013" defined the greatest problems facing urban spaces as follows:

- ▶ Overburdened transport infrastructure with negative environmental impacts (noise, exhaust emission);
- ▶ Insufficient green space and areas for day-to-day recreation (relaxation) for the population;
- ▶ Greater occurrence of socially pathological manifestations as a result of greater anonymity, the greater abundance of socially weak and inflexible citizens and their concentration in certain localities;
- ▶ The existence of unused, primarily industrial, complexes (brownfields) resulting from economic and industrial transformation.

Project execution included working meetings with commissioners and senior staff in the field of regional development in the NUTS II NE region. These meetings were used to provide detailed information about areas of interest and preferences of regional authorities in addressing problems currently facing urban space development in the NUTS II NE region in connection with pending JESSICA funding implementation. The following areas were identified:

- ▶ Development of healthcare infrastructure: projects to overhaul the Pardubice region hospital network (hospitals located in Pardubice, Chrudim, Svitavy, Litomyšl and Ústí n O.), projects to renovate Náchod Regional Hospital;
- ▶ Development of social infrastructure: modernization of the children's home in Pardubice into a family-type home, social welfare projects for the Liberec region (group homes under social welfare administration, homes for seniors and the handicapped);
- ▶ Revitalization of urban brownfields for tourism (and the spa industry): renovation of Běloves Spa, Náchod;
- ▶ Revitalization of dilapidated and unused historical buildings within city limits: revitalization of the Jaroměř-Josefov former military complex, renovation of the Jesuit college on u Valdštejnova Square in Jičín, renovation of the historical building housing the Institute for the Deaf and Mute in Hradec Králové;
- ▶ Development of urban transport infrastructure: revitalization of the area in front of Pardubice railway station, projects to address transport needs in Liberec region cities (e.g.: tram to Rochlice, renovation and building of transport terminals in Semily, Liberec and other cities in the region).

The above are examples of types of projects that can both bring socio-economic benefits and have revenue-generating potential, hence they could be potentially financed (in full or in part, depending on the specific case), on a repayable basis from a UDF. Taking into account also the impact of the financial and economic crisis on municipal budgets, it cannot be expected that municipalities will be able to cover the realization of these types of projects from their budgets; hence new sources of funding are needed.

3.3. Regional Operational Programme NUTS II Northeast – financial resources in support of urban development

Projects supporting the development of urban areas may be funded in NUTS II NE primarily under the following operational programmes:

- ▶ The Regional Operational Programme NUTS II Northeast (ROP NUTS II NE);
- ▶ The Operational Programme Business and Innovation (OP PI);
- ▶ The Integrated Operational Programme (IOP);
- ▶ The Operational Programme Research and Development for Innovation (OP VaVpl);
- ▶ The Operational Programme Environment (OP ŽP).

The Regional Operational Programme NUTS II NE (ROP NE), which is broken down into the following priority axes and support areas, may be identified as the most important operational programme supporting urban policy in the NUTS II NE region.

Table No. 3

Priority axis	Support area	Name
1		Development of Transport Infrastructure
	1.1	Development of Regional Road Transport Infrastructure
	1.2	Support for Projects Improving Regional Transport Serviceability
	1.3	Development of International Public Airports
2		Development of Urban and Rural Areas
	2.1	Development of Regional Centres
	2.2	Development of Cities
	2.3	Rural Development
3		Tourism
	3.1	Development of Basic Infrastructure and Ancillary Activities in Tourism
	3.2	Marketing and Coordination Activities in Tourism
4		Development of the Business Environment
	4.1	Support for Business Infrastructure Development
	4.2	Support for the Development of Cooperation with Secondary Schools, Training Institutions and Other Regional Educational Institutions and Labour Offices, Development of Innovative Activities in the Region
5		Technical Assistance
	5.1	Support for ROP NE Implementation and Management Activities
	5.2	Support for NE Cohesion Region Absorption Capacity

Projects with an urban development focus in ROP NE are included primarily in Priority axis 2 Development of Urban and Rural Areas, of course with the exception of area 2.3, which is designed for municipalities with up to 5,000 inhabitants. Support areas 2.1 Development of Regional Centres and 2.2 Development of Cities directly target support for urban development. These support areas comprise activities designed to promote investment in urban settlements, helping to increase their attractiveness and stability as a part of sustainable development (regeneration and revitalization of brownfields, renewal of selected urban districts). Investment may also favour the development of human resources potential (infrastructure development in education, further education, healthcare and social affairs).

The aim of Support area 2.1 Development of Regional Centres is to strengthen the role of cities as poles of growth and regional development. Support is only provided via the IUDP. The IUDP budget minimum was set at EUR 10 million with the aim of achieving a sufficient concentration of resources and preventing their dispersion. Moreover, the ROP NE Managing Authority has undertaken to try to ensure an average IUDP value of EUR 15 million. IUDPs may have the following fields of concentration:

- ▶ Deprived areas suffering from a high concentration of negative phenomena, e.g. high unemployment, criminality, social exclusion;
- ▶ Territories with high growth potential, where the leveraging of structural funds will bolster competitiveness;
- ▶ Thematic focus – a set of measures within one or more thematic areas: Attractive Cities, Environment, Accessibility and Mobility, Economic Development, Social Integration, Public Affairs Administration.

Cities with a population in excess of 50,000 are obliged to prepare an IUDP. In the NUTS II NE region, this means the cities of Liberec, Hradec Králové and Pardubice.

ROP NE also promotes the development of urban units by supporting activities designed to introduce long-term sustainable development principles. Priority axis 1 Development of Transport Infrastructure comprises, inter alia, activities supporting eradication of the adverse impacts of transport on the population and environment, the building of integrated transit systems and development of municipal mass transit. Support area 1.3 Development of Regional Airports will be implemented in a strictly urban setting. Priority axis 3 Tourism fosters development of the urban environment, in particular via Support area 3.1 Development of Basic Infrastructure and Ancillary Activities in Tourism. This support area is primarily designed to support the revitalisation of cultural, historical and technical monuments and the modernisation and upgrading of basic tourism infrastructure capacities and the renewal and development of ancillary infrastructure for tourism. Priority axis 4 Development of the Business Environment focuses on strengthening urban spaces and cities, in particular via Support area 4.1 Support for Business Infrastructure Development. Support area 4.1 comprises activities targeted at investment in transport and technical infrastructure.

At 31 May 2010, the Regional Council of the Northeast Cohesion Region (henceforth “RC NE”) had issued 29 calls for project application submissions for the provision of subsidies under the ROP NE. The total financial allocation from structural funds (henceforth “SF”) for the announced calls is CZK 14,267 million, representing 83.6% of the SF financial allocation for the ROP NE. A total of 1,090 project applications for subsidies under the ROP NE was registered with an aggregate SF funding request of CZK 27,183 million, representing 159.3% of the total SF financial allocation for the ROP NE. The Committee of the NUTS II NE Regional Council (henceforth the “CRC”) approved some 373 projects from the ROP NE for support with an aggregate SF funding request of CZK 9,192 million (representing 53.9% of the total financial allocation from SF for the ROP NE). Based on a downward revision of total eligible expenses for previously approved projects now in the implementation phase, or a reduction in the number of projects (e.g. as a result of project non-implementation by the applicant or contract non-execution due to non-fulfilment of contractual conditions), the number of projects approved for support from ROP NE fell to 366 while the aggregate SF funding requirement of approved projects dropped to CZK 8,659 million.

Table No. 4

ROP NUTS II NE allocation and balance at 31 May 2010

Priority axes / support areas	Allocation share in %	Allocation from SF 2007-2013 (in EUR)	Committed SF allocation (at 31.5.2010)		Remaining allocation for planned calls (at 31.5.2010)		
			EUR	CZK	EUR	%	CZK
1 Development of Transport Infrastructure	37%	242,889,314	208,954,500	5,432,817,012	33,934,814	14	882,305,152
1.1. Development of Regional Road Transport Infrastructure	61%	147,878,054	121,634,022	3,162,484,561	26,244,032	17.7	682,344,843
1.2. Support for Projects Improving Regional Transport Serviceability	34%	82,866,794	79,051,248	2,055,332,451	3,815,546	4.6	99,204,193
1.3. Development of International Public Airports	5%	12,144,466	8,269,231	215,000,000	3,875,235	31.9	100,756,116
2. Development of Urban and Rural Areas	34%	223,195,587	215,595,241	5,605,476,268	7,600,346	3.4	197,608,994
2.1. Development of Regional Centres	39%	87,051,270	78,395,007	2,038,270,189	8,656,263	9.9	225,062,831
2.2. Development of Cities	41%	91,505,200	85,606,603	2,225,771,677	5,898,597	6.4	153,363,523
2.3. Rural Development	20%	44,639,117	51,593,631	1,341,434,402	-6,954,514	-15.6	-180,817,360
3. Tourism	22%	144,420,673	123,316,885	3,206,239,009	21,103,788	14.6	548,698,489
3.1. Development of Basic Infrastructure and Ancillary Activities in Tourism	92%	132,867,021	115,278,070	2,997,229,811	17,588,949	13.2	457,312,683
3.2. Marketing and Coordination Activities in Tourism	8%	11,553,652	8,038,815	209,009,198	3,514,839	30.4	91,385,806
4. Development of the Business Environment	4%	26,258,304	17,948,975	466,673,339	8,309,329	31.6	216,042,565
4.1. Support for Business Infrastructure Development	85%	22,319,557	14,243,527	370,331,714	8,076,031	36.2	209,976,794
4.2. Support for Development of Cooperation with Secondary Schools, Training Institutions and Other Regional Educational Institutions and Labour Offices	15%	3,938,747	3,705,447	96,341,625	233,299	5.9	6,065,771
5. Technical Assistance	3%	19,693,728	13,482,169	350,536,384	6,211,559	31.5	161,500,544
5.1. Support for ROP Northeast Implementation and Management Activities	89%	17,443,728	11,644,496	302,756,890	5,799,232	33.2	150,780,038
5.2. Support for Northeast Cohesion Region Absorption Capacity	11%	2,250,000	1,837,673	47,779,494	412,327	18.3	10,720,506
Total ROP NE		656,457,606	579,297,770	15,061,742,012	77,159,836	11.8	2,006,155,744

Source: RC NE Authority

Note: The Committed allocation column presents the sum total of financial resources approved within aggregate application, the current requirement of approved projects not yet included in approved aggregate application and the allocation of planned and already announced calls where CRC project approval has not yet been conducted. The Remaining allocation for planned calls column includes remaining financial resources from SF within the ROP NE, i.e. the difference in the 2007-2013 SF allocation and total committed SF allocation.

Applicants currently have the options of submitting a subsidy application for a call in Support area 4.2 and a controlled call in Support area 3.1. An open call from Support area 2.1 is also ongoing for submitters of IUDP sub-projects. A call in Support area 1.3. with an allocation of CZK 215 million has been ongoing since 8 June 2010. The call was announced after 31 May 2010; therefore, the allocation is not reflected in the table below. The announcement of a call in Support area 1.1 is planned for November 2010.

According to the most recent information, available financial resources within the ROP total EUR 77 million, which drops to roughly EUR 70 million once the allocation for announced call 1.3 is deducted. However, this amount does not represent the definitive ROP NE allocation balance, as this must still be analysed in the context of the hitherto fulfilment of ROP NE indicators and the plan for future calls. We may also expect that in every support area a certain portion of resources will once again become available due to non-use of the full planned allocation (a reduction in the total requirement for financial resources of approved projects) in a given support area.

Hence, based on an analysis of possible funding sources within the ROP NE, it may be assumed that sufficient financial resources continue to be available within the ROP for the pilot phase of JESSICA implementation in the NE region. There is no predicting, whether the RC NE will decide to apply available financial resources as a one-off allocation of a certain amount for JESSICA creation or whether it will prefer to use up these grant resources and then only gradually transfer what remains in the form of unused allocations from various support areas to the JESSICA Fund¹.

An analysis of potential resources within the ROP NE clearly indicates that JESSICA implementation in the NE region would be facilitated by any additional allocation of resources to the ROP, e.g. through reallocations from thematic operational programmes that have used fewer resources than planned.

3.4. Analysis of urban development support within ROP NUTS II Northeast (Support area 2.1)

Support for urban development is one aim of Priority axis 2 of the ROP NE – Development of Urban and Rural Areas. Support areas 2.1 – Development of Regional Centres and 2.2 – Development of Cities are designated for cities. The objective of 2.1 is to enhance the role of towns/cities as poles of regional growth and development. It is designated for cities with over 50,000 inhabitants. Such cities are obliged to prepare Integrated Urban Development Plans as a precondition for using funds within this support area. Funding provided through this integrated approach under 2.1 can be also used for investment in the regeneration and revitalization of urban brownfields. Only brownfields owned by public entities are entitled to receive assistance in Support area 2.1.

Support area 2.1 is also focused on the development of infrastructures in education, further education, recreation, healthcare and social affairs and applies to investments fostering increased population safety and property protection and investment projects aimed at improving the connection of industrial areas and smaller industrial localities to existing transport and technical infrastructures.

At present, 4 IUDP are registered with the Office of the NUTS II NE Regional Council. These are:

- ▶ City of Liberec Lidové sady Park;
- ▶ City of Hradec Králové City Centre = Growth and Development Pole;
- ▶ City of Pardubice Attractive City;

¹ For example, the Moravia-Silesia JESSICA Holding Fund was established with a clearly defined opening contribution in an amount equivalent to EUR 20 million from Support area 2.3 ROP Moravia-Silesia.

- ▶ City of Liberec “Attractive and Quality Life in Liberec”.

The 3 approved IUDP have been allocated the following amounts from SF:

- ▶ Pardubice IUDP “Attractive City” – CZK 387,280,216;
- ▶ Hradec Králové IUDP “City Centre = Growth and Development Pole” – CZK 467,964,973;
- ▶ Liberec IUDP “Lidové sady Park” – CZK 643,025,000.

The Liberec IUDP “Attractive and Quality Life in Liberec” is currently with the RCB NE; its budget of total eligible expenses is CZK 635 million, of which the required subsidy within the ROP from SF is CZK 540 million.

3.4.1. Brief description of registered IUDP

- ▶ The City of Hradec Králové IUDP “City Centre = Growth and Development Pole”:

This is a zone-based IUDP in central Hradec Králové. Four projects are currently being implemented (Ramparts – reconstruction, U Špuláků House, The Scout House of the K. Šimek Centre – mini-school, Preparation and management of the IUDP City Centre = Growth and Development Pole). According to the current status, the funding requirement of the approved sub-projects represents 11% of the total IUDP allocation. However, the city is intensively preparing further sub-projects, such as Revitalization of the Vertex Factory Facility as a Lifelong Learning Centre, Reconstruction of 28. října Square and S. K. Neumann Street, Reconstruction of Velké náměstí, Regeneration of Dukelská Street, Reconstruction of the Pod Kanovnickými domy Terraces, Reconstruction of the White Tower – The White Tower is White Again, Reconstruction of the Right Bank of the River Labe, Pedestrian and Bicycle Bridges Spanning the River Orlice Near the Winter Stadium, Reconstruction of the Bavlna Sports Facility, The Philharmonic Hall, and Overhaul of Šimek Park.

- ▶ The City of Pardubice IUDP “Attractive City”

The city of Pardubice has produced the zone-based integrated urban development plan “Attractive City”. Implemented sub-projects include Dašická Sports Facility, Modernization of the T.J. Sokol Sports Facility Pardubice, the Vinice Boy Scout Centre in Pardubice, the Integration Centre of Social Activities in Pardubice and Modernization of the Pardubice Swimming Centre. These projects represent 74% of the approved SF allocation. A total of eight projects for the City of Pardubice, the Pardubice Region and some non-profit organizations is scheduled to be implemented in the coming years. Another important group of projects included in the IUDP is represented by sub-projects for which funding applications have been submitted under the OP Research and Development for Innovation. The University of Pardubice is the principal promoter of these projects.

- ▶ The City of Liberec IUDP “Lidové sady Park”

The “Lidové sady” IUDP is zone-based. The city of Liberec has acquired grants for two Lesní Primary School projects (“School for Europe” and a landscaping grant). The third registered and approved project addresses IUDP administrative arrangements. These projects represent 7% of the approved allocation for this IUDP.

At present, the city of Liberec has submitted the Liberec IUDP “Attractive and Quality Life in Liberec” with total eligible ROP NE expenses of CZK 635 million, of which the ROP NE subsidy from structural funds is CZK 540 million. This IUDP includes the following ROP NE sub-projects: Liberec – Růžodol Multipurpose Recreation Centre, Streetcar System History Centre, Modernisation of the F. X. Šalda Theatre, Lily Pavilion of the Liberec Botanical Gardens, Vesec Recreation and Sports Complex, Expansion of Liberec City Hall Building Use, Revitalisation of the Multipurpose Playgrounds at the Šverma and Aloisín Heights Elementary Schools, Recreation and Sports Trail Network in the Ruprechtice – U Kapličky Recreation Area, Geothermal Energy Use Support Centre, Zvolenská Multipurpose Rail, Construction of a Multipurpose Hall in the Municipal Stadium Complex in Liberec, Overhaul of the Harcov Sports Grounds, Redevelopment of the Single-Use Sports Grounds in the Municipal Stadium Complex in Liberec, Leisure Time Areas Liberec – Improvement, Nature Centre, Preparation and Administration of City of Liberec IUDP Implementation Management – Attractive and Quality Life in Liberec.

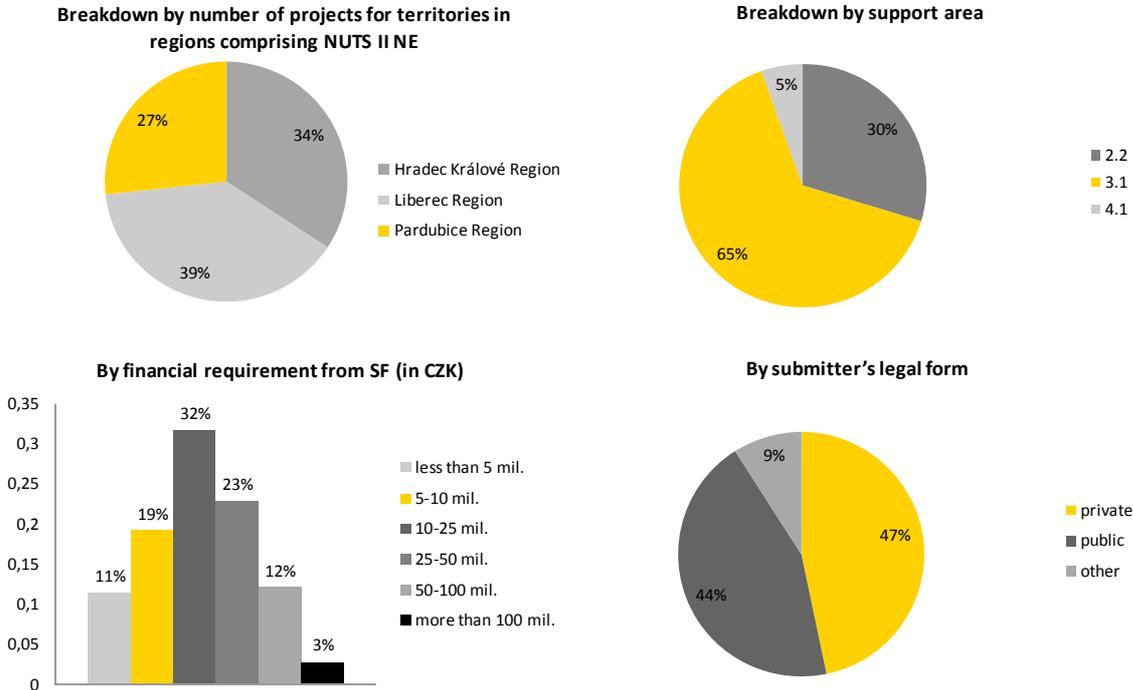
As mentioned in Section 3.3, sustainable urban development is indirectly supported within the ROP NE by projects carried out in support areas other than those that are explicitly targeted at urban development.

Functional overlaps with the theme of sustainable urban development may be identified in Priority axis 1 (Development of Transport Infrastructure), Priority axis 3 (Tourism) and Priority axis 4 (Development of the Business Environment)

3.5. Analysis of projects submitted in three selected support areas (OP 2.2, 3.1 and 4.1)

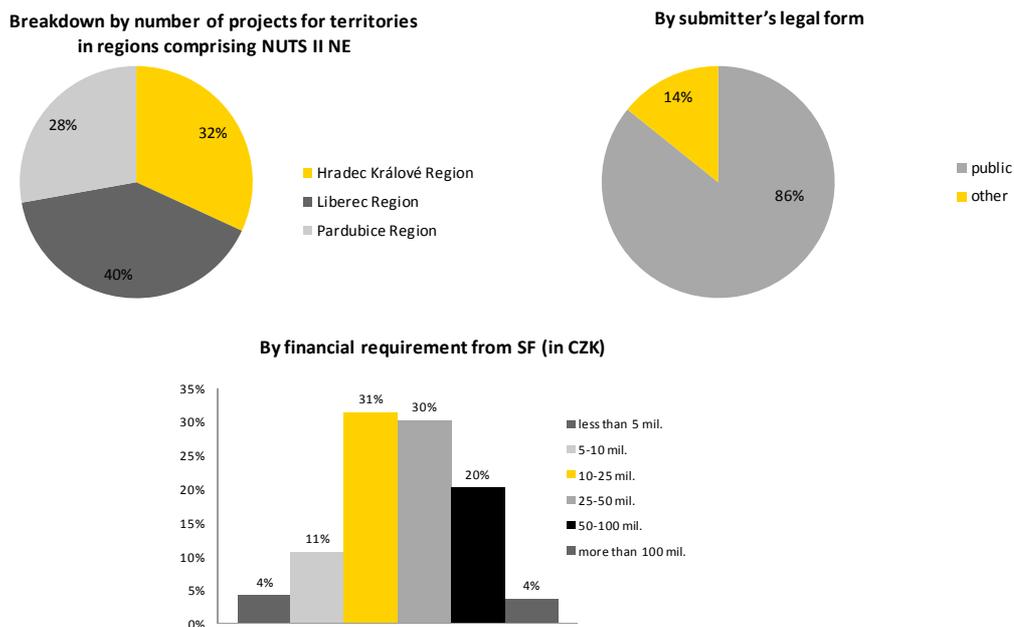
Based on an initial analysis of support area content within the ROP NE, it would be best for the purpose of analysing the use of the JESSICA financial instrument in the region to look at selected projects submitted in Support areas 2.2, 3.1 and 4.1. A total of 569 projects was submitted in these support areas, representing an aggregate financial requirement of CZK 15.53 billion. Of these registered projects, 128 were successful; the approved requirement amounts to CZK 3.86 billion. Another 234 projects with required total SF funding amounting to CZK 5.16 billion are currently being assessed.

Graph No.1: Profile of registered projects in OP 2.2, 3.1 and 4.1



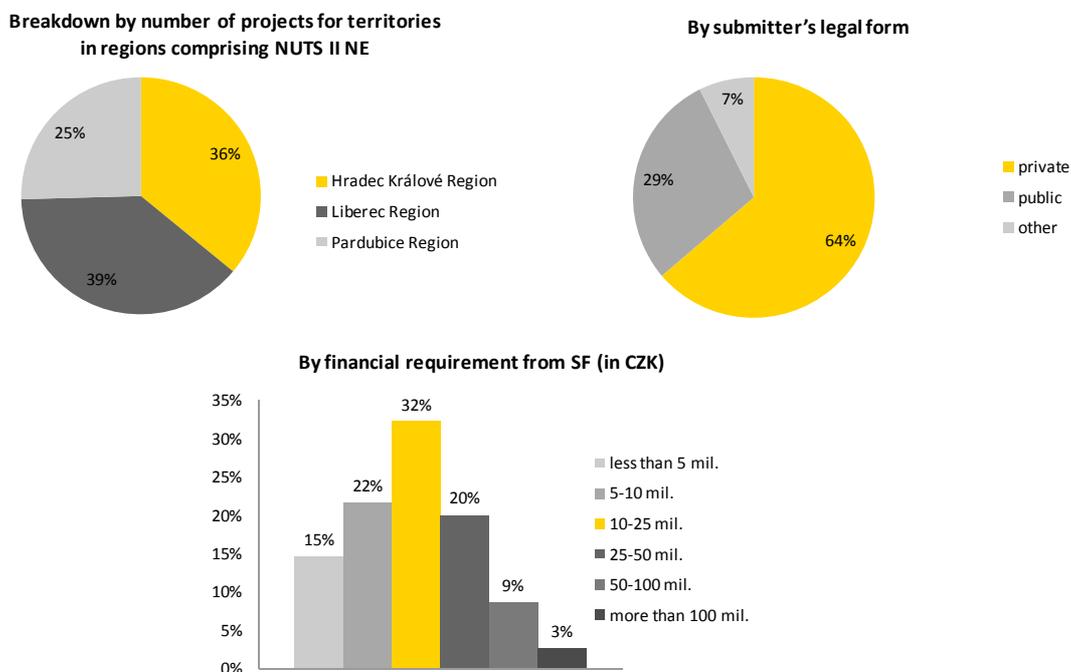
A total of 169 projects has been registered under Priority axis 2.2 targeting urban development (towns/cities with 5,000 to 50,000 inhabitants). Of these, 65 projects received approval. The registered projects' funding requirement from SF amounted to CZK 6.02 billion, of which the requirement for successful approved projects is CZK 2.24 billion. Most projects are focused on the revitalization of public spaces, sports, cultural and social centres, swimming pools and recreational facilities. Other project themes include improving social and medical services quality (modern technology, quality healthcare, overhaul and procurement of tools and technologies, group housing, a work rehabilitation centre for the mentally ill and people with disabilities, a barrier-free hospital, etc.)

Graph No. 2: Profile of registered projects in OP 2.2



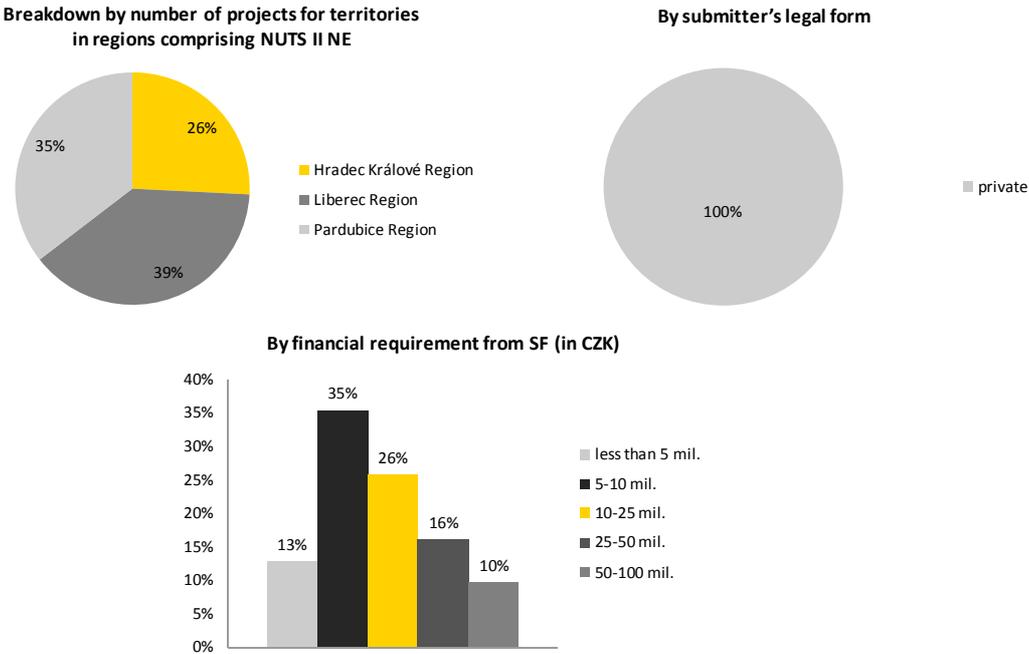
A total of 369 projects was registered in Priority axis 3.1 focusing on the development of basic tourism infrastructure and ancillary activities. (Forty six of these projects had been approved by February 2010.) Another 234 projects are under evaluation; the final assessments were not known at the time of this report. Registered projects represent a funding requirement from SF of CZK 8.85 billion; the approved requirement (for successful projects) was CZK 1.25 billion. The projects primarily address the modernization and expansion of accommodation and catering capacities (hotels, boarding houses, conference centres, museums, recreation centres, creation of cycle paths, etc.) Registered projects focus, inter alia, on spa promotion and development (including a “thermal paradise”, a spa hotel and a regeneration and relaxation centre).

Graph No. 3: Profile of registered projects in OP 3.1



A total of 31 projects, 17 of which have been approved, was registered in Priority axis 4.1 targeting the promotion and development of business infrastructure. The funding requirement relating to registered projects amounted to CZK 659 million; of this, successful project funding of CZK 371 million was approved. This priority axis has limits based on certain specifications defined in the funding use conditions in this support area. These relate to the addressing of overlaps with projects submitted in the Operational Programme Business and Innovation and the Rural Development Programme. The relevant services should focus on services provided to the public and the expansion of civic amenities. Projects submitted in this support area target the revitalization and use of brownfields, such as a retirement home, improvement of the infrastructure quality of medical services, a training centre, and an in-patient and social centre for the elderly.

Graph No. 4: Profile of registered projects in OP 4.1



3.6. Integrated plans, strategic and conceptual documents at local (urban) and regional levels in relation to the use of JESSICA

One requirement for the application of financial engineering instruments (see Council Regulation 1083/2006, Section 4, Article 44) is the support of projects “included in integrated sustainable urban development plans”. The concept of an integrated approach to urban development and sustainable urban development has been established in many international, European and Czech Republic documents (e.g. the Leipzig Charter, EC Regulation 1080/2006, Art. 8). Nonetheless, no precise definition of the term “integrated sustainable urban development plan” yet exists; thus, no clear stipulations exist concerning the requirements for applying financial engineering instruments in the ROP area.

The Integrated Urban Development Plan drafted pursuant to a Ministry for Local Development Methodological Directive and approved by the Czech Government (13 August 2007, No. 883) may be identified as the simplest concept. This document stipulates the main principles for preparing, evaluating and approving an Integrated Urban Development Plan. It was drafted in connection with the use of resources from EU funds (supporting the urban axis) and issued for the purpose of standardising the approach to preparing, evaluating, approving and implementing an Integrated Urban Development Plan (IUDP). An IUDP drafted pursuant to this methodology constitutes the basic coordinating framework for the overall vision and strategy of urban development for the purpose of identifying and resolving urban development issues in connection with the use of support from structural funds in the programme period 2007-2013. The Integrated Urban Development Plan is understood as a set of sequential, interconnected activities realised within a defined territory or the framework of a thematic approach in cities and designed to attain a joint objective or objectives of a city, municipality or locality. Support may come from one or more operational programmes. From the funding perspective, the IUDP’s main goal is to endeavour to

achieve the most effective possible use of public resources. This means the use of public resources in a manner that, by utilising the “leverage effect”, attracts private sector investment.

The methodology defines 2 basic types of IUDP:

- ▶ IUDPs to address issues in zones characterised as:
 - ▶ territories for intervention in the area of housing within intervention area 5.2 of the IOP [Commission Regulation (EC) No. 1828/2006, Article 47];
 - ▶ deprived territories;
 - ▶ territories with high growth potential.
- ▶ IUDPs to address a thematic issue [IUDP priority areas in accordance with Operational Programmes and with the Communication from the Commission to the Council and the European Parliament of 13 July 2006 SEC (2006) 928 are: Attractive Cities, Environment, Accessibility and Mobility, Economic Development, Social Integration, Administration of Public Affairs].

The use of resources is contingent on IUDP compliance with the foregoing methodology:

- ▶ Within the ROP – this obligation only pertains to cities with a population exceeding 50,000 inhabitants (see the ROP documents for more detail). According to these government directives, IUDPs in the NUTS II NE region are drafted, submitted and implemented for the cities of Hradec Králové, Pardubice and Liberec in compliance with the conditions for the use of subsidies from Support area 2.1 of the ROP NE. The IUDP shall include a list of sub-projects whose funding is expected to come from the ROP NE allocation for the given IUDP and, where applicable, shall also include projects submitted for thematic operational programmes that lack funding allocation.
- ▶ Within the Integrated Operational Programme (IOP), the IUDP as an obligatory form of use is stipulated in Support area 5.2 focusing on improving the environment at problem housing estates. Sub-projects are focused on revitalising housing estates and regenerating apartment houses. The obligation to submit an IUDP applies for cities with more than 20,000 inhabitants. Within NUTS II NE, the following cities have drafted and submitted IUDPs to the IOP: Hradec Králové, Chrudim, Jablonec nad Nisou, Liberec, Náchod and Pardubice. This study does not look further at these due to the work’s focus on options for implementing the JESSICA instrument within the ROP NE. The orientation of sub-projects points, inter alia, to limited possibilities for applying JESSICA use requirements.
- ▶ Other cities (< 50,000 inhabitants) were not obliged to submit IUDPs within the framework of ROP NE financial resource use.

Projects designed to strengthen urban development may also be submitted separately as what are known as individual projects within the ROP NE, in particular in Support area 2.2 Urban Development. These individual projects shall comply with the basic urban development principles framed in strategic, integrated or development plans (Note: this terminology is not found in the legislation, but has been coined by experts). Strategic plans declare basic approaches to sustainable development while balancing the economic, social and environmental pillars of sustainable development. Some concepts have been subject to SEA (Strategic Environmental Assessment), i.e. an assessment of the concept’s environmental and public health impacts. Cities execute their strategic plans/concepts via specific projects. If a strategic plan contains and ensures sustainable development principles, it is logical that individual sub-projects will also comply with this concept. In such a situation, there is potential for these projects to be supported by JESSICA and fulfil the requirement set down by the EC Regulation. However, by virtue of their structure these urban development concepts are not and cannot be in compliance with the methodology stipulated in the above cited government resolution as this resolution is purpose-tied to “mandatory” IUDPs.

Some cities have drafted “non-mandatory” IUDPs, which were prepared for a specific purpose and endeavour to comply with the government methodology. Nonetheless, their purpose prevents them from adhering to the methodology. A common characteristic of the IUDPs, however, remains their effort to achieve an integrated solution with a synergistic effect. One example is the IUDP of the City of Náchod for the period 2007-2013 entitled “Development of a Spa Town” or the Broumov Integrated Development Plan for the period 2007-2013 with the aim of setting up implementation for the use of structural funds in

the programme period 2007-2013. These “non-mandatory” IUDPs tie in with the comprehensive urban development strategy and endeavour to realise component parts or a specific theme thereof.

In their orientation and degree of detail for project identification focused on support for the urban dimension, the superior concepts, i.e. strategic and programme documents at the regional level, are more difficult to grasp. These regional development concepts are characterised, inter alia, by their own unique logic ensuing from the regional concept itself, from the broad spectrum of persons involved at the regional level and from the impossibility of setting up a financial framework for their performance. We may identify support for urban development and urban policies in all the documents, and the development plans drafted by individual cities comply with these regional concepts. At the NUTS NE regional level, these conceptual documents cannot logically be identified as sustainable urban development plans addressing the issue of urban development to a more concrete and detailed degree due, inter alia, to the competencies of the cities themselves that bear responsibility for their development.

The foregoing indicates that fulfilment of the requirements for applying the JESSICA financial instrument, i.e. support for those projects included in “integrated sustainable urban development plans”, can be assured not only via IUDPs drafted in compliance with the Local Development Ministry’s Methodological Directive (13 August 2007, No. 883) and the inclusion of the supported project in the list of sub-projects of such IUDPs, primarily because IUDPs thus prepared are purpose-tied documents (for more, see above) and their focus on coordinating the use of grant resources from a specific support area limits support for projects from the perspective of the type of recipient and target group (city size). The definition of an integrated sustainable urban development plan in the meaning of Article 44 of the General Regulation is also generally met by strategic urban development plans and, in some cases, by “non-mandatory” IUDPs that include basic approaches to sustainable urban development. This understanding of the term integrated sustainable urban development plan further provides, within the conditions of NUTS II NE, for financial engineering instruments to be applied outside the three main cities.

4. JESSICA project funding model

4.1. Project selection methodology to model JESSICA funding

A total of 625 projects submitted in Support areas 2.1 (IUDP), 2.2, 3.1 and 4.1 of the ROP NUTS II NE was analysed. Projects from Support area 2.1 (IUDP) were subject to individual selection (refer to Chapter 4.1.2). Criteria-based selection was applied for projects in Support areas 2.2, 3.1 and 4.1 (refer to Chapter 4.1.1). Other projects potentially suitable for JESSICA funding, but that had not solicited support from any of the above mentioned support areas, were also identified (refer to Chapter 4.1.3)².

The following steps were taken during the selection of projects suitable for model funding:

- ▶ Selection of projects from support areas 2.2, 3.1 and 4.1 pursuant to selection criteria (Chapter 4.1.1);
- ▶ Individual selection of projects from support area 2.1 (Chapter 4.1.2);
- ▶ Selection of projects focussing on urban space problems in the NUTS II NE region, which were described in Chapter 3.2.
- ▶ Additional selection of projects according to preferences of regional representatives beyond the scope of the three preceding steps (Chapter 4.1.3)³.

4.1.1. Criteria-based project selection

Projects were examined based on the following criteria to determine whether they should be included in the selected projects suitable to model JESSICA funding: financial return, minimum subsidy funding requirement, municipality population at the project implementation site (in connection with municipal strategic plans) and thematic focus of the project. Groups of projects that were submitted in Support areas 2.2, 3.1 and 4.1 of the ROP NE were included in the criteria-based selection. In total, 569 projects were analysed.

Financial return of the project

A primary condition for full-fledged use of the JESSICA financial instrument is that the project, or its selected part, shows a financial return. As many of the projects to be selected as potentially suitable for JESSICA funding solicited grant funding from the RC NE, their financial return was in many cases stated to be low. Projects analysed in this phase were not conceived by their submitters as projects with a financial return, but rather as projects generating either zero income or only enough income to cover all or part of operating expenses.

The selected projects were therefore broken down into the following two groups:

- ▶ project does not generate revenue (Variant 1)
- ▶ project generates enough revenue to cover operating expenses, but has no operating profit (Variant 2)

The following table indicates the breakdown of projects according to support area (the yellow field represents selected projects).

² The selection of projects for model funding does not represent an absorption analysis of the region and is not intended to represent an exhaustive demand analysis for the JESSICA instrument in the NUTS II NE region.

³ Additional project selection was based on the conclusions of discussions that followed the presentation of the model use of JESSICA in the NUTS II NE region on 14 June 2010 in the Pardubice Regional Authority building (for more, refer to Chapter 2.2.3. Communication with key persons).

Table No. 5

Projects	Variant 1	Variant 2
OP 2.2	127	42
OP 3.1	100	269
OP 4.1	0	31

Of a total of 569 analysed projects, 227 were relegated to the “non-revenue-generating project – Variant 1” category. The remaining 342 projects were placed in the “project generates revenue to cover operating expenses” category. Projects included in the “Variant 2” category were subject to further examination⁴.

Minimum subsidy funding requirement

For the criteria-based selection of submitted projects, only those projects with a subsidy request exceeding CZK 50 million were selected. We assume that projects to be funded via the Urban Development Fund will be both unique to their region and costly. A lesser number of financially demanding projects will be preferred for the purpose of effective Fund management and low administrative overhead.

Of a total of 342 projects, 52 met the condition of a subsidy funding requirement not less than CZK 50 million.⁵

The following table shows the breakdown of projects for further review (yellow field).

Table No. 6

Projects	Financial limit (CZK 50 mil.)	Variant 1	Variant 2
OP 2.2	>	25	15
	<	102	27
OP 3.1	>	8	34
	<	92	245
OP 4.1	>	0	3
	<	0	28

⁴ Projects directed toward regional development are often conceived with a low financial return because to date, subsidies are the only type of public funding (including from the ROP NE) available for these projects, and the presence of income in the project could result in a subsidy reduction. We may expect that the availability of a financial instrument enabling support for urban development projects in the form of repayable funding compels submitters of certain types of projects to include in them elements that generate income enabling gradual repayment of investment expenses. Nevertheless, a detailed analysis of the possibilities of revising already submitted projects exceeds the scope of this study.

⁵ The 50-million threshold represents a subsidy request, which we consider effective, from the point of administrative costs, for funding via the Urban Development Fund (UDF).

Number of inhabitants at the project implementation site

A further requirement for application of the JESSICA financial instrument is support of projects “included in integrated sustainable urban development plans”. In NUTS II NE, only the cities of Liberec, Hradec Králové and Pardubice have drafted and submitted IUDPs pursuant to the Local Development Ministry’s Methodological Directive. Among the other documents taken into consideration are strategic urban development plans and integrated urban development plans (for more on this issue, refer to Chapter 3.5). We assume that municipalities with more than 5 thousand inhabitants could have drafted a document that serves as an alternative to the IUDP. The 5-thousand-inhabitants criterion was selected, in part, in connection with Priority axis 2 Development of urban and rural areas of ROP NUTS II NE, where this criterion separates support area 2.2 Urban development from support area 2.3 Rural development⁶. In all, 42 of the 52 identified projects should be implemented in municipalities with more than 5 thousand inhabitants (Note: all projects submitted in Support area 2.2 are conceived to support urban development in cities with 5,000-50,000 inhabitants). The table shows the breakdown of projects by number of inhabitants. In all, 29 projects were selected for further review (yellow field).

Table No. 7

Projects	Financial limit (CZK 50 mil.)	Number of inhabitants (5. thous)	Variant 2
OP 2.2	>	>	15
OP 3.1	>	>	13
		<	21
OP 4.1	>	>	1
		<	2

Thematic orientation of the project

As a final criterion, we applied the favourable impact of a project on urban development at the project implementation site. Projects were broken down by thematic areas whose designations were created for the analytical purposes of this report. The following areas were thus selected as suitable for a model application of JESSICA funding:

- ▶ Infrastructure for sport;
- ▶ Infrastructure for culture;
- ▶ Infrastructure for education.

These thematic areas were selected on the basis of performed field (i.e. implementation site) reviews and applicant interest in support from the ROP NUTS II NE. A total of 14 projects were selected through the application of these criteria. Projects excluded based on thematic orientation came most often under the

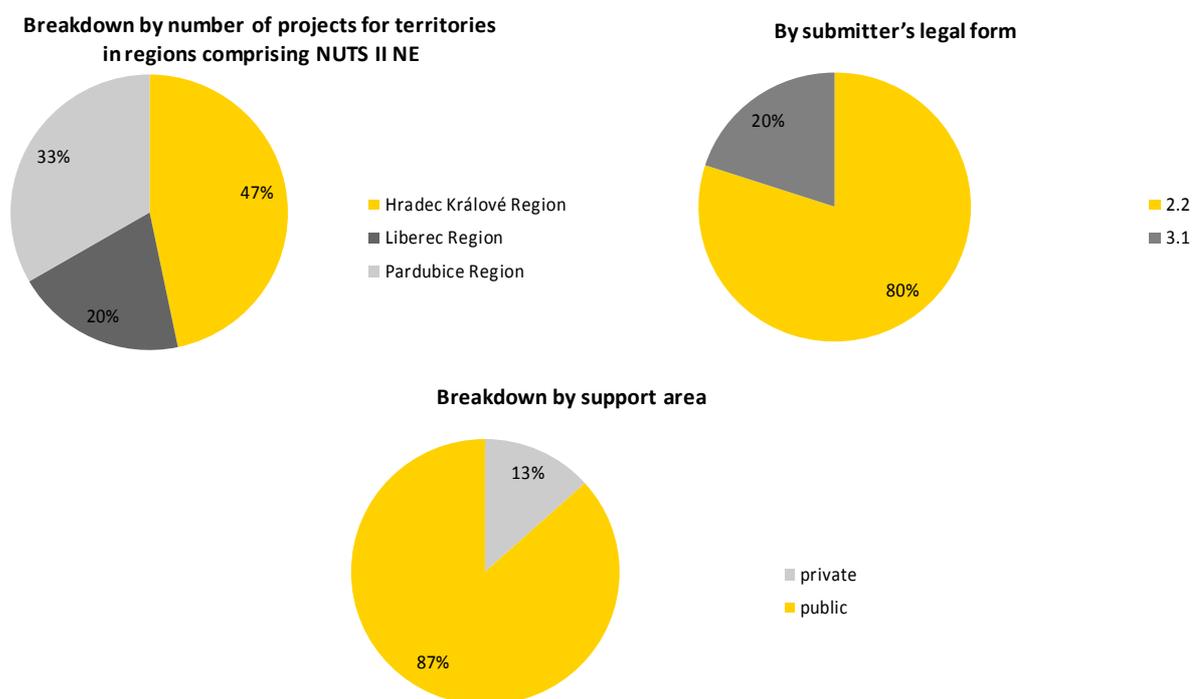
⁶ For this particular analysis, the “Number of inhabitants at project execution location” criterion is of more use than, e.g., a definition of the functional/catchment area, which would exceed the scope of this study. Determining catchment area size is a complex procedure (functional size of the area from a comprehensive perspective, economic ties, etc.), which for practical reasons cannot be recommended as a project evaluation criterion at this stage (e.g. relevance of data, measurement difficulties and differing expert procedures for defining a catchment area).

thematic rubric of tourism infrastructure (redevelopment and remodelling of hotels, hostels and pensions)⁷.

The following is a list of 14 selected projects that meet these criteria:

- ▶ Project was submitted in Support area 2.2, 3.1 or 4.1;
- ▶ Project generates revenue covering operating expenses; project generates no operating profit;
- ▶ Structural fund contribution request exceeds CZK 50 million;
- ▶ The municipality in which the project is to be implemented has more than 5 thousand inhabitants;
- ▶ The project's thematic orientation favourably impacts urban development.

Graph No. 5: Profile of identified projects



⁷ This analytical narrowing does not mean that project types other than infrastructure for sport, culture and education might not have a favourable impact on the development of a given city, too. This only entails a model narrowing for the purposes of this study.

The list of selected projects was anonymised. Projects are categorised according to the subsidy funding request from structural funds.⁸

Table No. 8

Project	Submitter	Request from SF in CZK million	Region	Support area
Community Centre	Municipality	176	Hradec Králové	2.2
Sports Centre	Municipality	130	Hradec Králové	2.2
Relaxation Centre	Joint-stock company	128	Liberec	3.1
Outdoor Pool Reconstruction	Municipality	119	Hradec Králové	2.2
Rehabilitation Centre	Municipality	86	Hradec Králové	2.2
Outdoor Pool Reconstruction	Municipality	79	Liberec	2.2
Regeneration Centre	Municipality	73	Hradec Králové	2.2
Community Pool	Municipality	69	Hradec Králové	2.2
Multiuse Hall	Municipality	64	Liberec	2.2
Swimming Pool	Municipality	59	Pardubice	2.2
Multiuse Centre	Municipality	58	Pardubice	2.2
Education Centre	Municipality	55	Pardubice	2.2
Municipal Building Reconstruction	Municipality	55	Pardubice	3.1
Sports Complex	Municipality	53	Pardubice	2.2

The “Outdoor Swimming Pool Reconstruction” project (Hradec Králové region) is described for modelling purposes in Chapter 4.2.2 from the perspective of possible JESSICA funding.

4.1.2. Individual project selection

This selection included projects that were submitted in specific Support area 2.1 (IUDP), where individual projects were subjected to individualised analysis. The characteristics of these projects are described in Sub-Chapter 3.3.1. Of a total of 56 analysed projects, only one was selected as suitable to model JESSICA funding (the sole criterion was the generation of income in an amount enabling at least partial repayment of investment expenses). However, the submitter did not provide project documentation for the selected project; therefore, no projects from Support area 2.1 are included for modelling purposes in this report.

⁸ A complete list of anonymised projects forms a non-public annex of this report.

4.1.3. Other potentially suitable projects

EY further analysed problems of urban space in the NUTS II region. During meetings with representatives of regional institutions, regional leaders defined those areas of urban development that strike them as most problematic, i.e. the development of healthcare infrastructure, the development of social infrastructure, the revitalization of urban brownfields for tourism (and the spa industry), the revitalization of dilapidated and unused historical buildings within city limits and the development of urban transport infrastructure. With respect to these areas, projects were also identified that had not been submitted to any calls for submissions within the Regional Operational Programme (ROP NUTS II NE) or any other operational programmes. Thus, they are projects with a low rate of investment return that are not of sufficient interest to the business sector. They are, moreover, projects that for the most part exceed the financial possibilities of municipalities. The "Spa Complex" project was selected from this group of projects to be used as a model for JESSICA use.

In the course of preparing the project, and in connection with the preferences of participants in the EY presentation at the Pardubice Regional Authority building on 14 June 2010, another healthcare infrastructure development project was selected. The project was submitted for support area 2.2 ROP, and was then approved and is now being successfully implemented.

4.2. JESSICA funding model

Based on the foregoing methodology, the following three projects were selected. In this chapter, a funding model, including funding using the JESSICA instrument, specifically in the form of an Urban Development Fund loan, has been elaborated for them. Funding by means of an Urban Development Fund loan has been elaborated in this study in two cases for projects selected from the set of projects submitted from subsidy applications and, in one case, for a project identified by EY separately from the set of subsidy-seeking projects.

Table No. 9

Project name	IUDP	Support area	Region	Funding requirement from SF (CZK)
Spa Complex	yes (non-mandatory)	-	Hradec Králové	-
Outdoor Pool	no	2.2	Hradec Králové	119.4 mil.
Healthcare Equipment	no	2.2	Liberec	39.5 mil.

Key modelling assumptions

- ▶ Only standard loan financing is considered (not equity, guarantees or, e.g., subordinated debt).
- ▶ The JESSICA interest rate is always 2.03%, which is more attractive than commercial interest rates^{9,10}

⁹ This value corresponds to the current basic reference rate for the Czech Republic pursuant to the Communication from the Commission on the Current Interest Rate for Repayable Government Support and on the Reference and Discount Rate for the 27 Member States to be used from 1 July 2010 (2010/C 166/05). To this basic reference rate must be added the minimum risk margin calculated in compliance with the Communication from the Commission on the Revision of the Method for Setting the Reference and Discount Rates (2008/C 14/02) based on the extent of the loan security and risk profile of the loan recipient. This procedure yields the resultant reference rate. The interest rate in the amount of the reference rate does not represent any form of advantage; thus, the indicators of public support are not met. For the needs of the model

- ▶ The JESSICA interest rate is fixed for the entire loan repayment period.
- ▶ Inflation is set at 2% for the entire JESSICA repayment period. Inflation is set according to the Czech National Bank inflation target valid from January 2010 until the Czech Republic's eurozone accession.
- ▶ All values were adjusted to 2010 prices (producer price index) and are valid at 1 July 2010.
- ▶ Investment expenses are stated inclusive of VAT. Direct taxes are reflected in the model.
- ▶ Capital structure is only designed to serve as an example. The share of individual capital components will be unique to each project and will reflect multiple factors, primarily project type and financial standing of the applicant. At the same time, UDF-funded projects may have a higher degree of risk, which in turn could affect capital structure (subsidy amount, ratio of equity to debt).

Limitation of the modelling scope

The scope of this project did not provide for a verification of the accuracy and credibility of data and information submitted in the studies of the projects' economic assessments. This assumption primarily pertains to data on revenues and expenses of projects and other outputs, e.g. the number of newly created jobs. The data could, of course, be converted or otherwise adjusted based on the evaluator's own analyses, experience and knowledge.

The financial analysis was performed for a model provided for this purpose by the European Investment Bank (EIB).

4.2.1. Spa Complex

This project was selected based on the individual assessment of projects suitable for JESSICA funding owing to the significant socio-economic impacts to be gained if they are implemented. The municipality in whose proximity the new spa complex is to be constructed is among the prominent spa towns that came into their own at the turn of the 19th and 20th centuries. After 1990, the spa complex was restituted to its original owners, who discontinued spa operation in the early 1990s. The original spa complex has been damaged by past flooding and now lay in a state of extreme disrepair. The spa, though non-functioning, maintains the status of a certified spa location in the Czech Republic.

In 2007, the municipality had a feasibility study prepared for the spa's redevelopment and return to operation. As a suitable alternative for the renewal of the city's spa culture, the study proposed the construction of a new spa complex away from the flooded area with access to the mineral water wells. Thus, the project is for a new greenfield spa complex. A hydrogeological survey was performed of accessible wells in the identified area, and the water sources were found to suffice for the operation of a spa and to meet the requirements of therapeutic standards. The municipality owns some of the land in the area planned for the complex's construction and has contracts in place for the purchase of additional lands in the event of project implementation¹¹. It is an extensive project that exceeds the municipality's

funding, the reference interest rate was used without the minimum risk margin, despite the fact that some cases may involve a form of public support.

¹⁰ This value of the interest rate is only a model narrowing. The interest rates of projects funded via JESSICA in the NUTS NE region will vary from case to case. Determination of an appropriate interest rate belongs to the key tasks of the management of the Urban Development Fund. The interest rate should reflect the local specifics and the loan affordability. At the same time, the interest rate should not be so low as to involve a disproportionate amount of state aid.

¹¹ It should be mentioned here that in the event of JESSICA project funding, it would in principle be possible to avoid the need to amalgamate the lands by establishing an association of legal entities into which the city and other owners would contribute the respective lands. The project would then have the character of a PPP, where a part of investment expenses could be covered by funding from the Urban Development Fund. This analysis, based on the existing feasibility study, nevertheless assumes the provision of land by the municipality for no consideration.

financial limitations. The spa investor and operator is expected to be a private entity. The municipality is willing to provide the investor with the land needed for the complex's construction. According to the feasibility study, the spa complex will offer 400 beds and modern spa and wellness services. Construction is expected to take 3 years.

The development of spa and wellness services has a high degree of economic potential in light of increasing living standards in the Czech Republic and neighbouring countries. Another important factor impacting demand for these services is the change in the demographic structure of the Czech Republic and neighbouring countries (the aging population).

The objectives of this project include:

- ▶ Renewed operation of the spa with the status of a certified spa location;
- ▶ Construction of a modern spa complex meeting European standards;
- ▶ Provision of new capacities for the treatment of diseases of civilization (e.g. circulatory system disorders) in the Czech Republic;
- ▶ Increased access to medical, social, spa and relaxation services for inhabitants of the municipality and the entire region. Some 20,000 people live in the municipality; the region's catchment area has 50,000-80,000 inhabitants;
- ▶ Bolster the region's tourism potential;
- ▶ Enhance cultural and social life;
- ▶ Create new qualified jobs – the project has the potential to create 140 new jobs (including specialised medical personnel). According to the number of employees, the spa complex would be among the 15 largest employers in the municipality. There is added potential for the creation of more jobs in related services;
- ▶ Bolster the regional economy and support new business.

The municipality has drafted an Integrated Urban Development Plan. It is a "non-mandatory" IUDP, where spa renewal counts among the urban development priorities. The drafted IUDP is tied to the following development-related documents: Strategic General Principles of the Communities, National Development Plan 2007-2013, National Strategic Preference Framework 2000-2013, ROP NUTS II NE 2007-2013, Hradec Králové Regional Development Strategy 2007-2015, Strategic Regional Development Plan and Municipal Zoning Plan for the Period until 2010. The topic of the spa industry is examined in detail in the last two of these documents. Spa industry revitalisation counts among the Strategic Regional Development Plan priorities and is included in the zoning plan.

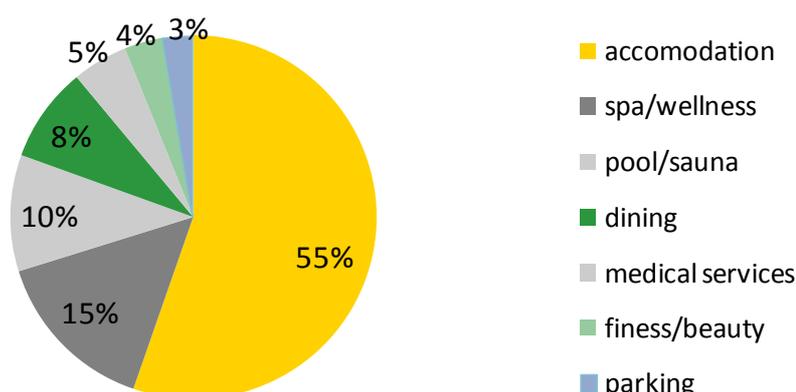
This is a project with significant positive socio-economic impacts on the entire region. There are some risks related to the project as lower facility occupancy and lower financial rating of spa clients.

The spa complex will provide three basic types of therapeutic care – preventive care, chronic care and follow-up rehabilitative care. In all, the spa complex will offer some 400 beds in 200 rooms and will provide accommodation of various categories, including barrier-free rooms.

The spa complex may be divided into its following components: accommodation, spa and wellness facilities, pool and sauna, dining, medical services, fitness and beauty, a parking.

Graph No. 6

Structure of investment expenses



Economic assumptions of the model

- ▶ Investment expenses – CZK 1.3 billion¹²

Investment expenses comprise budgeted building costs and total technological equipment costs. They further include technical documentation, construction management and resident inspector costs.

- ▶ Operating expenses – CZK 147 million/year
- ▶ Turnover – CZK 201 million/year

Operating expenses and turnover have been quantified based on 65% capacity use of all spa complex services¹³. For the sake of simplification, average service prices were quantified, i.e. no price differentiation was performed (e.g. distinguishing between prices of accommodation or varying spa service prices for self-payers and health insurers).

Model capital structure

Table No. 10

	in mil. CZK	Share in %
Equity ¹⁴	129	10
UDF loan	713	55
Subsidy	454	35
Investment expenses total	1 298	100

¹² It is a „major project“ in the sense of Article 39, Council Regulation (EC) No. 1083/2006. In such a case, the member state or the managing authority shall provide information to the Commission as is stated in Article 40 of the same regulation. Such a large project requires adequate preparation and strong project management.

¹³ Spa utilization capacity is drawn from a feasibility study prepared for this project at an earlier time.

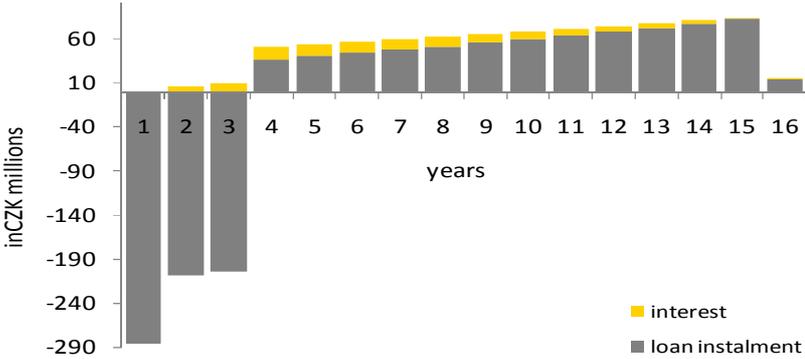
¹⁴ The share of equity generally reflects multiple factors, primarily project type, financial standing of the applicant and project risk rate. The bank employs an individualized approach for every project; in this case, the manner in which the bank reflects the subsidy portion of the funding is of key importance.

Financial results¹⁵

- ▶ The UDF loan is to be repaid over 16 years as of the project start date (the following graph shows cash flows from the perspective of the UDF; in the case of a JESSICA loan recipient, it is a mirror graph).
- ▶ IRR of the private investor 19.7%, investment recovery 11 years¹⁶.

Graph No. 7

Cash flows from the UDF perspective



4.2.2. Outdoor Pool

This project entails the reconstruction of an outdoor swimming pool that was built more than 70 years ago in a municipality with some 16 thousand inhabitants. The pool, located in the outer city centre, is easily accessed by public transit. The pool is in poor repair and fails to meet standard hygiene regulations. The pool’s technology is obsolete, and it lacks a filtration and cleaning system. The pool has been open for the last 6 summers, but only as a relaxation area – visitors bathed in the pool at their own risk. The municipality has no other (manmade or natural) outdoor swimming pools. Local residents are forced to go to neighbouring municipalities to visit outdoor pools or they relax at natural water sources in the municipality’s vicinity. The city’s residents have long criticised the lack of summertime recreational options. Thus the Municipal Council, in response to requests from the city’s residents, decided to renovate the existing historical outdoor pool, adding modern water filtration and heating technologies.

The project’s primary aim is thus to reconstruct an outdoor swimming facility that provides relaxation and leisure-time opportunities for local residents and visitors to the municipality, which will in turn enhance the quality of life and attractiveness of this historical catchment centre’s densely populated area (approx. 50 thousand inhabitants). The outdoor pool augments and expands the existing sporting opportunities of which citizens of all ages may take advantage. The building of new infrastructure will support the city’s economic development through related services necessary to the project. According to the project submitter, the outdoor pool’s renovation and re-opening will yield further favourable urban development (extending to the city’s immediate surroundings), causing residents not to leave the area for bigger cities. The project will also create 20 seasonal jobs.

The project complies with the ROP NE rules and was submitted in a call in Priority axis 2 Development of Urban and Rural Areas, Support area 2.2 Urban Development, operational goal Regeneration and

¹⁵ This is only one of the scenarios of the funding, based on the feasibility study, which was conducted previously.

¹⁶ Internal rate of return (IRR) corresponds to the financial results from a feasibility study prepared for this project at an earlier time.

Revitalisation of the Urban Environment. The project was approved by the Municipal Council and is in compliance with the city zoning plan¹⁷.

The ROP NE subsidy application, Study of the Economic Assessment of the Project “Outdoor Pool Reconstruction” and itemised construction were analysed for the purpose of modelling JESSICA use.

Total project spending was quantified at CZK 215 million, including VAT¹⁸. This amount included both eligible and ineligible project expenses. Eligible expenses amounting to CZK 164 million primarily comprise building and technology expenses. Swimming pool technology (water filtration and heating) is calculated at a price of CZK 55.4 million. Ineligible expenses of CZK 50.6 million represent expenses for ancillary activities – catering/dining facilities, boat rental, tennis and beach volleyball courts, access roads and VAT on eligible expenses.

Economic assumptions of the model

▶ Investment expenses – CZK 177 million

Investment expenses comprise existing facility demolition, excavation work, water filtration and heating technology, landscaping, technical documentation and resident inspector costs. Ineligible project expenses were not reflected in the calculation. Project implementation is expected to take 3 years.

▶ Operating expenses – CZK 1,694 thousand/year

The most significant item in operating expenses comprises personnel costs; this is followed by electricity costs, water and sewerage fees, costs of pool technology maintenance and other operating expenses.

▶ Turnover – CZK 4,801 thousand/year

Admission fees are the sole source of revenue in turnover. The turnover calculation is based on the demand for swimming pool services and an admission fee calculation. The admission fee was adjusted to be in line with fees charged by similar pools in the Czech Republic. Moreover, the newly calculated admission fee better reflects the high costs of reconstruction and the modern technology to be used. The amount of turnover is greatly affected by meteorological conditions. Thus this item is expected to be highly volatile, which could adversely impact the ability to meet JESSICA obligations.

Model capital structure

Table No. 11

	in mil. CZK	Share in %
Municipality contribution	17.7	10
UDF loans	26.5	15
Subsidy	132.8	75
Investment expenses total	177	100

¹⁷ The project was approved and is being realised as part of support area 2.2 Regional Operational Programme NUTS II NE. We may thus assume that the project met conditions with respect to the global and specific objectives of the ROP, including compliance with the principles of sustainable development.

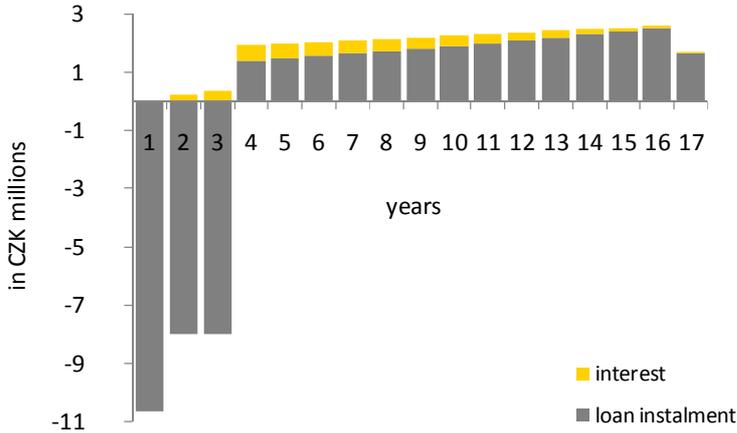
¹⁸ At 2007 prices.

Financial results

- ▶ The UDF loan is to be repaid over 17 years as of the project start date (the following graph shows cash flows from the perspective of the UDF; in the case of a JESSICA loan recipient, it is a mirror graph).
- ▶ IRR of the municipality’s contribution is 7.8%, investment recovery 19 years.

Graph No. 8

Cash flow from the UDF perspective



4.2.3. Healthcare Equipment

The aim of this project is to establish an MRI centre as part of a municipal hospital’s radiology department. The hospital has the status of an allowance organisation and its founder is the municipality. It is an urban hospital located in a municipality that is one of the 10 largest municipalities in the NUTS II NE region by population¹⁹.

The hospital has considered purchasing an MRI device in the past; therefore, its most recent renovation work included interior adjustments to accommodate a future MRI centre. Thus, the project calls for no major renovation work. The radiology department is equipped with the latest devices, including computer tomography (CT) equipment. There is an insufficient number of these facilities in the region. Patients must therefore travel some distance and are subject to appointment wait times of 1 to 3 months.

Of all imaging technologies, magnetic resonance imaging affords the highest quality tissue contrast with the lowest level of ionising radiation. Compared to a CT scan, the contrast materials used in MRI elicit fewer adverse effects. This examination is therefore better, inter alia, for young women (of child-bearing age), oncology patients and children. For patients with the following serious illnesses, magnetic resonance imaging is irreplaceable owing to its fast and accurate diagnostic capabilities:

- ▶ Infectious illnesses of the brain, spinal cord and joints;
- ▶ Cerebral haemorrhage and stroke;
- ▶ Multiple sclerosis;

¹⁹ The project was approved and is being realised as part of support area 2.2 Regional Operational Programme NUTS II NE. We may thus assume that the project met conditions with respect to the global and specific objectives of the ROP, including compliance with the principles of sustainable development

- ▶ Malignant soft tissue tumours (liver, pancreas, kidneys, intestine, prostate, female reproductive organs);
- ▶ Heart attacks;
- ▶ Torn ligaments and menisci of the large joints;
- ▶ Spinal disc herniation.

The need for this device also arises from the Czech Radiology Society guideline stipulating an optimal ratio of 1 magnetic resonance imaging device to 250 thousand people. In the given region, this indicator is presently 430 thousand people to 1 magnetic resonance imaging device.

The purchase of the MRI device complies with the following documents: Action Plan for the City (Measure No. 4.2 Healthcare, specific aim 4.2.1, activity: “Acquire and Install MRI Diagnostic Equipment (1.5 – 2 Tesla)”, Strategic Plan for the City (specific aim: “Hospital Development Plan Implementation”), the ROP NUTS II NE Regional Development Programme and the National Development Plan.

Economic assumptions of the model

- ▶ The projected useful life of the MRI device is 10 years. Warranty service is provided for the first 6 years of the device’s use. The costs of extending the service warranty to 10 years are reflected in investment expenses.
- ▶ Total investment expenses – CZK 44.6 million
 - ▶ Technology investment expenses (incl. magnet, screening system, inductors, cooling, Faraday cage and software) – CZK 34.7 million
 - ▶ Renovation expenses – CZK 9.9 million
- ▶ Capacity of a similar site in the region is 5 thousand examinations per year.
- ▶ Average examination price is CZK 5,300 based on an assumption of CZK 0.95/point.
- ▶ Operating expenses – CZK 8.4 million/year; electricity and personnel costs are the key items (3.5 specialised healthcare personnel).
- ▶ Total revenues – CZK 26.7 million
 - ▶ The revenue calculation is based on income from performed outputs pursuant to Ministry of Health Regulation No. 134/1998 Coll., which issues a list of healthcare outputs with point values, as amended, and Regulation No. 471/2009 Coll. on the setting of point values.

Capital structure

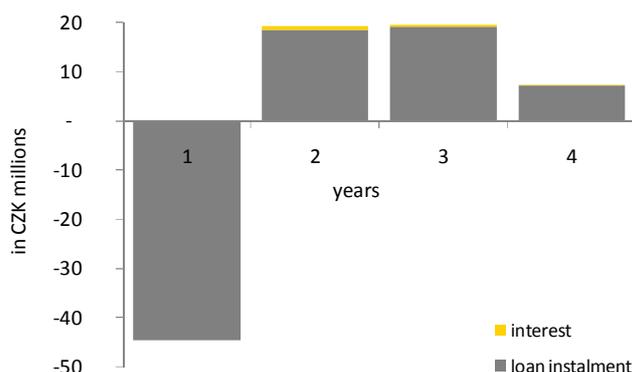
- ▶ UDF loan – CZK 44.6 million, i.e. 100%

Financial results

- ▶ The UDF loan is to be repaid over 4 years as of the project start date (the following graph shows cash flows from the perspective of the UDF; in the case of a JESSICA loan recipient, it is a mirror graph).

Graph No. 9

Cash flows from the UDF perspective



4.2.4. Modelling conclusions

Projects funded with JESSICA loans must generate operating profit; therefore, a very important role is played here, inter alia, by the quality of a business plan that shows market potential within the context of sustainable urban development plans. However, it is not financial return, but general socio-economic benefit, that is the main priority of projects submitted to the mentioned ROP NE support areas; in many cases, this may significantly limit, or indeed obviate, the ability of projects to generate operating profit.

JESSICA is a unique financial engineering instrument and, as indicated by the foregoing analysis of model projects, we cannot anticipate its blanket use to fund projects from the ROP NE. Rather, it will be applied for specific, carefully selected and implemented projects generating both socio-economic benefits and a financial return. Projects may also be expected in many cases to fail to generate income during their life cycles in amounts sufficient to cover all investment costs. It will thus be necessary to co-fund a commensurate amount of investment costs through subsidies. Preferential lending alone is not at this moment sufficiently attractive.

In projects submitted together with applications for subsidies from the ROP and elsewhere, we may of course find additional cases of investment eligible for full JESSICA funding that would effectively support regional development in selected areas.

5. Proposed JESSICA implementation structure

The proposed implementation structure is based on field investigations and knowledge of the NUTS II NE region and takes into account implementation procedures in the Czech Republic and other EU countries as well as the valid legislation.

For all three variants, the Urban Development Fund (UDF) or Holding Fund (HF), respectively, exists as a standalone legal entity independent of its founder or as a separate financial unit within an existing financial institution. Article 43 of Commission Regulation (EC) 1828/2006 and Commission Regulation (EC) 846/2009 require this legal and accounting subjectivity. The Fund's internal organisation structure is derived from the legal form of the UDF/HF.

All three implementation variants assume the following financial structure:

- ▶ 85% of resources contributed to the UDF or HF, respectively, will be provided from the ERDF (the contribution is made to the fund by the RC NE, pre-funded via regular subsidies provided to the RC NE by the Ministry for Regional Development, subsequently certified by the Ministry of Finance and reimbursed by the European Commission in compliance with Article. 78[6] of Regulation 1083/2006);
- ▶ 7.5% of the contribution to the JESSICA Fund will be a state budget appropriation (the contribution is made to the fund by the RC NE; the state budget appropriation is provided to the RC NE by the Ministry for Regional Development);
- ▶ The RC NE 7.5% contribution to the JESSICA Fund will have to be secured from other public funding sources (e.g. contribution from regions or cities).

The financial structure of the Urban Development Fund can be enlarged by further financial resources, e.g. from private investors, banks and other financial institutions. Nevertheless, it may be assumed that these additional financial resources will represent co-funding of the projects themselves as opposed to direct investment in the Urban Development Fund. Also to be considered are in-kind contributions to the Fund, e.g. in the form of land and real estate (brownfields).

The methodology to identify projects suitable for JESSICA funding should comprise a part of the UDF business plan²⁰. The methodology should include search methods and project evaluation tools as well as rules for cooperating with regional bodies, a method for providing expert support and consultations provided by these bodies.

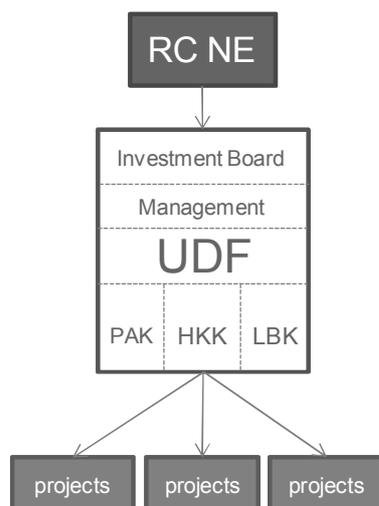
Projects suitable for JESSICA funding, i.e. the focus of the future UDF, should form a part of the UDF business plan. The portfolio of UDF projects should reflect the specifics of this funding instrument and the individual needs of the NUTS II NE region, e.g. the revitalization of brownfields or improvement of civic amenities. JESSICA represents a very narrowly identified funding instrument for urban development and the future portfolio of UDF-funded projects should reflect that fact. The shift from subsidy funding to JESSICA funding presupposes a change in how regional development projects are selected and supported. The approach differs entirely from that of ROP subsidy funding.

Pursuant to Commission Regulation (EC) No. 1828/2006, annual costs of running the Urban Development Fund shall not exceed an average value of 3% of capital contributed to the UDF. According to the same regulation, costs of running the Holding Fund (HF), if one is established, shall not exceed an average value of 2% of capital contributed to the HF.

²⁰ The business plan is defined in Article No. 43 of Commission Regulation No. 1828/2008. An evaluation of the submitted business plan should form a part of the tender procedure for management of the fund.

5.1. Implementation Variant I

This variant involves a single UDF at the NUTS II NE regional level. A description of the role of key implementation participants follows.



Regional Council of the Northeast Region

The Regional Council of the Northeast Region (RC NE) is responsible for managing and implementing the JESSICA instrument in the NUTS II NE region. The RC NE decides on the earmarking of a certain portion of financial resources from its current operational programme and the transfer of these resources for the purpose of JESSICA funding. It then establishes the UDF in which Fund management is appointed based on a tender procedure (pursuant to Act No. 137/2006 Coll. on public contracts). The Fund manager may be selected before or after UDF establishment, depending on the legal status of the UDF. The RC NE also defines the internal Fund rules for investing in selected projects based on approval by the Fund's Investment Council. The Fund rules shall comply with the valid legislation, in particular structural funds rules. The Regional Council shall establish the UDF as a standalone legal entity (for more, refer to Commission Regulation [EC] 1828/2006) or as a separate accounting unit within an existing financial institution. The UDF is established by the execution of a funding agreement in compliance with Article 43(3) of Commission Regulation 1828/2006.

Urban Development Fund (UDF)

The Fund is a standalone legal entity established by the Regional Council for the purpose of managing financial resources from the JESSICA instrument or a separate financial unit within an existing financial institution. Only one Fund has been established in the NUTS II NE region; it manages resources for all three of the regions comprising NUTS II NE. Investment resources are earmarked for each region. These resources are only divided in the accounting books, not in actuality.

The Fund is responsible for these activities:

- ▶ Promoting JESSICA to potential investors and providing advisory;
- ▶ Searching out potential projects;
- ▶ Conducting financial transactions between the UDF and JESSICA loan recipient;
- ▶ Monitoring projects and preparing interim reports for the Investment Council and the RC NE.

Fund Investment Board

The Investment Board is the Fund's managing body. Its members are representatives of the RC NE as well as other outside expert appointees and representatives of regions, cities or other regional institutions. The number of Investment Board members and voting rights will be defined in the Fund's foundation documents and the funding agreement concluded with the RC NE. The Fund's Investment Board approves all strategic documents and methods for selecting projects suitable for JESSICA funding; it also approves the announcement of calls for submissions and decisions on the provision of JESSICA funding.

Fund Management

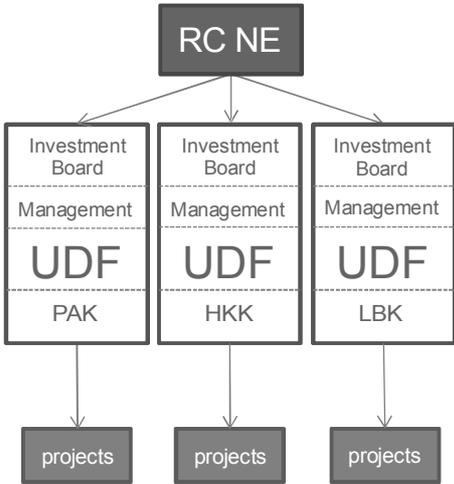
This represents the Fund’s executive body – it sees to all operating activities, including preparation of the Fund’s strategy, the announcement and preparation of calls for submissions, the analysis of submitted applications – verification of a project’s financial return, applicant solvency, verification of financial guarantees, the creation of source documentation for the Investment Board decision-making process and project monitoring. The Fund management will be selected based on a tender procedure (pursuant to Act No. 137/2006 Coll. on public contracts) after the UDF is established, if such UDF is a standalone legal entity. When the UDF is a separate unit within a financial institution, the management is selected before the funding agreement is concluded. This second variant applies on the condition that the financial institution serves as the UDF manager. The Fund’s activity may be broken down into an “administrative part” and a “financial part”. Therefore, the activity may be carried out by a single entity or, alternatively, the “administrative part” of the Fund’s activity will be carried out by the RC NE using its own resources (the Office of the RC NE) and only the “financial part” will be carried out using outside resources (e.g. a bank selected based on a tender procedure).

The disadvantages of this implementation structure include its relatively sluggish pace. Financial resources from the EDRF will be conveyed to the UDF after the UDF has been established and an agreement has been concluded between the RC NE and UDF or its management.

5.2. Implementation Variant II

This is the same as Variant I with the sole difference that a separate urban development fund is created for every region comprising the NUTS II NE region. The RC NE establishes three separate Funds for which tender procedures are conducted to select a Fund manager. Each Fund will administer the financial resources for calls/projects for the one region. Thus, the Fund’s Investment Board could, in addition to the RC NE representatives, include representatives of the region for which the UDF has been established. The powers of the UDF Investment Board and management are identical to those in Variant I.

The reasons that multiple UDFs might be set include the use of financial resources from various operational programmes to which differing allocation rules apply. This thematic breakdown based on original operational programme would give shape to the newly established Funds and their funding rules (per a funding agreement).

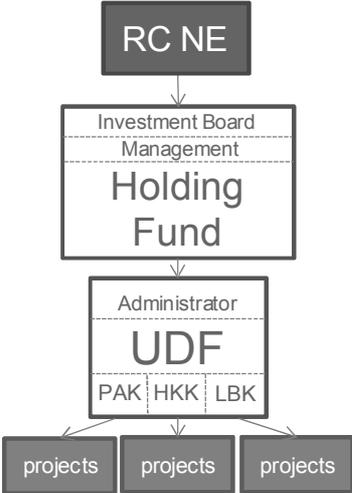


The benefits of this implementation structure include a greater emphasis on bringing Funds closer to their regions.

The disadvantages of this structure include higher fees for managing three separate Funds, higher administrative costs for the RC NE due to the existence of three separate Funds and, like in Variant I, its relatively sluggish pace.

5.3. Implementation Variant III

This variant entails the addition of a separate financial and administrative component – a “Holding Fund” – operating as an intermediary between the RC NE and the UDF.



Specifics of Variant III

The Holding Fund may be established as a standalone legal entity or as a separate financial unit within a financial institution²¹. The Holding Fund assumes temporary custody of financial resources contributed by the RC NE or the resources of other HF co-founders. Resources lodged with the HF are interest-bearing in the period between their transfer from the ERDF to the UDF. The primary role of the HF is to select a suitable manager (administrator) in the region for the Urban Development Fund/Funds (UDF) into which HF resources would then be invested. The Holding Fund organises a tender procedure for this purpose. In the case of an HF set up under EIB management, this tender procedure is not organised according to national law, but rather EIB rules. After an analysis of the proposals submitted by potential UDF administrators, a key component of which is the proposed UDF business plan (or other suitable document), the HF manager submits a proposal to the HF Investment Board. The members of the HF Investment Board are appointed by the Managing Authority, i.e. the RC NE. The Investment Board makes the UDF administrator selection; based on its decision, the HF management enters into an operating agreement between the HF and the UDF. The operating agreement is also subject to HF Investment Board approval. After the agreement is concluded between the UDF and the HF, the HF invests the resources into the UDF, either as a lump sum or incrementally contingent on the status of individual selected projects. The HF management continuously monitors the activity of the UDF and submits reports to the Managing Authority.

In this variant, too, a key implementation process role is played by the Urban Development Fund (UDF), which is focused on the region and acts as a funding intermediary for individual projects. The UDF prepares and announces calls for submissions of projects, provides advisory to potential submitters, actively promotes the preparation of projects and performs financial analyses of projects. The UDF decision-making mechanisms, including any involvement of public authorities, are described in the operating agreement between the HF and UDF. Key HF activities include selecting a quality UDF manager, setting the contractual terms between the HF and UDF and overseeing UDF activity. The primary role of the UDF is to ensure timely and efficient investment in urban development projects while achieving optimal socio-economic benefits and the desired financial return.

The variant that includes Holding Fund involvement enables the fastest transfer of financial resources from the operational programme to the JESSICA Fund. This timely transfer may incentivise the potential

²¹ In practice, there are 15 JESSICA Holding Funds operating in Europe as of 12 July 2010, of which 14 have been founded as a separate financial unit within the EIB, which also administers these HF, and the remaining HF was founded as a separate financial unit within the Estonian national financial institution KredEx.

UDF administrator to draft business plans and potential implementers of financially repayable projects to prepare such projects. Moreover, the speedy creation of a Holding Fund facilitates the allocation of unused operational programme resources (for which there will not be calls for submissions) in the form of repayable financial resources from subsidy recipients. From a timing perspective, then, this assures adherence to the N+2 and N+3 rules, respectively. Other benefits of this variant include the simplified Urban Development Fund selection and monitoring process from the point of view of the RC NE.

The extent to which transfer of resources to a JESSICA Fund (either a HF or a UDF) may have a catalytic effect on the preparation of financially repayable projects in the region of course depends also on whether a potential market of revenue-generating urban projects exists in the region. This study has identified a number of areas and project types where it can be expected that viable revenue-generating projects can be prepared. Needless to say, it is very important that work on project preparation starts sufficiently early - preferably no later than at the moment when it is obvious that some of the ROP resources will be used only through repayable instruments.

In the case of Variant III, the structural funds rules provide for the non-tendered appointment of the EIB as the HF manager. As the EIB is an EU financial institution mandated not to generate profit, the EIB only provides Managing Authorities with HF administrator services on the basis of actual costs.

5.4. Proposed optimal implementation structure for NUTS II NE

Our investigations indicate that a combination of Variants I and III represents the best solution. Implementation could be divided into two separate but linked steps.

In the interest of expediting the transfer of financial resources from the ERDF, the RC NE sets up a Holding Fund, which appoints the EIB to the position of Fund manager without holding a tender procedure (Variant III). RC NE and other regional representatives will be appointed to the Holding Fund Investment Board. The RC NE will thus ensure that resources from unused structural funds and returned funding from recipients remain available sources of funding in the NUTS II NE region. The EIB launches a tender procedure for the position of Urban Development Fund administrator (operator). This tender procedure will not be launched according to Czech law, but rather in accordance with the EIB internal rules. The selected entity will then be submitted to the HF Investment Board for approval. If the Investment Board approves the proposed entity, an operating agreement is concluded between the Holding Fund and the UDF. This agreement is also subject to Investment Board approval. After an agreement is concluded between the UDF and the EIB, the EIB invests the HF resources in the UDF. The UDF will be headquartered in the region and see that the investment is transferred to individual projects. The UDF may in part be staffed by qualified employees of the Office of the RC NE, while some UDF activity may be carried out by the bank.

After the initial phase of JESSICA implementation is completed, the RC NE organises a tender procedure in which it selects a new Holding Fund administrator or it decides to terminate the activity of the Holding Fund and only maintain the UDF (Variant I), while HF receivables from the UDF would be transferred to the RC NE or another competent authority. Variant II may at the same time be considered, i.e. a new UDF would be established at the level of each region. In this phase, there is no longer a threat of timing delays in the allocation of additional financial resources. In the initial implementation phase, moreover, sufficient advantage will be taken of EIB technical assistance and know-how.

6. Proposed action plan

The following list describes key steps in the JESSICA implementation strategy for the NUTS II NE region. The individual steps are listed chronologically, though some may be carried out concurrently or in an alternative order:

- ▶ The Committee of the Regional Council of the Northeast Region approves the transfer/allocation of financial resources from certain ROP NE support areas to the future JESSICA Fund;
- ▶ The RC NE secures the Czech Republic's 7.5% capital participation in the future JESSICA Fund;
- ▶ The RC NE secures the remaining 7.5% of resources that must be provided from other public sources (e.g. a contribution from regions or cities);
- ▶ The RC NE decides on an implementation structure;
- ▶ The RC NE concludes a funding agreement with the UDF, or HF, management;
- ▶ The RC NE solicits the European Commission for an interim payment from the ERDF;
- ▶ The requirements for regional support are determined (e.g. IUDP requirements are defined);
- ▶ The UDF commences operation;
- ▶ The first calls for submissions are announced, consultations are held with potential applicants, applications are evaluated.

The first step in JESSICA implementation in the region is the RC NE decision on the transfer of a financial allocation. It is not clear at this moment how large a financial amount this would be. At the same time, the RC NE must secure 15% co-funding.

It must be noted here that the creation of the JESSICA Fund, creation of its investment strategy, selection of a manager and preparation of any related changes in the ROP would be more easily implementable in the case of the clear appropriation of resources for transfer to the JESSICA Fund than in a case where questions of the amount and source of resources to be transferred to the JESSICA Fund were to be left open. Aside from the administrative demands of implementation based on an unspecified amount of resources, we must consider the fact that the use of resources allocated to the JESSICA Fund as part of the ROP will be tied to the specific requirements of the support areas from which resources are transferred to the Fund (e.g. types of projects and costs that may be funded in a given support area).

In this report, we presented three different implementation structures and recommended an optimal variant for the NUTS II NE region. The RC NE is responsible for the final decision on the implementation structure form. The implementation structure must differentiate between versions with and without a Holding Fund. The benefits of an implementation structure that includes a Holding Fund are described in Variant III of the implementation structure. Should the decision be made to include a Holding Fund administered by the EIB, there will be no need to organise a tender procedure for this purpose, which will accelerate the financial resources transfer process. Based on a funding agreement, the EIB will organise a tender procedure for a UDF administrator and evaluate the tender submissions (whereas the final decision will be in the competence of the HF Investment Board). Should a Holding Fund not be established, a tender procedure for UDF management shall have to be organised by the RC NE.

From the timing perspective, we may distinguish between the variant with a holding fund (variant III) and the variant without – with UDF alone (variants I and II). Were variant I or II to be chosen, the above mentioned JESSICA implementation steps may be expected to be carried out 14 to 16 months after approval of the shift in funding resources to the future JESSICA fund. Variant III implementation may be broken down into two stages. The first is the signing of a funding agreement with a selected holding fund manager: in the case of the recommended variant, the EIB. This stage may be realised within 2 months of decision adoption. The next stage is selection of a local UDF manager. The process is subject to the internal rules of the EIB and comprises several parts (call for expressions of interest, first phase of evaluation, second phase of evaluation, selection decision). We may expect the EIB to select a UDF manager within 10 – 12 months based on experience with JESSICA implementation in the NUTS II Moravia-Silesia region, for a total time savings of 2 to 4 months. The specific situation would represent

a decision in which a detached branch of the Office of the NE Regional Council would carry out the work of the UDF, thus greatly reducing the UDF manager selection time.

The initial implementation structure set-up may be altered and the organisation structure optimised subsequent to the introductory phase.

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