



Blending EU Structural and Investment Funds and PPPs in the 2014-2020 Programming Period

Guidance Note

January 2016



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Table of contents

Executive summary	10
1 Introduction	15
1.1 Background	15
1.2 Purpose and focus of this guidance note	15
1.3 Structure of this guidance note	16
2 Overview of EU funding.....	17
2.1 The multiannual financial framework.....	17
2.2 European Structural and Investment Funds	17
2.3 Some key terms and principles	19
2.4 Partnership Agreements and Operational Programmes	19
2.5 Managing Authorities	20
2.6 Allocating grants.....	20
3 The concept of blending in PPPs.....	22
3.1 Rationale for blending	22
3.2 Blended structures and their limitations under the previous regulations	23
3.3 Past blending activity and implementation issues.....	27
3.4 Impact of the new regulations	27
4 Legal and administrative framework for Blended Projects	29
4.1 Common Provisions Regulation on ESI Funds.....	29
4.2 Relevant delegated acts.....	30
4.3 State aid issues in the context of EU-supported PPP projects	30
4.4 Eurostat issues in the context of EU-supported projects	31
4.5 Issues related to the procurement of PPPs	32
5 PPP-specific provisions of the CPR.....	33
5.1 Beneficiary of ESI Funds for Blended Projects	33
5.1.1 <i>Who can be the beneficiary of a grant using ESI Funds?</i>	33
5.1.2 <i>Procuring authority as beneficiary</i>	33
5.1.3 <i>Conditions for the private partner to be the beneficiary</i>	34
5.1.4 <i>Replacement of the private partner beneficiary</i>	34
5.1.5 <i>When can a grant Decision be received?</i>	35
5.2 Eligibility of project expenditure in Blended Projects	37
5.2.1 <i>When expenditure is considered eligible</i>	37
5.2.2 <i>Escrow account</i>	38
5.2.3 <i>What type of expenditure is eligible?</i>	41
6 The PPP project blending cycle.....	43
6.1 Importance of sound project preparation in the grant application process	43
6.2 Potential sequence of activities in the project blending cycle	44
6.2.1 <i>Overview of the PPP project cycle</i>	44
6.2.2 <i>Expected blending activities in the PPP project cycle phases</i>	44
7 Key provisions of the CPR relevant to revenue-generating Blended Projects ...	52
7.1 Main factors that determine the amount of grant funding	52
7.2 Revenue-generating projects and determining the funding gap	53
7.2.1 <i>Relevant regulations</i>	53
7.2.2 <i>What is a revenue-generating project?</i>	53
7.2.3 <i>How is the net revenue impact on eligible costs determined?</i>	55

7.2.4	<i>The flat-rate method</i>	55
7.2.5	<i>The decreased co-financing rate method</i>	56
7.2.6	<i>The discounted net revenue method</i>	56
7.2.7	<i>Determining the EU grant</i>	61
8	Practical considerations in planning, procuring and managing a Blended Project	64
8.1	Description of the Blended Project illustration case	64
8.2	When to secure the grant approval?	65
8.3	What is the impact of different PPP structures on the level of the grant?.....	67
8.4	What is the expected grant amount if the project is expected to be revenue-generating?	68
8.4.1	<i>Calculation of the grant using the flat-rate method</i>	69
8.4.2	<i>Calculation of the grant using the discounted net revenue method</i>	69
8.5	Who will be the beneficiary of the grant?	73
9	Particular issues regarding Major Projects	74
9.1	Relevant regulations	74
9.2	Securing a grant from ESI Funds for a Major Project	75
9.2.1	<i>Grants application requirements</i>	75
9.2.2	<i>Assessment of grant applications</i>	77
10	Getting technical support	80
10.1	JASPERS	80
10.2	EPEC	81
10.3	The Connecting Europe Facility	81
11	Conclusion	83
	Annex I – Blended Project illustration case calculation tables	84
	Annex II – Worked example of the impact of change in discount rate	91
	Annex III – Main changes in the rules for Major Projects compared to the 2007-2013 programming period	93

Glossary of terms

Blended Project	a PPP project within the EU that combines public funding and private financing and where part of the public funding is provided directly to the project in the form of a grant from an ESI Fund
bn	billion (i.e. 1bn equals 1 000 000 000)
CBA Guide	Guide to Cost-Benefit Analysis of Investment projects , published by the Commission (DG Regio) in December 2014
CBA IR	Annexes II and III to the Commission Implementing Regulation (EU) 2015/207 of 20 January 2015 , supplementing Article 101 of the CPR, providing the models for submission of information on a Major Project and the methodology for carrying out cost-benefit analysis
CEF	the Connecting Europe Facility, a Commission initiative supporting trans-European networks and infrastructure in the transport, telecommunications and energy sectors
Certifying Authority	the authority that certifies to the Commission that the grant expenditure complies with applicable EU and national rules, based on verifiable supporting documents submitted by the Managing Authority
CF	Cohesion Fund
Commission	European Commission
commercial close	the point at which terms of the PPP are agreed and the PPP agreement is signed. This is usually concomitant with, or followed shortly by, financial close when the financing agreements are finalised
completion	completion of construction of a project asset for which the grant funding is made available
CPR	Common Provisions Regulation, Regulation (EU) No 1303/2013 of the European Parliament and of the Council of 17 December 2013
CSF	Common Strategic Framework referred to in Annex I to the CPR

DG MOVE	Directorate-General for Mobility and Transport of the Commission
DG REGIO	Directorate-General for Regional and Urban Policy of the Commission
EAFRD	European Agricultural Fund for Rural Development
EIB	European Investment Bank
EMFF	European Maritime and Fisheries Fund
ERDF	European Regional Development Fund
ESF	European Social Fund
ESI Fund	European Structural and Investment Fund available from the EU budget, namely: EAFRD, EMFF, ERDF, ESF and CF
EU	European Union
Financial Instruments	EU measures of financial support provided on a complementary basis from the EU budget in order to address one or more specific policy objectives of the EU. Such instruments may take the form of equity or quasi-equity investments, loans or guarantees, or other risk-sharing instruments, and may, where appropriate, be combined with EU grants
financial close	the point at which, for a PPP, all financing agreements are signed and all the required conditions contained in them have been met. It enables financing and funding sources for the project (e.g. loans, equity, grants) to start flowing so that project implementation can start ¹
GNI	Gross National Income
ICT	information and communication technology
INEA	Innovation & Networks Executive Agency ²
implementation	in CPR terms, usually refers to the period during which the project is being constructed and when grant amounts are disbursed

¹ For a detailed description of the activities related to financial close, see the [EPEC PPP Guide](#).

² INEA is the successor to the Trans-European Transport Network Executive Agency (TEN-T EA); it is one of the agencies related to DG MOVE and its remit is to bring expertise and high-quality programme implementation to the management of infrastructure and research projects in the fields of transport, energy and telecommunications, and to promote synergies between such activities for the benefit of the project promoters, the Commission and stakeholders.

Implementation Guidance	Implementation Guidance on Operations Generating Net Revenues , Version 2 – 24/03/2014 published by DG REGIO in March 2014
IQR	Independent Quality Review, a review carried out by independent experts (as delegated to JASPERS or other experts that Managing Authorities may select) of a Major Project as part of the process of project approval required under Articles 101 and 102 of the CPR
JASPERS	Joint Assistance to Support Projects in European Regions initiative (http://www.jaspers-europa-info.org/)
m	million (i.e. 1m or 1 000 000)
Major Project	project with eligible costs in excess of EUR 50m or, generally in the case of a transport project, in excess of EUR 75m ³ and which is subject to additional information and approval processes as set out in the CPR
Member State	State that is a member of the EU
Managing Authority	the authority that bears the main responsibility for the effective and efficient deployment of EU funds and thus fulfils a substantial number of functions related to programme management and monitoring, financial management and controls as well as project selection
MFF	multiannual financial framework of the EU, laying down the maximum annual amounts that the EU may spend in different fields over a period of at least five years. The current MFF covers seven years, from 2014 to 2020: it is not the budget of the EU but provides a framework for financial programming and budgetary discipline ensuring that EU spending is predictable and stays within agreed limits
OP	Operational Programme, a document drawn up by a Member State in accordance with the Partnership Agreement between the Member State and the Commission, setting out the strategy and priorities of the relevant ESI Fund as well as the level of funding support at EU and national levels
Partnership Agreement	document agreed by a Member State and the Commission, setting out the thematic objectives for

³ See CPR, Articles 100–103 for a legal definition.

each of the ESI Funds in the Member State and the indicative allocation of support from the EU⁴

PPP	public-private partnership, which is defined in the CPR as forms of cooperation between public bodies and the private sector that aim to improve the delivery of investments in infrastructure projects or other types of operations, delivering public services through risk sharing, pooling of private sector expertise or additional sources of capital
PPP DR	PPP Delegated Regulation, Commission Delegated Regulation (EU) 2015/1076 of 28 April 2015 , supplementing the CPR and laying down additional rules on the replacement of a beneficiary and on the related responsibilities and minimum requirements to be included in PPP agreements funded by grants from ESI Funds, including in relation to Articles 63(4) and 64(4) of the CPR
private partner	the private sector entity that contracts with the procuring authority under a PPP arrangement
priority axis	comprises one or more investment priorities of an ESI Fund, corresponding to one or more thematic objectives highlighted in a Partnership Agreement. Priority axes are referred to in OPs and are used to define the targets and indicators of an OP for management and reporting purposes
procuring authority	the public sector entity responsible for procuring a project as a PPP and subsequently usually the public sector partner in a PPP
programming period	the period covered by an MFF, the current programming period running from 2014 to 2020. The term is usually used in the context of the procedures that are required to take place over the period of the MFF in the context of the agreed allocation of resources under a financial framework for the same period
project	in the context of this guidance note, an ‘operation’ or ‘action’ in CPR terms (i.e. an investment project that contributes to the objectives of a priority axis)
PPP project	a project implemented or intended to be implemented under a PPP arrangement

⁴ See CPR, Articles 14-17 on the definition, content, preparation and amendment of a Partnership Agreement.

RDI	research, development and innovation
RGDR	the Revenue-Generating Delegated Regulation, Commission Delegated Regulation (EU) No 480/2014 of 3 March 2014, supplementing the CPR, including in relation to CPR, Article 61 (3)(b)
VAT	value added tax
VfM	value for money

Executive summary

Combining European Structural and Investment Funds (ESI Funds) with private financing resources in a PPP structure is often referred to as 'blending'. Around EUR 450bn of ESI Funds are potentially available over the current 2014-2020 programming period to support public investment and help deliver EU regional and cohesion policy. While most of these resources can be expected to be deployed in more traditional, purely grant-funded structures, blending these resources with private finance can generate additional benefits in certain circumstances.

Rationale for blending

Blending can be attractive from an ESI Funds perspective as the use of a PPP structure may bring additional disciplines in the deployment of funds and improve value for money (VfM). Such PPP disciplines typically include encouraging long-term approaches that take into consideration proper assessment of, and provision for, the life-cycle maintenance and operating costs of delivering the public service, not just the cost of constructing the underlying asset. PPPs involve paying the private sector partner on delivery of the service as opposed to delivery of the underlying asset. This helps to ensure that a project is delivered to the agreed time and budget. PPP disciplines may also encourage efficient risk management by allocating a particular risk to the most appropriate party involved and unlocking benefits of third party project scrutiny from investors and lenders. A PPP delivery approach may therefore help to improve the long-term quality and effectiveness of public expenditure in the use of ESI Funds.

From the perspective of a public authority seeking to develop a PPP, blending can reduce the quantum of national funding resources that may be required to pay for the project or, in the case of user-pay PPPs, the level of user charges required. The use of ESI Funds may therefore make the PPP project more affordable for the procuring authority and/or for users. At the same time, blending may improve the bankability of the PPP as a result of lowering the levels of private finance that need to be raised.

Constraints to blending under previous programming periods

To date however, blending operations have been quite limited. According to EPEC research, in the programming periods from 1994-99 to 2007-13, only 50 Blended Projects reached financial close compared to over 1 500 PPP projects that did not involve blending. Limited public sector capacity to manage the combination of grant funding and PPP preparation and procurement processes appeared to be the single most important barrier. The research also suggested there was often a perception among project sponsors that Blended Projects would not be accepted by Managing Authorities or the Commission.

The need to select the private partner in advance of the grant application created, in many cases, unacceptable risks for procuring authorities who could find themselves having to guarantee the availability of funding in the event that the grant from the ESI Fund was not approved or reduced. The uncertainties in establishing the grant amount, particularly for projects classified as '*revenue-generating*' under the relevant

regulations, also added risk and complexity for procuring authorities. The Blended Projects that were concluded often involved a lengthy two-step process.

Another constraint appeared to be the requirement for grants to be disbursed within two years of planned expenditure and within two years of the end of the Operational Programme (OP), at the latest. These requirements were not well suited to accommodate PPP structures where payments are made over the much longer-term service delivery period. Those Blended Projects that were carried out therefore could only use grants to help pay for up-front capital costs, limiting the full benefits of a PPP as a procurement tool that links payment to long-term service performance.

Current programming period regulations

In December 2013, the Common Provisions Regulation (CPR) was published, providing a common set of terms for the use of ESI Funds in the current programming period. Importantly, the CPR explicitly recognises the relevance of PPPs as an *'effective means of delivering operations which ensure public policy objectives'*. The CPR also includes a helpfully broad definition of PPPs. But most significantly, the CPR, and the subsequent delegated acts published in the course of 2014/15, include provisions (detailed below) that better enable the use of grant funding in PPP projects. These address a number of important obstacles that previously hindered the blending process.

Of course, ESI Funds can be used to support projects in other ways than directly providing grants for investment costs. Financial Instruments, supported by EU funding, provide financing products that play an increasingly important role in the financing (as opposed to grant funding) of PPPs. This is a form of blending in a wider sense of the term. Grant funding may also be available to support the preparation costs of projects, including those delivered as PPPs, as is possible under the Commission-managed Connecting Europe Facility (CEF), which is governed by its own regulations. The use of Financial Instruments and CEF resources is not however covered in this guidance note, which focuses exclusively on ESI Funds available in the form of grants. Nevertheless, it is important to be aware of the other ways of combining EU funds with private finance.

Many of the requirements for more traditional uses of grants apply to blending. It is important for procuring authorities that promote and 'own' PPP projects to understand these requirements. They include the requirement for the project to be identified as a part of, or compatible with, the 'priority axes' established as a part of an agreed OP for the current programming period, as well as the requirements around cost eligibility, revenue generation and grant disbursement. A successfully executed Blended Project depends on the procuring authority and Managing Authority working closely together.

What has changed?

To address the constraints of the previous funding regulations highlighted above, the new regulations have introduced a number of improvements including:

Conditional approval of the private sector beneficiary: while the grant beneficiary could be a public or private sector body under the previous regulations, the new regulations permit conditional approval of a private sector beneficiary prior to its selection as the private partner under the PPP procurement process. This has important benefits:

- *in terms of timing:* where the intention is for the private partner to be the beneficiary, a procuring authority is now able to proceed with the grant application in parallel with, and prior to, completing the PPP procurement. This should allow for a faster overall process in these circumstances; and
- *in terms of risk:* the procuring authority can avoid being exposed to any grant shortfall as a result of otherwise having to commit to a PPP agreement before the grant amount is known.

Accommodation of longer-term PPP payment schedules: the new regulations allow for grant proceeds to be disbursed to the private partner beyond the end of the programming period. This allows for payments to be made to the private partner that are more in line with the longer-term payment profile of the PPP agreement. This works by disbursing the grant into an escrow account, controlled by the procuring authority, from which payments can subsequently be made to the private partner in line with a payment schedule that has been agreed as part of the PPP arrangement. The PPP agreement should include the operational and reporting requirements of the escrow account and the basis upon which the bank providing the escrow account is selected.

Ability to replace the grant beneficiary without loss of grant: the new regulations can better accommodate lenders' step-in and substitution rights, which are vital to most PPP financing arrangements.

Simplified approaches for revenue-generating projects: the regulations for ESI Funds require that if a project is expected to generate revenue (i.e. users are expected to pay a charge for the service), such revenue, net of operating costs, should be deducted from the eligible project costs. As revenue can be used to help fund the project, grants from ESI Funds are only available to meet any 'funding gap' that remains. The regulations require this gap to be calculated on the basis of cost and revenue projections and in line with a set of conditions that take into account residual values and the use of justified discount rates. This calculation can be complex. While this approach is still available, the new regulations provide considerably simplified alternatives, using pre-established funding gap rates ('flat rates') for particular sectors. Furthermore, the grant amount, if calculated in this way, is not at risk of subsequent reduction as a result of later, policy-driven, changes in revenue. For projects that are not expected to generate revenue, e.g. government-pay PPPs, such analysis is not required.

Major Projects and the importance of thorough project preparation

Thorough project analysis and preparation, however, remains a key element of successful applications for an ESI Funds grant. This is equally applicable to Blended Projects. In addition to ensuring that the purpose of the project is in line with the

priority axes for the relevant ESI Fund and that the expenditure meets the general eligibility criteria, the success of a grant application will depend on fully addressing the information requirements for the project. The new regulations set out in some detail the requirements for Major Projects (i.e. projects with eligible costs above EUR 50m or EUR 75m in the case of transport projects aimed at promoting sustainable transport and removing bottlenecks in key network infrastructure). Information requirements include the need for a clear identification of expected project costs, assessment of different project options, cost-benefit analysis, risk analysis, environmental impact assessment and a clear financing plan and timetable.

Due to their size and sector, many Blended Projects can be expected to be Major Projects. Accordingly, the preparation requirements for a grant application using ESI Funds are not dissimilar to those that would in any case be required for a well-prepared PPP project. In other words, much of the preparation work for a PPP will be the same as for the grant application.

With respect to the grant approval process, the new regulations now provide the option for the procuring authority to choose between the Commission appraising the grant application for a Major Project and the use of an Independent Quality Review (followed by a no-objection from the Commission), a function that can be carried out by JASPERS. In both cases, the Commission approval is conditional on the PPP agreement being signed within three years.

Key decisions in the blending process and interaction with the PPP process

The new regulations should allow for the PPP and grant application preparation to work better together. Indeed, the design and preparation of the PPP and grant application are interdependent in a number of important areas. The PPP preparation process will therefore play an important role in informing some of the key decisions that need to be taken in preparing the application for a grant. These include:

- *choice of beneficiary*: this will be driven by the nature of the PPP. Should, for example, the procuring authority decide that the form of PPP will involve availability payments, then it may wish to designate itself as the beneficiary in order to control payment of the grant proceeds in line with performance-based payments;
- *choice of level of the grant*: the form of the PPP may also determine the level of the grant that can be applied for. If users are required to pay or part-pay for the project through user charges, the revenue from these charges will need to be taken into account in determining the grant amount in accordance with the rules on revenue-generating projects;
- *choice of payment mechanism and timing of grant disbursement*: the nature of the PPP will determine if the grant is disbursed as a direct contribution towards capital costs as they are incurred (reducing future user charges or availability payments) or used as a contribution towards future availability payments, linking payment to long-term performance; and
- *choice of timing of the grant application*: the procuring authority will need to decide whether it wishes the Managing Authority to apply for the grant after completion of the PPP procurement process or for the Managing Authority to

seek a conditional approval in parallel with the PPP procurement phase. The latter strategy may speed up the overall process and reduce the risk of committing to a grant funding level in the PPP structure that may not materialise. Bidder interest and the quality of bid preparation are usually enhanced when all sources of funding for the project are known.

Availability of technical assistance

Initiatives led by the Commission and EIB include the provision of access to technical assistance and independent experts to support procuring authorities and Managing Authorities with the blending process. Importantly in the blending context, these include JASPERS, which supports Managing Authorities in beneficiary countries in preparing Major Projects for grant applications using ESI Funds, and EPEC, which also provides PPP policy and upstream PPP project support to public authorities (working with JASPERS on blending issues as required). Further forms of technical support and guidance are also often available at national levels.

Looking ahead

Overall, the new regulations provide a number of significant improvements to the blending process. They provide more choice, greater simplification and better compatibility between the ESI Fund grant application and PPP processes than were previously available. Undoubtedly, the regulations cannot be expected to cover every eventuality. It will remain to be seen in practice how the regulations will be implemented by procuring authorities and Managing Authorities and how they will work in practice. EPEC will seek to revise and update its blending guidance to reflect the collective experience gained once Blended Projects materialise under the new regulations.

1 Introduction

1.1 Background

Since the establishment of EPEC in 2008, EPEC Members and other public stakeholders have expressed interest in the subject of Blended Projects. In this context, a Blended Project is a project delivered within the EU under a public-private partnership (PPP) arrangement that combines public funding and private finance where part of the public funding is provided directly to the project in the form of a grant from a European Structural and Investment Fund (ESI Fund).

Through different network activities and a pan-European stocktake exercise,⁵ EPEC and its Members identified a number of challenges facing public authorities when attempting to deliver Blended Projects and mapped potential solutions to these challenges. These network activities were timely as further development of the rules on the deployment of EU funds were being proposed by the European Commission (the Commission) and discussed among Member States and the European Parliament ahead of the 2014-2020 programming period. EPEC and its Members took an active role in this process, helping to identify some of the earlier challenges to delivering Blended Projects and proposing solutions.

The final version of the Common Provisions Regulation (CPR) for ESI Funds was approved on 17 December 2013. This set out the key regulations that govern the use of the main sources of EU funding for investment projects. Many of the Blended Project-related provisions of the CPR and associated delegated acts are based on contributions from EPEC and its Members. Consequently, the CPR contains some significant positive developments and improvements for Blended Projects for the current programming period. The CPR was followed in 2015 by a subsequent delegated act which provides some further clarity on blending.

1.2 Purpose and focus of this guidance note

With the new PPP-related provisions in place in the CPR, and in keeping with its goal to foster better PPPs, EPEC has developed this guidance note to (i) raise awareness of the challenges inherent in delivering Blended Projects and (ii) update and improve the general understanding of the practical implications and possibilities afforded by the new regulations for Blended Projects.

This guidance note focuses on the principles, rules and regulations applicable to the use of ESI Funds. This is the funding that is available under the various funds/programmes that are regulated by the CPR and together represent the single largest potential source of EU funding for Blended Projects.⁶ While blending of ESI

⁵ See [EU Funds in PPPs – Project Stocktake and Case Studies](#), EPEC report, May 2012. See also [Poznan Waste-to-Energy Project, Poland. Using EU Funds in PPPs Case Study](#), EPEC report, June 2012 and [Using EU Funds in PPPs - explaining the how and starting the discussion on the future](#), EPEC report, May 2011.

⁶ This guidance note is focused on the co-funding of PPP projects with ESI funds and does not take into account the rules related to funds allocated to the Connecting Europe Facility. See Regulation (EU) No 1316/2013 of the European Parliament and of the Council of 11 December 2013 establishing the Connecting Europe Facility.

Funds with PPPs could be understood to cover a wide range of different forms,⁷ this guidance note focuses **only** on the use of ESI Funds provided in the form of direct project grant support as opposed to other forms of project support from ESI Funds, such as Financial Instruments.

Furthermore, this guidance note does not cover blending EU funds in PPP structures outside the EU.

1.3 Structure of this guidance note

This guidance note is structured as follows:

- **Chapter 2** provides a brief introduction to the framework of EU funds and introduces some of the jargon that is widely used across this area for those who are less familiar with EU grant funding mechanisms;
- **Chapter 3** describes the rationale for blending and, conceptually, the different ways in which it is possible to blend grants from ESI Funds with national funding and private finance sources in a PPP structure. This Chapter also examines some lessons drawn from past programming periods;
- **Chapter 4** sets out the broad legal and administrative framework for blending grants under ESI Funds with PPPs and identifies some of the main issues related to implementing Blended Projects;
- **Chapter 5** focuses on the more detailed CPR provisions specific to Blended Projects;
- **Chapter 6** sets out the steps that might be expected in the preparation and implementation of a Blended Project, based on the PPP project cycle and the relevant regulations, and highlights the close interaction that needs to take place between the PPP and grant-related processes;
- **Chapter 7** sets out the key provisions of the CPR relevant to revenue-generating Blended Projects, including methods for determining the funding gap;
- **Chapter 8** describes some of the issues related to the practical implementation of Blended Projects covered in Chapters 5, 6 and 7, using an illustration case;
- **Chapter 9** describes the legal basis and different options for the preparation and assessment of the grant application for Major Projects;
- **Chapter 10** provides an overview of the different sources of support available to provide advice to stakeholders involved in Blended Projects; and
- **Chapter 11** draws the main conclusions from the above.

⁷ See [JASPERS Working Paper Combining EU Grant Funding with PPP for Infrastructure: Conceptual Models and Case Examples](#), December 2010.

2 Overview of EU funding

For those less familiar with EU grant funding mechanisms, this Chapter provides a brief context and introduction to the framework of EU funds. It also introduces some of the jargon that is widely used across this area. EPEC's 2011 note '[Using EU Funds in PPPs – explaining the how and starting the discussion on the future](#)' and the '[Project Stocktake of EU Funds in PPPs](#)' carried out in 2012, also provide some useful background to EU funding issues in line with the regulations in place at the time.

2.1 The multiannual financial framework

The programming of EU funds is set within the context of an agreed multiannual financial framework (MFF) covering a specified 'programming period' (the current one being 2014-2020). The MFF allows for long-term financial planning, setting the overall limits to the amounts of money that may be spent from the EU budget in a range of agreed policy areas. To allow for flexibility over the period in line with economic activity, the overall funding envelope is also expressed as a percentage of the EU's estimated Gross National Income (GNI). This percentage is updated every year on the basis of the latest available GNI forecasts. Annual EU budgets are then set within (and usually a little below) the framework of the MFF amounts and the MFF itself can be reviewed (as it will be in 2016). Annual EU budget expenditure must be completely covered by annual revenue - the EU budget cannot operate a deficit.

The MFF is divided into six broad categories of expenditure ('headings') corresponding to different areas of EU activity: (i) smart and inclusive growth; (ii) sustainable growth and natural resources; (iii) security and citizenship; (iv) global Europe; (v) administration and (vi) compensations. The different funding programmes are designed to support the delivery of EU policy under these headings.

The legal basis for spending in different policy areas is established through various regulations in accordance with the MFF framework. Regulations for the individual funding programmes typically set out the conditions of eligibility and the criteria for the allocation of EU funds. An example is the CPR which covers five funds described further below.

2.2 European Structural and Investment Funds

A significant proportion of funding made available under the current MFF is allocated through five large Funds, representing EUR 443.2bn. These funds, known collectively as the ESI Funds, have agreed objectives that underpin the core of the EU's cohesion policy and the delivery of Europe's 2020 Strategy for Growth. ESI Fund resources are allocated to Member States and delivered through national, regional and cross-border programmes under the regulatory framework of the CPR. The ESI Funds (and the amounts indicated over the 2014-2020 programming period) comprise the:

- European Regional Development Fund (ERDF) – EUR 199.4bn;
- European Social Fund (ESF) – EUR 88.8bn;
- European Agricultural Fund for Rural Development (EAFRD) – EUR 85bn;
- European Maritime and Fisheries Fund (EMFF) – EUR 6.4bn; and
- Cohesion Fund (CF) – EUR 63.6bn.

Of these Funds, the ERDF and the CF, which both fall under the Directorate-General for Regional and Urban Policy (DG REGIO) of the Commission, are potentially the most relevant for Blended Projects.

The **ERDF** focuses on several key thematic areas (innovation, digital agenda, SMEs and low-carbon). The extent to which a particular project needs to address one or more of these themes is known as 'thematic concentration'.

The **CF** on the other hand focuses on addressing economic and social disparities and the promotion of sustainable development. It is aimed at Member States with a GNI per inhabitant that is less than 90% of the EU average (Bulgaria, Croatia, Cyprus, the Czech Republic, Estonia, Greece, Hungary, Latvia, Lithuania, Malta, Poland, Portugal, Romania, Slovakia and Slovenia). Funds are allocated under two broad categories: (i) trans-European transport networks, notably priority projects of European interest as identified by the EU and (ii) environment, for projects related to energy or transport, that clearly benefit the environment in areas such as energy efficiency, use of renewable energy, developing rail transport, supporting inter-modality and strengthening public transport.

Within the CF, an amount of EUR 11.3bn has been ring-fenced as the Connecting Europe Facility (CEF) to co-fund transport sector projects in CF-eligible Member States. CEF funds, with a total budget of EUR 26.25bn, provide support to infrastructure projects that are intended to fill the gaps in energy, transport and information and communication technology (ICT) networks across EU Member States. CEF funds can be deployed to cover project preparation studies as well as project construction costs. CEF provides its support predominantly as grants (and also through supporting Financial Instruments to mobilise private finance). CEF is governed by its own specific set of regulations and procedures.⁸ This guidance note does not cover blending issues for CEF grants. Guidance for potential CEF beneficiaries is being developed by the Innovation and Networks Executive Agency (INEA) of the Commission and is expected to be published shortly.

In accessing ESI Funds (and other EU funds) the issue of eligibility is very important - the ESI Funds are managed according to strict rules to ensure that they are used in line with their agreed purpose and that the money is spent in a transparent and accountable manner.

⁸ Regulation (EU) 1316/2013 of 11 December 2013.

2.3 Some key terms and principles

It is useful to understand a number of terms and principles relevant to blending and the use of ESI Funds:

Co-financing of ESI Funds and national funds - this is a key principle designed to help ensure Member States ownership of EU grant funded activities. A 'co-financing' rate is a maximum fixed percentage of 'eligible costs' that can be funded by the relevant EU grant. These rates are fixed in the OP in accordance with the different Fund-specific rules.⁹ In any event, grants have an absolute limit which may not exceed the value of 'eligible costs'.¹⁰ Grants cannot be awarded retroactively for an activity that has already been completed.¹¹

Excessive profit principle - fundamental to the objective of EU grant funding is the avoidance of creating excessive profits for the beneficiary. A balance needs to be struck between ensuring financial sustainability through the provision of the grant while at the same time ensuring that the costs of delivering the policy remain reasonable.

Funding versus financing - it is important to distinguish between the terms 'funding' and 'financing', although these are often used quite loosely. This is especially important in the case of Blending Projects which combine funding and financing resources. In this guidance note, 'funding' refers to a non-recoverable financial resource (e.g. a grant) which generally does not need to be paid back to the provider if it is used in accordance with its terms. On the other hand, 'financing' refers to a potentially recoverable financial resource, i.e. one that needs to be paid back to the provider (e.g. loans or equity from the public or private sector).

Shared management - while ultimate responsibility for implementing the EU budget lies with the Commission, some 76% of the budget is spent under what is known as 'shared management'. Under this arrangement, budget implementation is delegated to EU countries to distribute funds and manage expenditure.¹² Grants from ESI Funds are usually administered under shared management. Some EU grants are managed directly by the Commission in relation to the implementation of EU policy. This for example is the case for CEF, with funding decisions taken centrally by the Directorate-General for Mobility and Transport (DG MOVE) of the Commission with the assistance of INEA – this is referred to as '*centralised management*'.

2.4 Partnership Agreements and Operational Programmes

In keeping with the approach of 'shared management', Member States draw up and implement strategic plans with investment priorities covering the five ESI Funds.

⁹ See CPR, Article 60. Supplementary rules on costs' eligibility are also provided in and tailored to individual Operational Programmes (OPs). See [the list of the OPs financed by ERDF and/or by the Cohesion Fund officially adopted by the Commission](#).

¹⁰ See Financial Regulation (FR), Article 126.

¹¹ See FR, Article 130.

¹² See: ec.europa.eu/budget/explained/management/managt_who/who_en.cfm.

These Partnership Agreements (PAs) are negotiated between the Commission and national authorities, following consultation at various levels. These include interest groups, civil society and local and regional representatives.

The Commission also works with the Member States as they draw up their Operational Programmes (OPs) that break down the investment priorities and objectives of the PAs into more detailed concrete actions. These OPs can cover entire Member States and/or regions or they can be cooperation programmes involving more than one country. The Commission negotiates with the national and regional authorities on their final content. The OPs are then implemented by the Member States and their regions. While PAs are meant to remain fixed for the period of the programming period, OPs may be reviewed and revised during the course of the period.

2.5 Managing Authorities

Member States are responsible for managing the OPs and the constituent programmes that are supported by ESI Funds. This work is organised by Managing Authorities in each country and/or region under the principle of shared management and subsidiarity.¹³ A Managing Authority is a public body or bodies designated by the Member State to manage a programme – typically it would be a ministry responsible in the Member State for activities most closely related to the particular programme.

A Managing Authority provides information on the programme to the Commission, and, crucially, selects projects and monitors their implementation. Not all individual projects are therefore selected in advance of the seven-year programming period, but are selected throughout the period by the Managing Authorities in line with the agreed OP. The Commission commits the funds (to allow the countries to start spending on their programmes), monitors implementation of programmes and eventually pays the certified expenditure to each country on the basis of the reports provided by the Managing Authorities.

The rules in the current programming period require a stronger focus than previously on results that are to be measured, monitored and published throughout the programming period.

2.6 Allocating grants

The allocation of grants takes place in line with the agreed OPs. Unless an allocation is set aside specifically for a Major Project already identified in an OP, this is conducted through a call for proposals by the relevant Managing Authority. For more details on Major Projects, see Chapter 9.

¹³ The principle of subsidiarity determines whether the EU can intervene or should let the Member States take action. The EU may intervene in areas which do not fall within its exclusive competence only insofar as the objectives of the intended action cannot be sufficiently achieved by the Member States but can rather, by reason of the scale or effects of the proposed action, be better achieved at Union level. This principle is established in Article 5 of the Treaty on the EU.

If a grant is allocated as a result of a call for proposals,¹⁴ the call will specify the selection and award criteria, the deadline for submitting applications and for applicants to receive information on the outcome of the evaluation of their proposals. The call will also specify the indicative date for signature of the grant agreement or notification of the grant Decision.¹⁵ However, this approach may not be relevant for many Blended Projects which, due to their size, can be expected to be treated as Major Projects.

¹⁴ As per FR, Article 131 (2), normally applications for grants are to be submitted by legal persons as applications by natural persons are only allowed when required by the nature or characteristics of the action.

¹⁵ See FR, Articles 128 (1) and (2).

3 The concept of blending in PPPs

This Chapter describes the rationale for blending and, conceptually, the different ways in which it is possible to blend grants from ESI Funds with national funding and private finance sources in a PPP structure. This Chapter also examines some lessons drawn from past programming periods.

3.1 Rationale for blending

From a [Managing Authority's perspective](#), when appropriately used, PPPs can improve VfM in the use of EU funds, by bringing PPP disciplines to bear.¹⁶ These disciplines might include:

- improved project delivery to time and budget due to payments being based on performance (outputs) rather than inputs;
- a long-term life-cycle approach to project cost assessment and delivery, leading to better designed and constructed assets and lower overall costs;
- improved project preparation, management and implementation;
- innovation in asset and service delivery;
- efficiencies in risk allocation; and
- third party investor/lender scrutiny of projects.

Thus, a PPP as a procurement tool for a project that involves the use of ESI Funds can help to improve the long-term quality of expenditure and effective use of such funds.

From the [perspective of a procuring authority](#) seeking to deliver a project as a PPP, the use of ESI Funds can strengthen PPP delivery by:

- reducing the quantum of national funding resources that may be required to pay for the project either as up-front capital payments or in availability payments;
- reducing the level of financing that needs to be raised;
- reducing the level of user charges; and
- improving the overall structure of the PPP by supporting components of the project that may not be amenable to private sector financing.

By blending ESI Funds in a PPP structure, the public sector can therefore make a project more affordable for the procuring authority and/or for users. At the same time, blending may improve the bankability of the project as a result of lowering the financing levels required and/or risks of the PPP.

¹⁶ See [PPP Motivations and Challenges for the Public Sector](#), EPEC Report, October 2015.

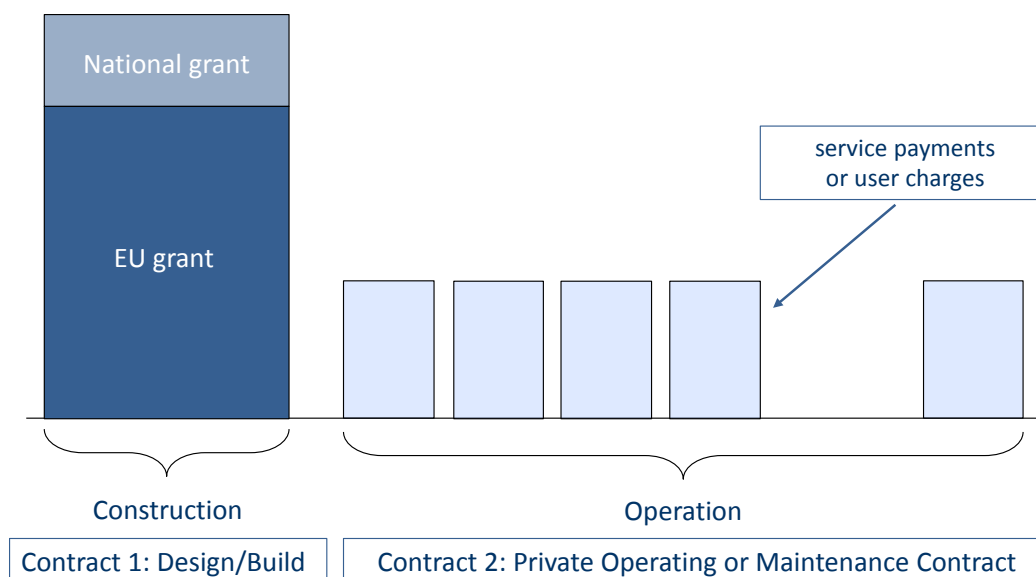
In order to understand blending approaches and the context for the new regulations, it is useful to look at the different approaches that have been used to date and the limitations that have been faced. This is examined in the following two sections.

3.2 Blended structures and their limitations under the previous regulations

The previous EU funding regulations did not include any PPP-specific provisions. Nevertheless, Blended Projects have been (and can continue to be) structured broadly in a number of ways.^{17,18,19} It is important to understand that these structures were fundamentally tailored to work with grant approval and disbursement mechanisms that had been created for conventional forms of procurement (i.e. paying only for upfront capital expenditure costs as and when such costs are incurred). These mechanisms are less suited to PPPs, which often seek to pay for service outputs if and when they are delivered over the longer-term operational phase of a project.

The following are potential examples, presented in increasing levels of complexity, of structures that seek to combine grants with private finance. Each example illustrates the particular limitations of the structure in a PPP context.

EU grant as a contribution to the capital costs in a construction-only contract. This involves separate contracts with private sector companies for the construction of the project asset and the operation of the asset.



This is the simplest structure from a grant perspective with no private financing for construction and limited risk transfer to private sector lenders/investors. Operating

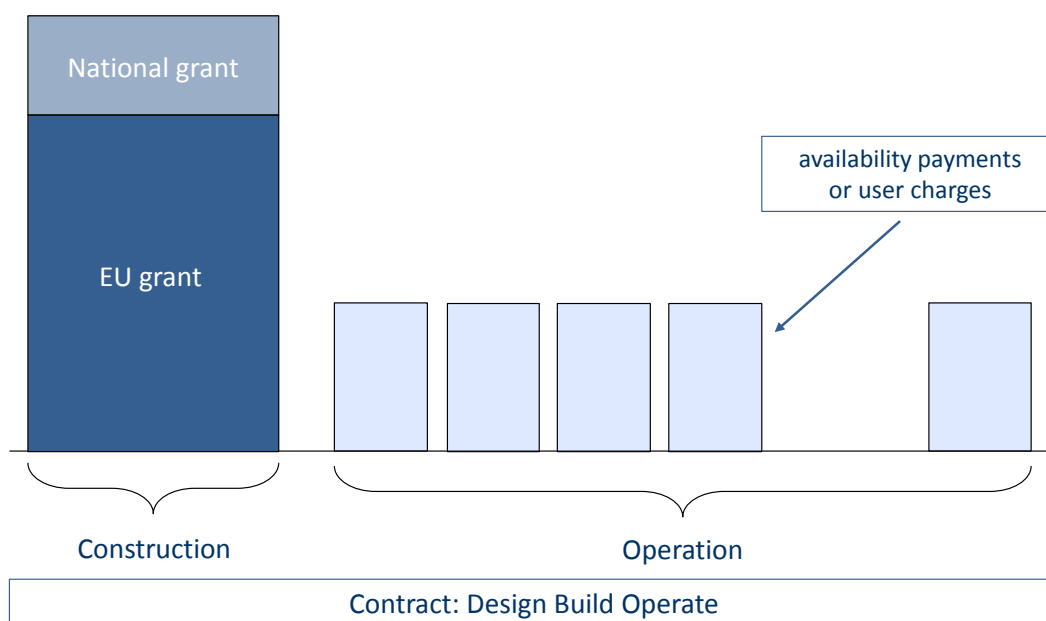
¹⁷ See '[Using EU Funds in PPPs - explaining the how and starting the discussion on the future](#)', EPEC report, May 2011, pp. 13-14.

¹⁸ See '[Combining EU Grant Funding with PPP for Infrastructure: Conceptual Models and Case Examples](#)', JASPERS Horizontal Task Outputs – Working Paper, December 2010, pp. 38-66.

¹⁹ See '[Public-Private Partnerships and Structural Funds](#)', Presentation by Brendan Smyth, DG REGIO, 2013.

and maintenance payments to the private sector are shown by the pale blue blocks in the diagramme. These payments do not include any element of capital repayment. Thus, although the private sector is involved in long-term operation and maintenance, this structure is hardly a PPP as it has very few, if any, PPP features and benefits: for example, the design and construction of the asset and its operation and maintenance are separately contracted. Furthermore, there is no private sector capital involved that is at risk to long-term performance. Potential interface problems between the separate contractor and operator may arise and appropriate coordination of the timing of the procurement processes for the two separate contracts may also be problematic.

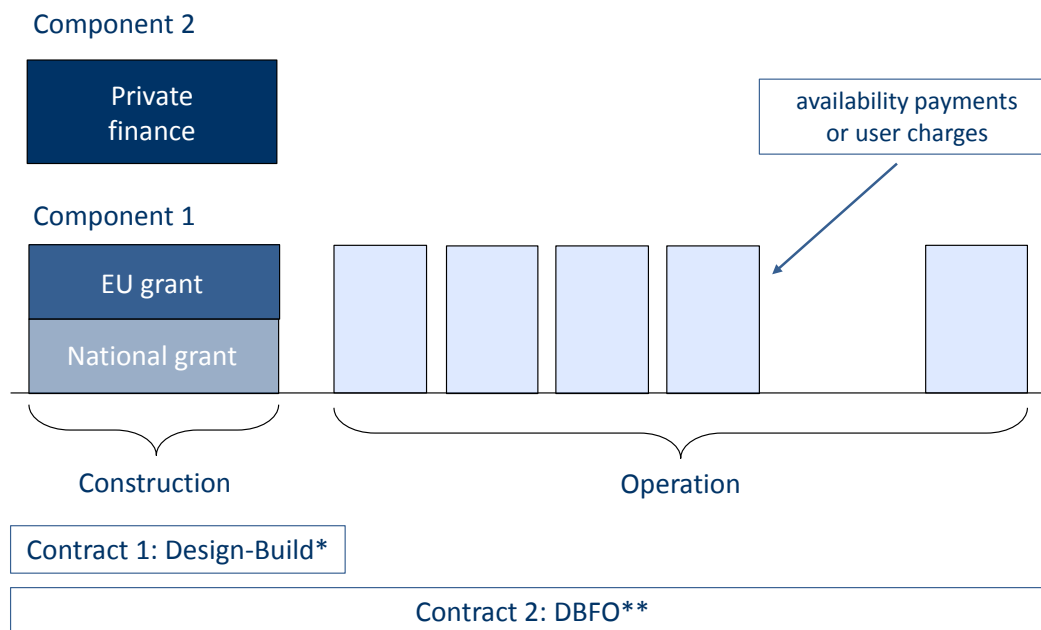
EU grant as a contribution to the capital costs based on a single contract covering construction and operation with the private partner responsible for the design, build and operate (DBO) functions but not for the provision of financing.



This structure potentially involves fewer interface risks as a single contract commits the private partner both to the design and construction of the asset and its subsequent operation and maintenance. Payments to the private sector during the operating phase cover operating and maintenance costs only and do not include any element of capital repayment: as the construction is fully publicly-funded, private finance is not at risk to long-term performance, a core feature of PPPs.

Parallel funding and financing of capital expenditure based on two separate contracts. This comprises two components: a design and build contract (contract 1) funded by national and EU funds for infrastructure component 1; and a design, build finance and operate (DBFO) contract (contract 2) financed by the private sector for infrastructure component 2. Contract 2 also covers the operation of infrastructure component 1 funded by national and EU funds (an example could be the design, construction, operation and financing of a hospital building by a private partner and the design and construction only of a separate maternity unit building on the hospital

campus funded by national and grant resources but subsequently maintained by the private partner).

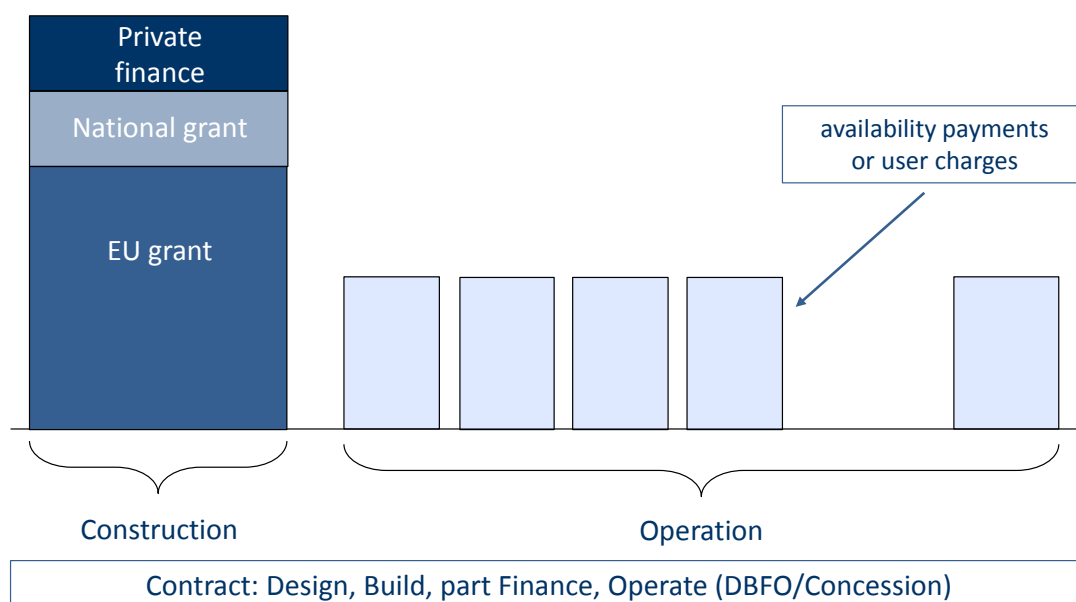


* Design and Build of Component 1

** Design and Build of Component 2 and Operation of Component 1 and 2

The split into two contracts makes the grant structuring easier as the grant application only needs to be filed for contract 1. At the same time it also allows for a higher risk transfer to the private partner (as private finance is now at risk to performance in contract 2). However, this structure is more complicated than the previous structures outlined, not least because it involves handling (i) two distinct contracts of different natures and (ii) potentially, two procurement and construction processes carried out at the same time (although the two contracts might be let to the same contractor to help mitigate potential problems). The structure may also give rise to considerable interface risks between the two components.

Funding of part of the capital expenditure on the basis of a single design, build, finance and operate contract



This structure, where EU grants are used to fund part of the capital expenditure, allows for leveraging in private finance and higher risk transfer to the private partner. However, this model is still constrained by limiting the use of grant funding to the costs over the construction period only, as in the other structures outlined above (i.e. no use of EU grants during the operational phase or, in case of delays, beyond the eligibility period). This might not be so constraining if the level of national and grant funding compared to the level of private financing is quite small, enabling enough private sector finance to be exposed to long-term performance. However, coordinating the management and timing of a PPP process and an EU grant application may also be challenging, as described in more detail in Chapter 6.

In summary, all of these approaches have a drawback in limiting risk allocation to the private sector more than might otherwise have been the case for a PPP that does not involve blending (although in the last example this constraint may be less if the relative amount of the grant is quite small). Fundamentally, in the previous programming period (2007-2013), EU grant funding was designed to pay for project *inputs*, in line with traditional procurement approaches. The essence of a PPP on the other hand is a procurement approach based on the payment for *outputs*. If the EU grant component of the project is substantial, this limits one of the fundamental benefits of the PPP structure because the level of private finance that is exposed to long-term performance may either be non-existent or less than optimal, thereby questioning the rationale of using a PPP structure in the first place.

3.3 Past blending activity and implementation issues

In its blending stock-take carried out in 2012, EPEC identified close to 50 Blended Projects²⁰ across 13 countries that involved the use of grants secured from European structural funds or cohesion funds under programming periods from 1994-99 to 2007-2013. The projects were split 50/50 between minor and Major Projects suggesting that there may be little correlation between the use of blending and the size of a project. By value, transport projects dominated but by number, ICT projects were the most common. France, Slovenia and Greece were the largest users by number. This activity however compares with over 1 500 PPP projects where no blending was used, worth over EUR 279bn, over an equivalent time period.

In addition to the risk transfer limitations mentioned above, EPEC also identified a number of implementation issues that were likely to explain the relatively low use of blending. These included:

- Lack of flexibility in the grant procedures in terms of the required timing and disbursement of the grant element, such that the PPP had to be designed around the grant application process rather than the other way round or together;
- The requirement that revenue-generating projects required some level of national funding to enable access to the EU grant;
- The risk of clawback of the grant in the event of substantial change in tariff policy applied, leading to the revenue stream being different in the future; and
- The difficulties and uncertainties of not knowing the level of grant or ‘*funding gap*’ required to be met until the PPP procurement results were known, which would mean the procuring authority having to bear the funding risk in case the grant amount turned out to be less than expected.

Overall, however, limited public sector capacity to deliver complex structures was one of the most important barriers to the development of Blended Projects together with a perception that Blended Projects would not be accepted by Managing Authorities or the Commission.

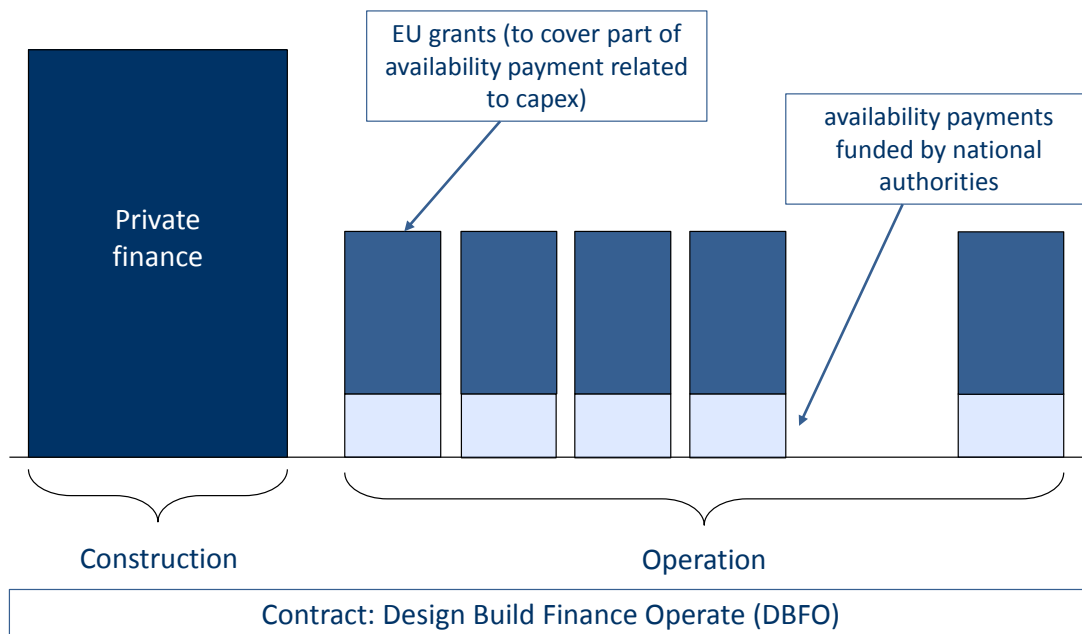
3.4 Impact of the new regulations

The regulations for the current programming period have recognised a number of the important shortcomings and seek to address them. They also enable Blended Projects to take place with payment structures more typical of PPPs.

To compare with the previous structures outlined above, one of the key changes has been to provide the option for EU grants to co-fund payments of eligible capital costs but in a way that payment to the private partner can be made over the operational period of the project (even if this extends beyond the current programming period).

²⁰ Projects included were those that involved (i) the construction of the physical assets by the private partner (i.e. projects where the private partner was only the operator were excluded), (ii) approval of the grant by DG REGIO or relevant Managing Authority and (iii) a private sector financing component.

Thus, the opportunity for risk transfer incentives and benefits of the PPP can be better preserved.



The following Chapters provide greater detail of the basis upon which this structure can be implemented and the wider range of options available to implement Blended Projects under the new regulations.

4 Legal and administrative framework for Blended Projects

This Chapter sets out the broad legal and administrative framework for blending grants under ESI Funds with PPPs and identifies some of the main issues related to implementing Blended Projects.

4.1 Common Provisions Regulation on ESI Funds

The CPR sets out the framework for shared management between the Commission and each Member State with respect to the funding available from the various ESI Funds.²¹

By setting out a series of common rules for the use of ESI Funds, the intention is to simplify policy delivery. The CPR contains important provisions on revenue-generating operations, Major Projects, co-financing rates and the duration of operations that can be supported by ESI Funds.²² These are explored in more detail in subsequent Chapters of this guidance note.

The new stand-alone chapter on PPPs focuses on operational aspects of the allocation and disbursement of ESI Funds to PPP projects. The direct reference to PPPs in the context of EU regional policy shows that blending public and private financial resources is considered an important way of leveraging EU funds and achieving EU policy objectives. As reflected in the recitals to the CPR: *'Public Private Partnerships ("PPPs") can be an effective means of delivering operations which ensure the achievement of public policy objectives by bringing together different forms of public and private resources. In order to facilitate the use of ESI Funds to support operations structured as PPPs, this Regulation should take account of certain characteristics specific to PPPs by adapting some of the common provisions on the ESI Funds'*.²³

Building on past blending experience, the new PPP-specific provisions of the CPR seek to put PPP projects on the same level as traditionally procured projects in securing support from ESI Funds.

The CPR also provides a definition of PPPs that is broad and refers to some basic features of PPPs, namely as a form of cooperation between the public and private sector for the delivery of public services. Since ESI Funds are about investment, it is not surprising that the definition also introduces a concept of investment in infrastructure – hence excluding arrangements with the private sector that only involve a service element (for instance ICT maintenance contracts with no capital investment). However, the definition is not prescriptive as to the type of contractual

²¹ Measures under shared management in Title V of the FR, as such term is defined in the 2nd preamble of the CPR.

²² See CPR, Articles 60 (Determination of co-financing rates), 61 (Operations generating net revenue after completion), 71 (Durability of operations) and 100-103 (Major Projects).

²³ See CPR, recital 59.

arrangements, payment mechanisms, financing schemes or risk-sharing agreements required to fall under the definition:

'Public private partnerships' (PPPs) means forms of cooperation between public bodies and the private sector, which aim to improve the delivery of investments in infrastructure projects or other types of operations, delivering public services through risk sharing, pooling of private sector expertise or additional sources of capital'.²⁴

4.2 Relevant delegated acts

The CPR introduces subsidiary regulations in the form of delegated and implementing acts, and implementation guidance.²⁵ These are used to supplement the CPR in defined areas. A number of these are relevant to PPPs:

- [Commission Delegated Regulation \(EU\) No 480/2014 of 3 March 2014](#) concerning the calculation of discounted net revenue for revenue-generating projects (referred to in this guidance note as the 'RGDR');²⁶
- [Commission Delegated Regulation \(EU\) No 2015/1076 of 28 April 2015](#) concerning the replacement of a beneficiary and minimum requirements to be included in PPP agreements regarding escrow accounts and reporting and audit trail (referred to in this guidance note as the 'PPP DR');²⁷
- [Commission Implementing Regulation \(EU\) 2015/207 of 20 January 2015](#) concerning the information required on Major Projects²⁸ and the methodology to be used for performing a cost-benefit analysis²⁹ (referred to in this guidance note as the 'CBA IR'); and
- [Implementation Guidance 2014-2020 Version 2 of 24 March 2014](#) concerning methods for calculating the EU grant amounts for revenue-generating projects (referred to in this guidance note as the 'Implementation Guidance').

4.3 State aid issues in the context of EU-supported PPP projects

EU funds that are implemented under shared management (such as ESI Funds) and flow through national budgets are subject to state aid rules. These rules examine issues such as the market conformity of the investment or its compatibility under state aid guidelines/regulations. The Member State remains responsible for ensuring compliance with these rules, and if necessary, the notification of any state aid to the

²⁴ See CPR, Article 2, paragraph 26.

²⁵ Delegated and implementing acts are two types of instrument the Commission may adopt in order to ensure the implementation of EU law. Delegated acts are defined as non-legislative acts of general application to supplement or amend certain non-essential elements of a legislative act. They represent an explicit decision by the EU legislators to grant the Commission power to act on a certain issue. The extent of the delegation has to be clearly determined in the original legislation. An implementing act on the other hand is inherently more procedural (templates, procedures, deadlines) providing guidance on the practical implementation of rules that already exist in the original legislation.

²⁶ See CPR, Section II, Title VII, Chapter I, Article 61 (3). See also the Implementation Guidance, page 4.

²⁷ See CPR Section II, Title VII, Chapter I, Articles 63 (4) and 64 (4).

²⁸ See CPR, Part three, Title II, Chapter II, Article 101.

²⁹ See CPR, Part three, Title II, Chapter II, Article 100.

Commission's competition services. Given that national Managing Authorities are involved in the selection of projects and administration of grants from ESI Funds, Blended Projects can therefore be expected to be subject to state aid rules.

It should be noted that direct funding from the EU under direct management (e.g. funding obtained under the CEF) as well as funding from the EIB, do not qualify as state aid. Therefore substantive and procedural requirements, such as notification, monitoring or reporting of the state aid rules do not apply. It should be emphasised that this is only when the project or programme consists exclusively of EU resources without the involvement of any resources from, or under the control of, Member States.

Determination of state aid is a complex area and is referred to in this guidance note only to highlight that blending will usually give rise to state aid issues and that these issues should be carefully assessed when preparing Blended Projects.

4.4 Eurostat issues in the context of EU-supported projects

Blended Projects benefiting from EU funds may require special consideration as to their statistical treatment for the purposes of Maastricht deficit and debt classification. In general, Eurostat rules consider financing and funding support from any government entity (be it on a central, regional or local basis), whether through loans, grants or guarantees, as one of the factors for the assessment of the statistical treatment of a PPP project.³⁰ Any Blended Project with government contributions, or benefiting from government guarantees (or from a combination of both), for a value of more than 50% of the investment (capital) costs of a project needs to be reported on the Government's balance sheet.

The [Eurostat Manual on Government Deficit and Debt](#)³¹ specifies that EU co-funding by way of grants, however, is neutral for statistical classification of PPPs and concessions (under Eurostat, there is a distinction between government-pay PPPs which are referred to as 'PPP's' and user-pay PPPs which are referred to as 'concessions'). So, the amount of an EU grant contributed to a Blended Project does not add to the volume of government support taken into account for the analysis. The rationale put forward is based on the fact that the EU funding is granted from the Commission as an international institution and as a result does not count as support from the national government. Consequently, EU funding contributions to Blended Projects are not considered a source of government funding that has an impact on the classification of 'PPP's' and 'concessions' (under Eurostat definitions) and their inclusion on the Government's balance sheet.

However, if a Government provides a grant to cover capital expenditure for a Blended Project which is subsequently reimbursed by the EU, EU funding would be

³⁰ In its Manual on Government Deficit and Debt - Implementation of ESA 2010 -2014 edition, Eurostat defines PPPs as '*long-term contracts in which government is paying to a partner all or a majority of the fees under a contractual arrangement, thus covering most of the total cost of the service (including the amortisation of the assets)*'. On the subject of the statistical treatment of PPPs, see also EPEC publications: '[Eurostat Treatment of Public-Private Partnerships: Purposes, methodology and recent trends](#)' and '[Risk Distribution and Balance Sheet Treatment – Practical Guide](#)'.

³¹ See [Manual on Government Deficit and Debt - Implementation of ESA 2010-2014 edition, Chapter VI.4](#).

counted as a national government contribution towards a project. In such cases, the amount of EU funding covering the government expenditure in the project would need to be taken into account when assessing the cumulative government support to a Blended Project.

4.5 Issues related to the procurement of PPPs

A prerequisite of all projects funded by the EU, and therefore Blended Projects, is that they comply with the public procurement rules of the EU. In the case of PPPs, the most relevant Directives are the recently reformed [Public Procurement Directive](#) (2014/24/EU) and the newly created [Concessions Directive](#) (2014/23/EU). These are required to be transposed into Members States' respective national laws by 18 April 2016.

The Directives set out the various rules and regulations governing procurement by public authorities over specified thresholds to ensure that the process is conducted and bids evaluated in an open, fair and transparent manner. Unlike the issues with state aid, there are no specific procurement issues introduced by using ESI Funds that go beyond this overriding principle. In line with the issues raised in the rest of this guidance note, procuring authorities may, for example, wish to consider how potential uncertainties around the timing of confirmation of funding or change of beneficiary are managed in a way that does not affect their ability to run a procurement process in an open, fair and transparent way.

5 PPP-specific provisions of the CPR

The CPR has introduced special rules on the way ESI Funds may be used to support PPPs. These address some of the difficulties that previously existed, including issues around changes to the beneficiary of the grant, the timing of grant approvals and the eligibility of expenditure over the lifetime of the PPP contract.

This Chapter covers each of these key areas of the CPR. Another area of improvement involves the determination of the level of the grant, especially for revenue-generating projects, although this is not PPP-specific. Determining grant levels for revenue-generating projects is covered separately in Chapter 7.

5.1 Beneficiary of ESI Funds for Blended Projects

5.1.1 Who can be the beneficiary of a grant using ESI Funds?

While the initiator of a Blended Project would be a public body, the provisions of the CPR establish that:

'in relation to a PPP operation,³² and by way of derogation from point (10) of Article 2, the beneficiary may be either:

- (a) *the public law body initiating the operation; or*
- (b) *a body governed by private law of a Member State³³ (the 'private partner') selected or to be selected for the implementation of the operation.'³⁴*

The procuring authority therefore has a choice as to whether it will be the beneficiary and remain so throughout the project life or whether the private partner will be the beneficiary.

5.1.2 Procuring authority as beneficiary

The decision for the procuring authority to be the grant beneficiary will be governed by the extent to which it wishes to retain control over payment of the grant proceeds to the private partner (for example in the case of a government-pay PPP) and implement the 'no service, no pay principle' in relation to the deployment of the grant.

To help mitigate any risk for the procuring authority that the grant is not available to meet payment obligations towards the private partner, financial close can take place when the grant approval is in place. Equally, any risks associated with the timely

³² See 'old' Council Regulation (EC) No 1083/2006: although there was no definition of 'operation', it is understood to refer to the infrastructure project to be constructed by the private partner under the PPP contract. The new CPR provides for a definition of 'operation' in Article 2(9), where it is stated that "*operation*" means a project, contract, action or group of projects selected by the Managing Authorities of the programmes concerned, or under their responsibility, that contributes to the objectives of a priority or priorities'.

³³ The reference to 'a body governed by private law of a Member State' appears to exclude non-EU private law bodies.

³⁴ See CPR, Article 63.

disbursement of the grant could also be mitigated by including provisions in the PPP agreement to cover the private partner's obligations that might cause a delay.

It is also important for the procuring authority to recognise that it will rely on the private partner to provide much of the information required for reporting and grant disbursements. In this case, it would be advisable for the PPP agreement to mirror the beneficiary reporting obligations under the grant agreement. This would help to ensure the private partner provides the required information under the grant agreement in a timely manner.

5.1.3 Conditions for the private partner to be the beneficiary

The private partner can only be a beneficiary if this is proposed by the procuring authority initiating the project.³⁵ Furthermore, the approval Decision for the grant is conditional on the Managing Authority satisfying itself that the selected private partner 'fulfils and assumes all the corresponding obligations of a beneficiary under the Regulation'.³⁶

It is reasonable that in the context of a conditional grant approval (see section 5.1.5) where the private partner, once selected, will then be the beneficiary, the private partner is required to confirm its willingness to be the beneficiary of the grant. This also implies that the private partner must agree to undertake the corresponding obligations and responsibilities that come with being the beneficiary of the grant (e.g. payment requests, proof of eligible expenditure, regular reporting).

To help ensure acceptance by the private partner of the obligations required of a beneficiary, measures could include: market testing on acceptability of the obligations, disclosure to the bidders of such obligations in the procurement documentation (together with early involvement of the Managing Authority to prepare the required documentation prior to launching the procurement phase).

It is also a condition of bidders pre-qualifying for the PPP procurement that they will accept these obligations – it would be unfortunate to select a bidder who then refused to accept the conditions of a beneficiary.

Equally, to help ensure that the private partner will be acceptable to the Managing Authority, the Managing Authority should be kept informed throughout the selection procedure.

5.1.4 Replacement of the private partner beneficiary

The CPR³⁷ allows for the replacement of the private partner beneficiary. The Commission has further supplemented these provisions through the PPP DR. In reality, replacement of the private partner is most likely to be an exceptional event.

Under these provisions the private partner can be replaced during the implementation of the project when this is (i) required under the terms and conditions

³⁵ See CPR, Article 63 (2).

³⁶ Ibid.

³⁷ See CPR, Article 63.

of the PPP agreement or (ii) provided for in the financing agreement between the private partner and the institution(s) financing the project. The Managing Authority must satisfy itself that the replacement partner (private or public) fulfils and assumes all the corresponding obligations of the previous beneficiary.^{38 39}

These provisions are particularly relevant for the financing of PPPs as they preserve lenders' step-in and substitution rights without the risk of loss of the grant.

The PPP DR specifies additional conditions that must be met by the replacing partner, that:

- it is able to provide at least the service, including at the minimum quality standards, determined in the (original) PPP agreement;
- it agrees to assume the rights and responsibilities of a beneficiary in relation to the grant, from the date of notification of the replacement proposal to the Managing Authority;
- the replacement right already exists under the PPP agreement or financing documentation; and
- the replacing partner is aware of the terms and conditions of the grant by having been provided with a copy of the original grant agreement (and any amendments made to it).

The PPP DR also requires that the Managing Authority must receive the proposal to replace the private partner as beneficiary within one month of the decision to replace it.⁴⁰ The proposal must contain:

- the terms and conditions of the relevant PPP or financing agreement;
- evidence that it fulfils the conditions set out above, together with the obligations of a beneficiary under the CPR; and
- evidence that the replacing partner has been provided with a copy of the original grant support agreement and any amendments to it.

Provided these conditions are met, the Managing Authority is required to register the new partner as the beneficiary as of the date of its being notified of the replacement proposal.

5.1.5 When can a grant Decision be received?

By the use of the words '*the private partner selected or to be selected for the implementation of the operation*', the CPR suggests that (i) a procuring authority with

³⁸ See CPR, Article 63 (3).

³⁹ Article 71 of the CPR on 'Durability of operations' prescribes that grant contributions should be repaid in certain events, such as change in ownership or substantial changes affecting the implementation conditions of an operation. Article 63(5) of the CPR therefore explicitly states that the replacement of the beneficiary under a PPP contract neutralises the potential effect of Article 71(b).

⁴⁰ This may be challenging in practice.

a well-prepared project⁴¹ may now file an application *prior* to having selected the private partner and (ii) that this should not prevent the Managing Authority or the Commission from issuing a *conditional* grant Decision for a beneficiary that is yet to be identified (the possibility of applying for a grant before selecting the private partner beneficiary is also catered for in the Major Projects information form - see Chapter 9).⁴²

Equally, where the beneficiary is likely to be the procuring authority throughout, for example in a government-pay PPP, it can be inferred that the procuring authority can apply for a grant and obtain a grant approval before awarding the PPP contract (as in this case the beneficiary is not changing).

It is important to highlight these options as, based on previous experience, there may still exist a perception by some Managing Authorities that the grant application can only be processed once the PPP procurement process has been completed and all facts are known, including the identity of the private partner.

Securing a grant Decision before concluding the PPP agreement

Securing a grant Decision before concluding the PPP agreement can have the following benefits:

- avoiding the risk for the procuring authority with regard to the level/availability of the grant once it has entered into a PPP commitment (and therefore avoiding the need to backstop the grant amount);
- potentially reducing the overall length of the blending process by allowing for the time required to prepare and process the grant application to run in parallel (to a great extent) with the PPP preparation/procurement phases;
- allowing bidders to understand up-front the sources of all funds/financing to plan their bids; and
- reducing the risk of a challenge to the bid decision by losing bidders as the grant availability and conditions are clear up-front.

Assuming the grant application is submitted at the end of the project preparation phase, there may be options as to when to plan to receive the conditional grant application in relation to the PPP procurement process: e.g. (i) just prior to, or at the commencement of, the procurement phase with the advantage of clarity for bidders on all funding sources from an early stage. On the other hand, if time is of the essence, the procuring authority may decide to commence the early stages of the procurement process (e.g. pre-qualification) and allow the grant approval process to take place in parallel. The choice will depend on, among other things, the expected level of bidder interest, the procuring authority's capacity to run parallel processes, the flexibility of the project delivery timetable and expected grant approval times.

⁴¹ While the provisions indicate that an application could be filed for a private partner to be identified, this application remains subject to the general provisions of the CPR, which requires a high level of preparation of the project in order to have the information required to file a grant application.

⁴² See [Commission Implementing Regulation \(EU\) 2015/207 of 20 January 2015](#).

The timing of the procurement process will be dependent on the grant approval process and there may be a risk that the grant amount applied for is insufficient in light of the actual PPP bids received. This highlights the importance of good project preparation to minimise any delays in the grant approval process and in ensuring that the expected project funding and financing estimates are sound: often, the delay in grant approvals is caused by requests for further information as a result of poor project preparation, rather than the grant application and Decision process itself.

Securing a grant Decision after concluding the PPP agreement

The procuring authority may, however, decide to secure the grant Decision after concluding the PPP agreement. Drivers for this option might include:

- allowing for some greater flexibility with the PPP project implementation timetable by de-linking the grant process from the procurement process;
- potentially simplifying the overall project process as the PPP and grant application processes take place separately, not at the same time; and
- providing certainty at the start of the grant application process on the amount of grant funding to apply for, so avoiding the risk of having to re-apply for a higher or lower grant amount.

The significant downside of this option for the procuring authority however is exposure to the risk that the grant amount is not approved or approved for a reduced amount, having already entered into a PPP commitment. The procuring authority is then committed to funding those amounts from its own resources that might otherwise have been funded by the grant.

5.2 Eligibility of project expenditure in Blended Projects

5.2.1 When expenditure is considered eligible

The rules on eligibility of expenditure are established nationally except where specific rules are laid down in the CPR or the specific fund regulations.⁴³ The CPR specifies that expenditure eligible for ESI Fund support must have been incurred and paid before 31 December 2023. The CPR also contains 'de-commitment' provisions whereby the Commission may 'de-commit' amounts (i.e. remove their availability) under OPs where payment of the grant does not take place by 31 December in the third financial year following the year of the budgeted commitment (referred to as the 'N+3 rule').⁴⁴ One of the anchor principles of government-pay PPPs however is that payment by the procuring authority to the private partner is dependent on delivery of

⁴³ See CPR, Article 65(1).

⁴⁴ See CPR, Article 136(1). The N+3 rule relates to funding rules for the annual allocation of money from the European Union's Structural and Cohesion Funds. This applies at the level of programmes and funds, but not at the level of individual projects. If the funding in question has not been spent by that date, the Commission can 'de-commit' future budget allocations. Automatic de-commitments are made if funding is not spent, or requests for payments are not made, by the end of the third calendar year following ('N+3') - see CPR, Article 136. This deadline was two years (N+2) in the previous programming period. A similar rule is found in Article 102(3) regarding Major Projects where, in the case of a PPP, the PPP contract needs to be signed within three years of the approval Decision. National legislations governing grants tend to mirror this 'use or lose' principle.

the required level of service over the whole contract period: the ‘no service, no fee’ principle.⁴⁵

5.2.2 Escrow account

The CPR contains specific provisions to accommodate the use of grants from ESI Funds for a project over an extended payment period. This could be as long as the operating period of a PPP. It avoids the need to front-load payment to [the private partner](#) of the grant contribution to a project in order to comply with the N+3 rule and the final cut-off date of 31 December 2023. The solution is effectively to allow ESI Funds to be disbursed into an escrow account controlled by the procuring authority as eligible project expenditure takes place. The escrowed amounts can then be used by the procuring authority to make payments to the private partner in accordance with whatever schedule is agreed in the PPP agreement, even as long as the availability payment schedule. Nevertheless, the request for the grant disbursement into the procuring authority-controlled escrow account still needs to take place as early as possible and on a regular basis in order to reduce the risk of losing funds at the programme level.

For avoidance of doubt, the amount of the grant funding relates to eligible capital expenditure of the project and not to the amount of the availability payments which are bid for and agreed in the PPP agreement. Thus they may fund a significant proportion, but not the totality of any availability payments.

Given that funds will effectively be sitting unused for a period in the escrow account, procuring authorities may choose a shorter-term payment schedule – this is for the procuring authority to decide (e.g. to the extent it may wish to pay only once services are delivered over the term of the PPP agreement) and so long as it is in accordance with the terms in the PPP agreement.

Grant disbursement into the escrow account controlled by the procuring authority must follow the usual grant disbursement rules that are established at national level and the terms of the PPP agreement. Typically, the procuring authority would submit payment claims to the Managing Authority based on actual eligible expenditure by the private partner. The relevant grant amount would then be disbursed into the procuring authority’s escrow account based on such payment claims, instead of directly to the private partner (subsequently the private partner would be paid with the monies in the escrow account in accordance with the PPP agreement, as mentioned above).

In any event, the expenditure of the private partner that triggers grant disbursement to the escrow account must be incurred and paid into the escrow account no later than the cut-off date of 31 December 2023. Also, the underlying asset that is the subject of the PPP must be completed and operational by the time of final closure of the 2014-2020 OP (15 February 2025). If this condition is not met, the grant that has not been used must be paid back to the Commission. In order to avoid this, the Managing Authority might seek to negotiate with the Commission the phasing of the

⁴⁵ See EPEC, [Using EU Funds in PPPs – explaining the how and starting the discussion on the future](#).

Blended Project so that a part of it falls into the new OP for the next programming period. Such an option however has an intrinsic risk due to the uncertainty of the rules for project phasing and of the outcome of such a negotiation.

The CPR provides that in the case of a PPP project⁴⁶ where the procuring authority is the beneficiary of the grant, expenses incurred and paid for by the private partner may be considered as incurred and paid by the procuring authority, subject to the following conditions:⁴⁷

- expenditure may only be deemed incurred and paid by the procuring authority if a PPP agreement has been entered into. The CPR does not define what a ‘PPP agreement’ is, but a reasonable interpretation would point to the long-term contract for the provision of the service whereby the beneficiary has committed to take or pay for the service. In the case of a concession, the PPP agreement would be one under which the beneficiary has received contractual commitments from the private partner to deliver the service in line with the CPR definition of a PPP;
- with regard to monitoring obligations of the Managing Authorities, the CPR⁴⁸ requires that the Managing Authority must ensure that the eligible expense was effectively paid by the private partner and that the operation complies with national and EU legislation and other conditions in support of the project. The control function of the Managing Authority in this case is only an extension of what the Managing Authority is already obliged to do in respect of expenditure directly incurred and paid for by beneficiaries; and
- the grant funding must be segregated from the general funds of the beneficiary and paid into an escrow account specifically set up for that purpose in the name of the procuring authority. The escrowed funds can then be used to make payments as and when required under the PPP agreement, including in the event of termination.⁴⁹

Another benefit of the escrow account arrangement is that it may help to provide some certainty both for the procuring authority and the private party that contracts with it, that funds will be available over the PPP contract period to meet, at least in part, the payment obligations of the procuring authority.

In addition to the CPR, the PPP DR lays down minimum requirements that must be included in the PPP agreement in relation to the establishment and operation of the escrow account. These are:

- where appropriate, the criteria for the selection of the financial institution where the escrow account will be held, including in relation to its creditworthiness;
- the conditions under which payments can be made from the escrow account;

⁴⁶ See CPR, Article 64. This is by derogation to the normal rule found in CPR, Article 65 (2) where the eligible expenditures are defined as those incurred and paid directly by the beneficiary.

⁴⁷ See paragraphs (a) and (b) of Articles 64(1) CPR.

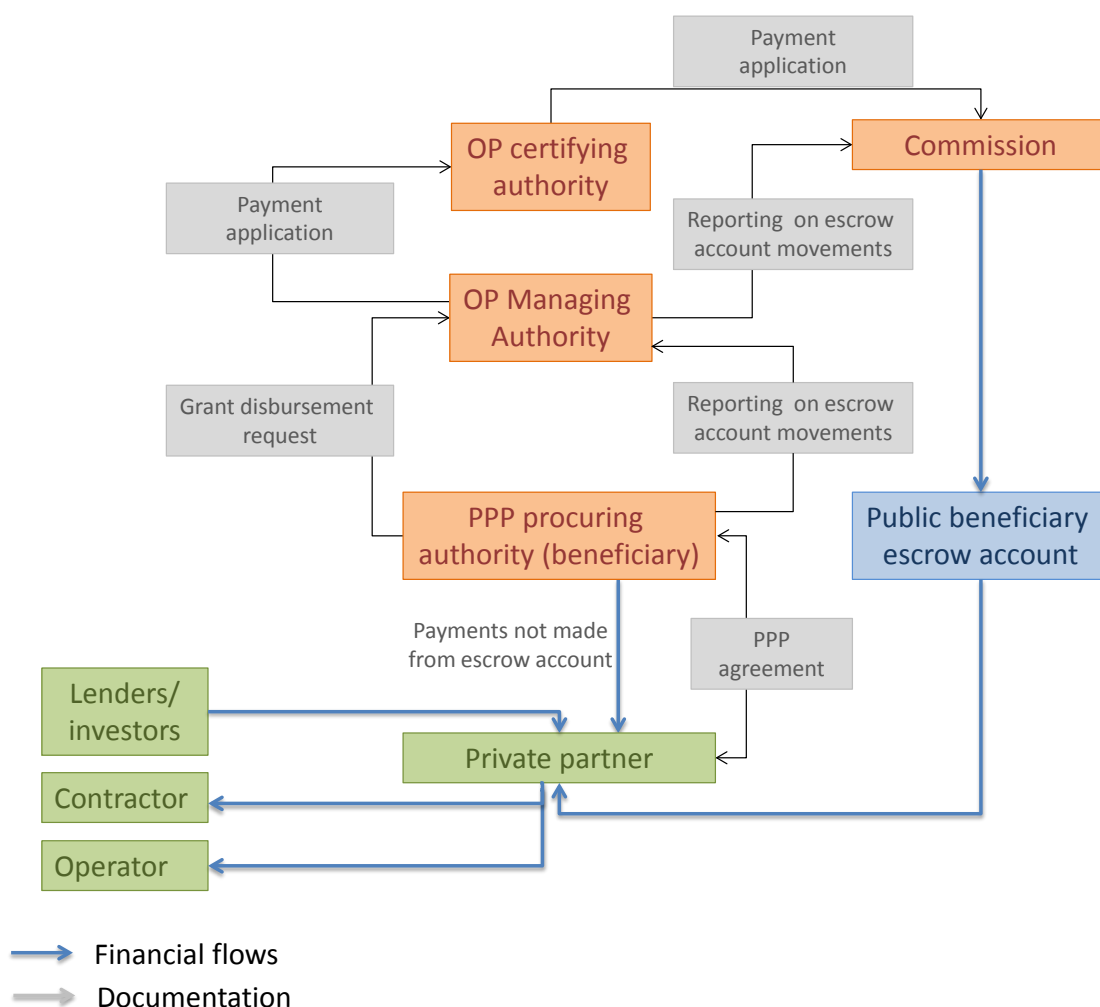
⁴⁸ See CPR, Article 64(1)(b).

⁴⁹ See CPR, Articles 64 (2) and (3).

- whether the procuring authority may use the account as collateral/security for the performance of its own or the private partner's obligations under the PPP agreement;
- the obligation of the procuring authority as holder of the escrow account to inform the Managing Authority, upon its written request, as to the amount of funds that has been disbursed from the escrow account and the balance remaining;
- how the remaining funds in the escrow account are to be disbursed in the event of the account being closed due to termination of the PPP agreement; and
- the PPP agreement must also contain:
 - provisions for establishing a reporting and document retention mechanism which is the same as those of the procuring authority; and
 - procedures to ensure an adequate audit trail in accordance with the requirements of the RGDR⁵⁰, in particular allowing for the payment incurred and paid by the private partner to be reconciled with the expenditure declared by the beneficiary (i.e. the procuring authority) to the Managing Authority.

Although not specifically set out in any detail in the CPR, the flows of payments can be expected to be as follows for a government-pay Blended Project (see Figure 1):

⁵⁰ See RGDR, Article 25

Figure 1 – Schematic of payment flows for government-pay Blended Projects

5.2.3 What type of expenditure is eligible?

Investments supported by grants should also be located in or benefit the area covered by the OP.

Total project costs need to be split into eligible and ineligible costs according to several cost categories in the grant application form.⁵¹ Under certain conditions, contributions in kind, such as the provision of works, goods, services, land and real estate may be eligible.⁵² This may be relevant for a PPP where the public partner provides contributions in kind such as land/real estate or services. Apart from the core investment costs, contingencies and similar items may also be taken into account in the grant application form.

⁵¹ See CBA IR.

⁵² See CPR, Article 69.

There are, however, several cost factors that are considered ineligible according to the CPR.⁵³ These costs include interest on debt and land purchase costs above 10% of total eligible expenditure.

Generally, the payment of value added tax (VAT) is not eligible for ESI Funding, unless the VAT amounts are not recoverable under national VAT legislation.⁵⁴ As a consequence, whether or not the VAT is an eligible expense will significantly depend on national legislation and on the VAT status of the beneficiary (i.e. VAT taxable person or not).⁵⁵ The CPR also provides specific rules on the eligibility of depreciation costs and of contributions in kind.

It should be noted that the grant amount disbursed is based on actual not projected costs. For a government-pay PPP, this means that there is the possibility that the grant amount disbursed into the escrow account may be less than anticipated if the actual eligible costs are less than expected. This may be unlikely but it could have an impact in relation to the amount of grant that the procuring authority might be expecting in relation to the availability payments it will have been committed to under the PPP agreement. Any funding difference that might result would have to be met by the procuring authority. Similar risks to the grant amount actually disbursed may also arise if actual revenues turn out to be greater than expected – this is examined in more detail in Section 7.2.6.

⁵³ See CPR, Article 69 (3).

⁵⁴ See CPR, Article 69 (3)(c), corresponding to Article 126 (3)(c) of the new Financial Regulation (Reg. 966/2012).

⁵⁵ For more details on key issues arising in relation to VAT in the European context, see also '[VAT and PPP contracts. Review of key issues arising in the European context](#)', EPEC Report (in collaboration with Deloitte), July 2013.

6 The PPP project blending cycle

This Chapter sets out the series of steps that might be expected in the preparation and implementation of a Blended Project. This is based on the typical PPP project cycle (as described in more detail in the [EPEC PPP Guide](#)) and CPR. While there is significant experience on which to base the PPP process, as yet there is no experience of combining the PPP project cycle with the grant application process (the 'project blending cycle') under the new regulations.

It is worth noting that a number of the key decisions in relation to the grant application will be driven by the design of the PPP. This underlines the close interaction between the PPP and grant application processes. Equally, many of the early preparation tasks will be the same for both the PPP and grant processes. Procuring authorities and Managing Authorities therefore need to work closely together throughout the blending cycle.

6.1 Importance of sound project preparation in the grant application process

While consideration may be given as to how and when to prepare the grant application, in practice one of the most important factors to consider is the level of preparation of the project itself. This will help ensure that the grant approval process is carried out in a timely manner.

In order to secure a grant from ESI Funds, the investment project needs to be well defined. This includes, amongst other steps, a thorough cost-benefit analysis and justification for the underlying project and a detailed design of the PPP arrangements prior to launching the procurement phase. Procuring authorities that have not invested sufficient time and resources to reach this key stage of PPP project preparation are likely to find it difficult to complete both the PPP and grant application processes successfully.

As set out in Chapter 9, the regulations detail specific requirements for the grant application process for Major Projects (in many respects similar to what a well prepared PPP project would require).

For a revenue-generating project, one of the key steps will consist of the appropriate (maximum) grant contribution, based on the methodology provided for in the RGDR. This is the subject of Chapter 7.⁵⁶

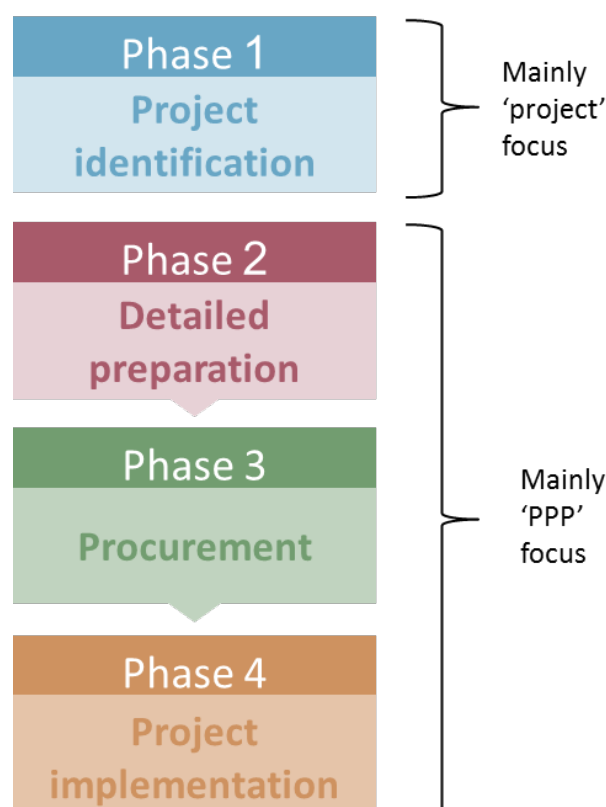
⁵⁶ See CPR, Article 101 and Annexes II and III to [Commission Implementing Regulation \(EU\) 2015/207 of 20 January 2015](#).

6.2 Potential sequence of activities in the project blending cycle

6.2.1 Overview of the PPP project cycle

As set out in the [EPEC PPP Guide](#), the typical PPP project cycle can be summarised as shown in Figure 2.

Figure 2 - The typical PPP project cycle



6.2.2 Expected blending activities in the PPP project cycle phases

It is useful when preparing a PPP project to revisit the key questions with regard to ensuring that the requirements of the project continue to be met at its different stages, whether the project still makes sense in terms of economic costs and benefits, whether it remains affordable, that the market will respond competitively to the demands made of it and that the procuring authority continues to have appropriate skills and the capacity to manage a particular phase. Checking that these five components can all continue to be met throughout the PPP project preparation process is the key to sound PPP project preparation. Please refer to the [EPEC PPP Guide](#) for more details and EPEC's PPP Project Preparation Status Tool.⁵⁷

Taking the PPP project cycle outlined above and assuming the project is a Major Project, the PPP and grant application activities and decisions in each of the four phases could be expected to look as follows:

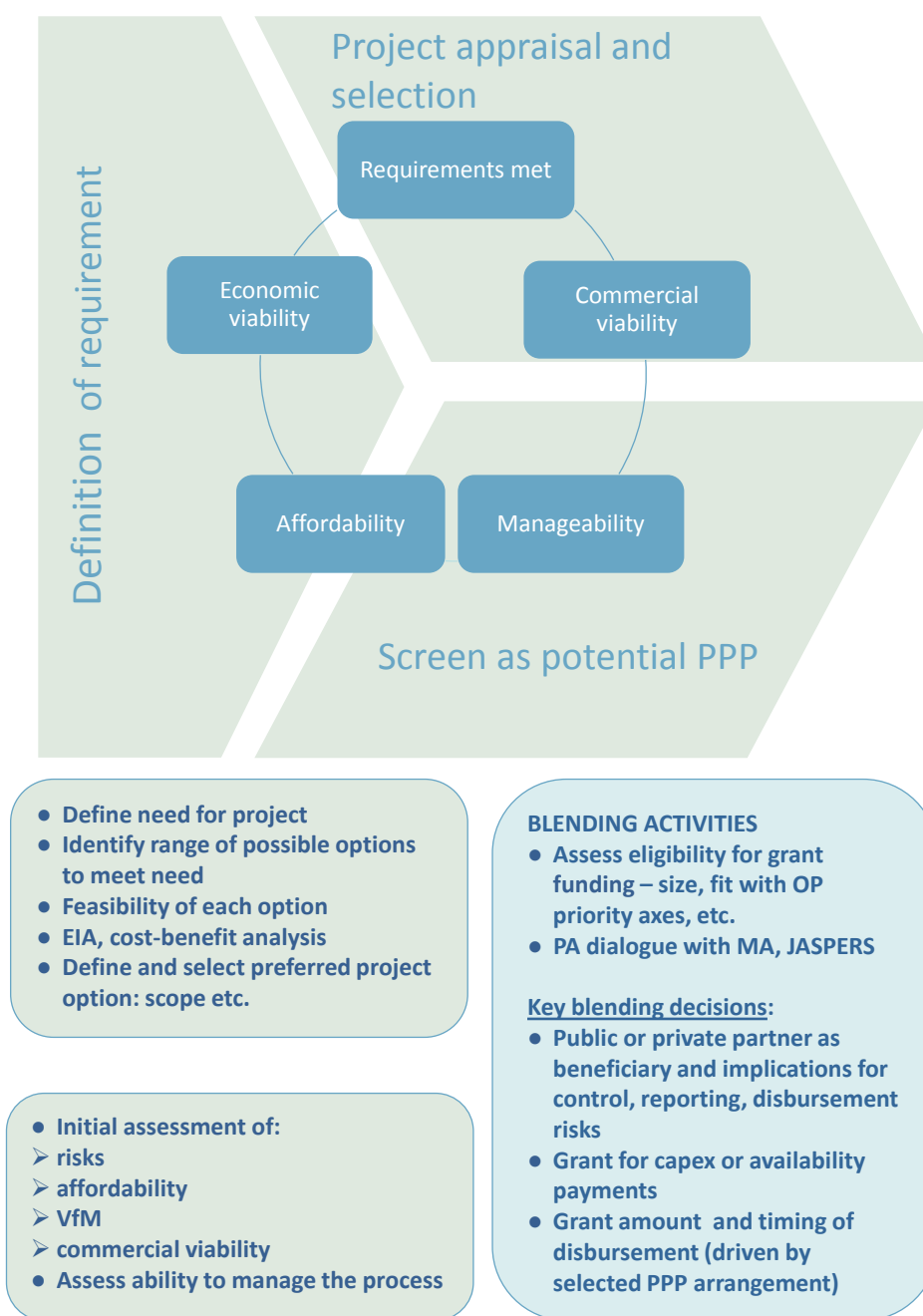
⁵⁷ Available at: [EPEC - Western Balkans Initiative](#).

Phase 1 - Project identification. During this initial stage, the procuring authority would make the case for the underlying project as an investment. Alternative project options would normally be considered and prioritised. The costs and benefits of the project itself, together with preliminary environmental and other relevant assessments, would usually be carried out by the end of this phase. Once the underlying project has been identified, the project's potential to be procured as a PPP would also be initially assessed.

With regard to the grant preparation process, during this phase the procuring authority would also confirm the eligibility of the project for grant funding as a Major Project in the OP. This may involve a dialogue between the procuring authority and the relevant Managing Authority (both of which may be part of the same government entity).

A number of underlying decisions with regard to the grant application process would be made towards the end of this phase, once the nature of the project and its potential structure as a PPP have been defined (see Figure 3).

The Managing Authority may seek support with the preparation of the grant application from JASPERS, if the project is eligible for such support (see section 10.1 for further details on JASPERS).

Figure 3 - The blending cycle - Phase 1: project identification

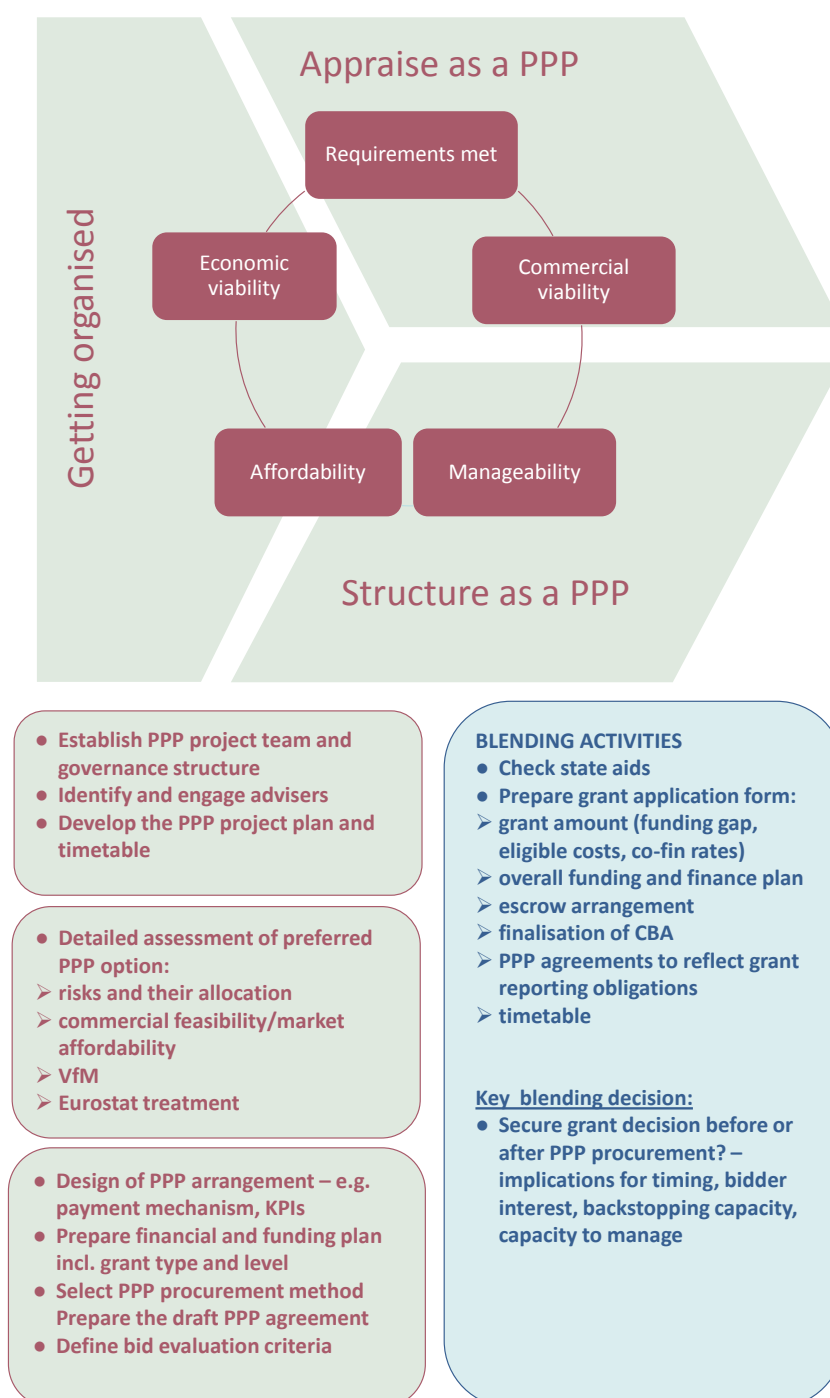
Phase 2 – Detailed preparation of the PPP and grant application. If the project is assessed as a potential PPP in Phase 1, then resources will need to be committed to develop the project as a potential PPP. Thus a project team would usually be put in place within the procuring authority and advisers would be appointed to assist it in the more detailed assessment and preparation of the PPP option.

Much of the detailed assessment of the PPP project, such as determination of the expected level and nature of costs, detailed cost-benefit analysis and a financing plan will also be required to inform the grant application, especially as it is a Major Project (see section 9.2). Therefore, given the similar information requirements, preparation of the grant application could take place at the same time as the PPP

preparation requirements, such as detailed cost and funding assessment, reinforcing the quality of grant preparation. When appointing the advisers, their terms of reference might also include assistance in the preparation of the grant application.

During this phase, the procuring authority and Managing Authority would take a decision on when to seek grant approval. This would take into account the issues referred to in section 5.1.5. This decision will help to inform the planning of the PPP procurement phase to follow (see Figure 4 below).

Figure 4 - The blending cycle - Phase 2: detailed preparation of the PPP and grant application



Phase 3 – PPP procurement and submission of the grant application. Once the detailed project assessment and preparation have been carried out and there is confidence in the expected project costs that will be bid, the procuring authority would launch the public procurement process. Assuming the decision has been taken not to complete the bidder selection before doing so, the Managing Authority (potentially working with JASPERS' support) would then proceed with the submission of the grant application (based on the information provided by the procuring authority). This would seek conditional grant approval at the start of or during the procurement phase, depending on the approach decided in the previous phase. The procuring authority would want to be in a position where the only residual condition on the grant approval is signature of the PPP agreement. During the procurement process, the procuring authority would also monitor the progress of the grant approval at key stages.

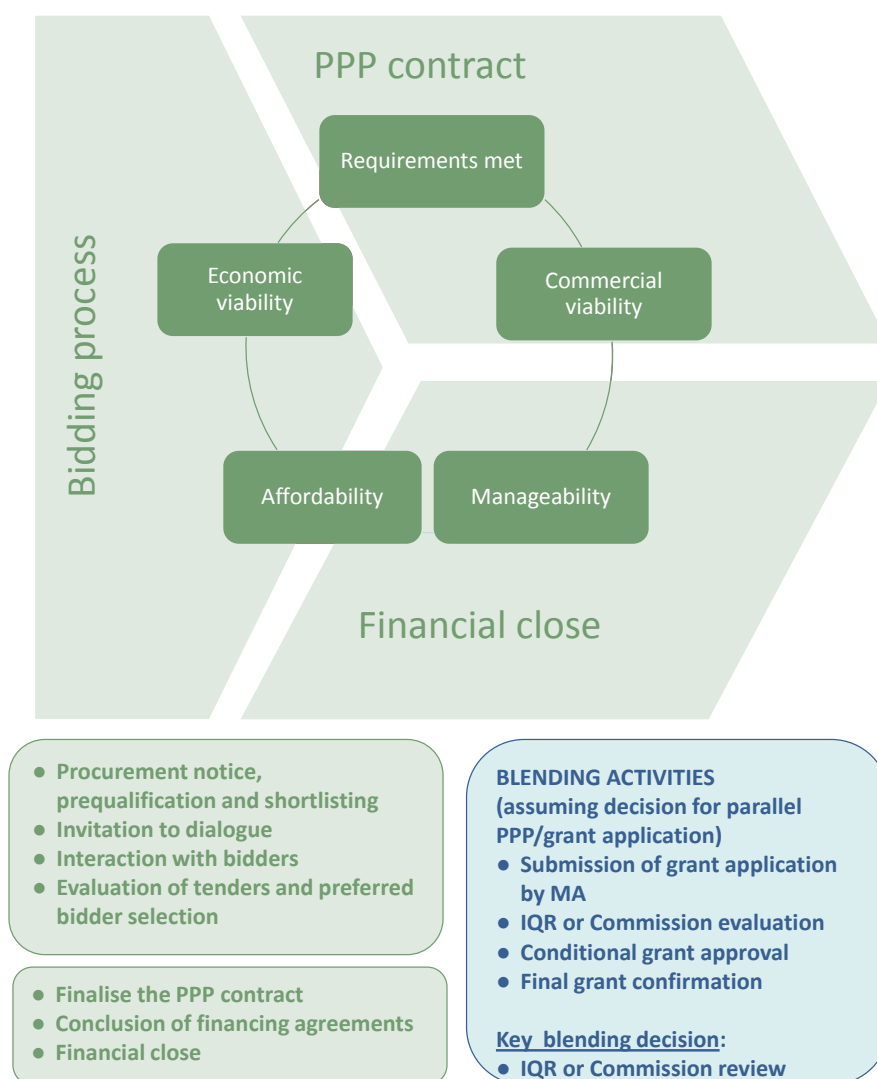
During this phase, depending on the nature of the project, the Managing Authority may also need to decide either to use the IQR and Commission 'no-objection process'⁵⁸ or a direct Commission evaluation (see Chapter 9).⁵⁹

The grant would then be confirmed prior to financial close after which drawdowns from the various financing and, if relevant, funding sources would occur to meet project expenditure (see Figure 5). It is generally good practice to avoid any delays between commercial and financial close. It is to be seen how the sequence of events around commercial close and financial close will take place in practice in different jurisdictions and the timing and flow of documentation. For example, lenders will require evidence of grant approval to enable financing to be drawn down, while at the same time the Managing Authority will require confirmation of signature of the PPP agreement. The procuring authority and private partner legal advisers would usually be involved in ensuring an acceptable process for all parties.

⁵⁸ i.e. a process in which the Commission has the right to object but if it does not do so within a specified time period, then approval is deemed to be given.

⁵⁹ See CPR, Article 102. This applies to all cases, not just to PPPs.

Figure 5 – The blending cycle - Phase 3: PPP procurement and submission of the grant application



Phase 4 – Project implementation and grant disbursement. During the life of the project and until expiry of the PPP agreement, the procuring authority would regularly monitor the project’s performance and take appropriate action in accordance with the terms of the PPP agreement. In some circumstances, changes to the agreement may be required (e.g. adjusting the service specifications) or contract disputes may need to be handled.

With regard to the grant, the beneficiary would make disbursement requests to the Managing Authority as expenditure takes place during the construction phase. These requests would then be submitted to the Commission after validation by the Certifying Authority. If an escrow account has been established, the grant amount would be disbursed into this account and later paid to the private partner in accordance with the payment provisions of the PPP agreement. The beneficiary (either public or private) would also have to meet various reporting and audit obligations towards the Managing Authority and the Commission over this phase (see Figure 6).

Figure 6 - The blending cycle - phase 4: project implementation and grant disbursement

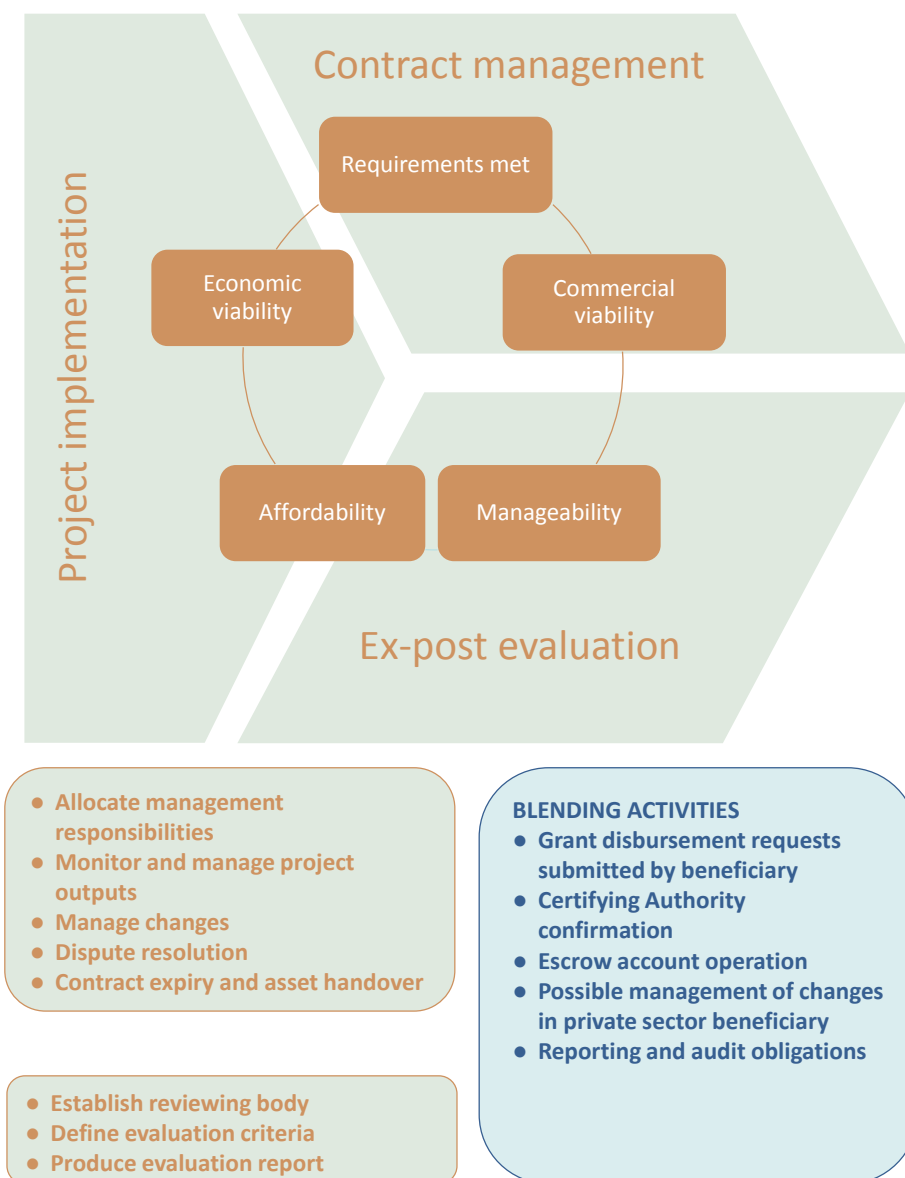
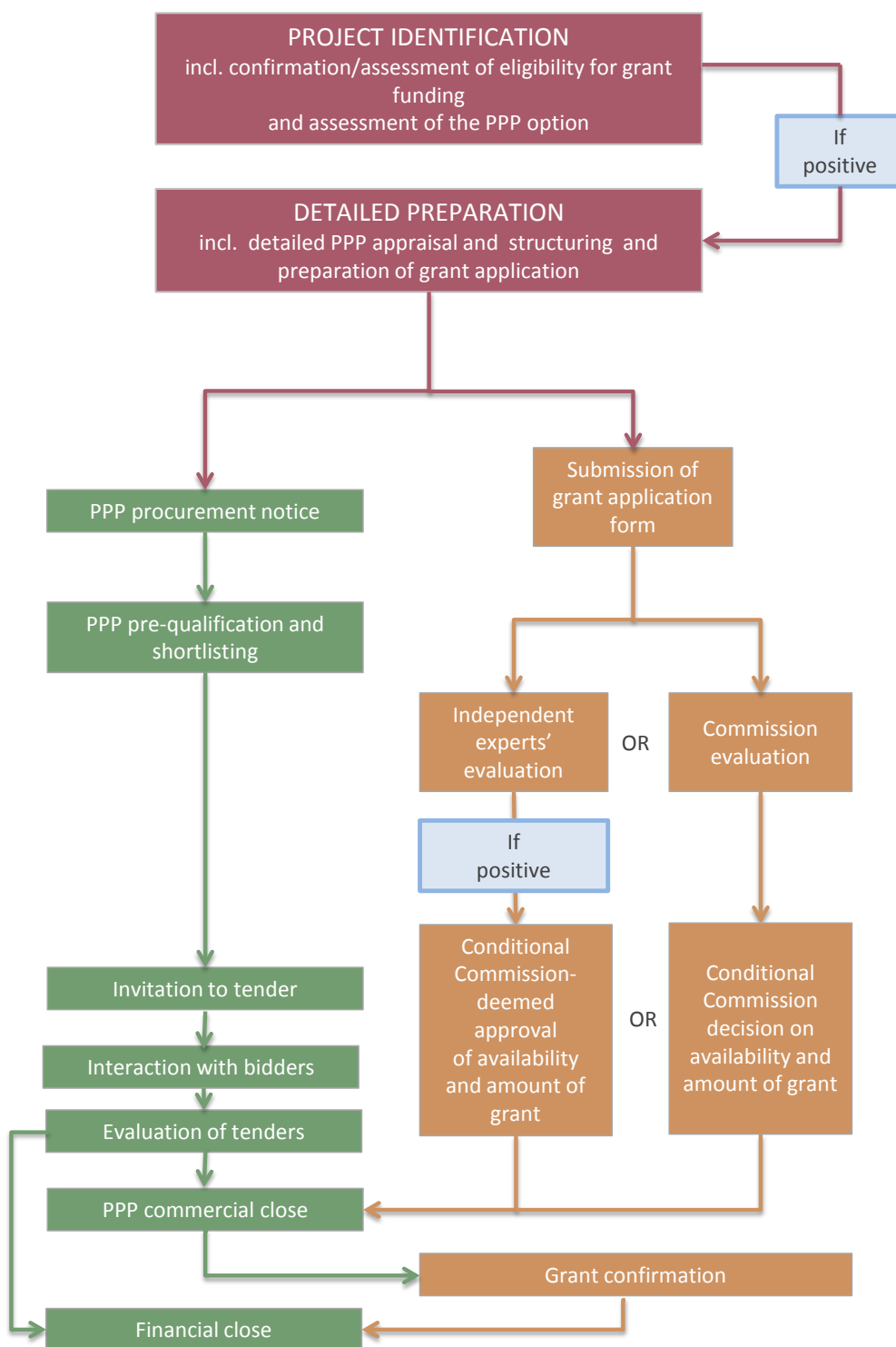


Figure 7 summarises the possible interactions between the PPP and grant application processes until grant confirmation. This assumes that the preferred approach is to obtain a conditional grant Decision prior to starting the interactions with pre-qualified bidders.

Figure 7 - Outline of expected project blending cycle



- Activities common to PPP procurement and grant application process
- PPP procurement process
- Grant application process

7 Key provisions of the CPR relevant to revenue-generating Blended Projects

A fundamental question for any project seeking grant funding supported by ESI Funds will be the amount of the grant that can be made available. An important factor in this will be consideration of the revenue, if any, generated by the project.

While the treatment in the CPR of revenue generation applies to all projects, whether PPPs or traditionally-procured, this is particularly relevant to PPPs which may be designed as user-pay schemes.

The regulations set out a number of alternative methods for estimating the level of the grant where a project is expected to be revenue-generating (i.e. where users pay directly for the services delivered). This Chapter sets out the key provisions of the CPR relevant to Blended Projects that are expected to be revenue-generating, including methods for determining the funding gap.

7.1 Main factors that determine the amount of grant funding

The amount of grant funding available to a project is determined by the following main factors:

- if a *Major Project*, the level of grant foreseen for the project in the relevant OP;
- the *co-financing rate* of the OP relevant to the project. EU grants can only support a pre-determined maximum proportion of the overall costs. The CPR establishes the maximum rates that apply for different regions based on GDP per capita and economic transition considerations;⁶⁰
- *funding gap*: the extent to which the project's costs are not expected to be covered by 'net' revenue (i.e. revenue after deducting operating and maintenance expenses) from users.⁶¹ The principle is that EU grants should only be used to the extent that the project itself is not able to generate enough revenue to cover its costs. As described in more detail below, this may be determined by applying pre-determined *flat rates* if the project falls into certain sectors foreseen by the Managing Authority; and
- *eligibility*: the amount of expenditure associated with the project that is eligible for grant funding. The principle is that certain types of costs are not eligible to be covered by EU grants (as already mentioned in section 5.2.3).

⁶⁰ See CPR, Article 120.

⁶¹ See CPR, Article 61 (2).

7.2 Revenue-generating projects and determining the funding gap

7.2.1 Relevant regulations

The rules on revenue-generating projects, including a definition of ‘net revenue’ and the rules for determining the funding gap, are provided in the CPR.⁶² The RGDR⁶³ also supplements the CPR on a number of provisions, including the methodology for the calculation of discounted net revenue. In addition, the Commission has published the Implementation Guidance which provides, *inter alia*, the formulae to be used for the calculation of the funding gap.

7.2.2 What is a revenue-generating project?

The CPR defines a revenue-generating project as one where users pay directly for services,⁶⁴ i.e. the user pays for (at least a portion of) the cost for the services provided. Where a specific tax is levied, the situation may be less clear. If the tax imposed is *directly proportional* to usage of the project, a reasonable interpretation could be that this is a revenue-generating project. A shadow tolling arrangement would not be seen as a revenue-generating project: while demand risk is transferred to the private sector, the toll is paid by the public sector and not by users in this case.

Also, a PPP project where the private partner’s entire remuneration is structured around an availability fee payable by the procuring authority would not be classified as a revenue-generating project (provided that there are no direct user charges collected by a different body) as payments are made by the procuring authority for the availability of the project’s services. It is important to highlight this, as in other areas, availability payments may be treated as a form of project revenue for different purposes.⁶⁵

The CPR does not contain any specific provisions in relation to PPPs and so the revenue-generating provisions apply equally to traditionally-procured projects and to PPPs so long as there is a net revenue feature.

There are some exceptions: net revenue considerations do not need to be taken into account in the case of projects that involve the European Social Fund (ESF), projects that amount to EUR 1m or less in total eligible costs, or where the grant is provided in the form of technical assistance and a number of other exclusions.⁶⁶

Box 1 provides an example of a revenue generating Blended Project from the past programming period.

⁶² See CPR, Article 61.

⁶³ See RGDR, Section III (Articles 15-19).

⁶⁴ See CPR, Article 61 (1).

⁶⁵ In the financial analysis of a PPP project, availability payments would be the main, if not the only, source of revenue for the private partner.

⁶⁶ See CPR, Article 61 (7).

Box 1

A revenue-generating Blended Project from the previous programming period: Poznan waste-to-energy PPP project, Poland⁶⁷

The project involves the construction, maintenance, financing and operation of a waste-to-energy plant. The project was procured as a PPP (through the competitive dialogue procedure) and was partly co-funded by an EU grant through the Polish Operational Programme 'Infrastructure and Environment' 2007-2013 under the previous programming period.

The City of Poznan, the procuring authority, opted to select the private partner before the submission of the grant application, although the City provided the Commission with some advance information on the project prior to its making a formal submission of the grant application.

In order to avoid having to backstop the grant, fully-financed Best and Final Offers (BAFOs) were requested from the bidders under the assumption that the private partner would finance 100% of the project's investment costs. If a grant was eventually approved for the project, then this would be paid to the private partner and future availability payments would be reduced accordingly. This therefore reduced the risk for the City of non-availability of the grant as private finance could be available for 100% of the project's investment costs, if necessary.

The expected funding gap for the project was then calculated in line with the applicable funding gap regulations at the time, using cost assumptions based on the preferred bidder's BAFO submission. This therefore dealt with the problem of the PPP bid otherwise requiring a different grant amount. In line with these regulations, the City would however still be exposed to adjustments of the grant in the event that project revenues turned out to be larger than expected.

The City was identified as the beneficiary of the grant, but in line with guidelines issued by the Polish Managing Authority, it was able to designate the selected private partner as 'an authorised entity to provide eligible expenditure' for the project. Under this arrangement, the EU grant could therefore be paid to the private partner on the basis of documentation demonstrating eligible expenditure as it was incurred by the private partner over the course of construction.

The amount of the EU grant disbursed and paid to the private partner would then be deducted from future service payments by the City over the life of the PPP contract.

As this project was carried out under the previous grant funding regulations, which did not explicitly cover the arrangements set out above, the operation was based on national guidelines that then needed the *ad hoc* approval of the Commission.

⁶⁷ As part of its ongoing work on the subject of combining EU funds and PPPs, EPEC produced in 2012 a paper reviewing the choices made by the procuring authority and its strategy for the PPP procurement and the grant application. This took into account the challenges for Blended Projects based on the regulations for EU funds in the previous programming period. See '[Poznan Waste-to-Energy Project, Poland. Using EU Funds in PPPs. Case Study](#)', June 2012.

7.2.3 How is the net revenue impact on eligible costs determined?

The CPR allows for the Managing Authority to choose among three methods, the:

- ‘flat-rate’ method (see section 7.2.4);
- ‘decreased co-financing rate’ method (see section 7.2.5); or
- ‘discounted net revenue’ method (see section 7.2.6).

The choice of method is exercised by the Managing Authority and must be applied consistently across a sector, sub-sector or type of operation and not by individual beneficiaries on a project-by-project basis.⁶⁸ Notwithstanding the provisions of both the RGDR and the Implementation Guidance, how, where and when the Managing Authority will exercise this choice appear to be issues that may require further clarification. This also applies to how the choice will be communicated to potential beneficiaries and whether a Managing Authority may be able to change methodology during the programming period.⁶⁹

7.2.4 The flat-rate method

The flat-rate method involves applying a pre-determined sector-specific percentage or rate to the project’s eligible costs.

The flat-rate method simplifies the determination of the grant amount as it does not: (i) require projections of revenue and operating expenses to calculate the net revenue of the project; nor (ii) entail applying any discounting in the calculations. In effect, the flat-rate method bypasses the need to establish a project-specific net revenue amount.

The flat-rate methodology also appears to bring the important advantage that:

*‘all the net revenue generated during the implementation and after completion of the operation shall be considered to be taken into account by the application of the flat rate and shall therefore not be deducted subsequently from the eligible expenditure of the operation’.*⁷⁰

It may be inferred therefore that any subsequent increases or new sources of revenue will not lead to a downward adjustment of the grant later on.

This approach however is limited to those sectors for which Annex V to the CPR has established flat rates (see Table 1). According to the CPR,⁷¹ additional rates were also to be established for the ICT, research, development and innovation (RDI) and energy efficiency sectors. A delegated regulation of 10 June 2015⁷² confirmed a flat

⁶⁸ See CPR, Article 61 (3).

⁶⁹ The Implementation Guidance, for example, refers to an indication by Managing Authorities of a ‘general preference’ at least for the flat-rate and the decreased co-financing rate methods.

⁷⁰ See CPR, Article 61 (3). See also Implementation Guidance, page 4.

⁷¹ See CPR, Article 61(3).

⁷² See [Commission Delegated Regulation C \(2015\) 3759](#) of 10/06/2015 establishing, pursuant to Regulation (EU) No 1303/2013 of the European Parliament and of the Council, a flat rate for operations funded by the European Structural and Investment Funds in the RDI sector.

rate for the RDI sector but also stated that establishing rates for the other two sectors was not possible due to the wide variation in profitability and limited data available for these sectors. The Commission may in future establish rates by delegated act for further sectors falling under the thematic objectives.⁷³

Table 1 – Flat rates for revenue-generating projects⁷⁴

Sector	Flat rates
Road	30%
Rail	20%
Urban transport	20%
Water	25%
Solid waste	20%
Research, development and innovation	20%

7.2.5 The decreased co-financing rate method

As a variant on the flat-rate method, a Member State can decide at the programming stage that one of the flat rates is applied to all operations covered by the OP that are supported under a chosen priority axis. The choice of rate will form part of the Commission's Decision on the relevant OP. No Member State has chosen this option so far, but there is the possibility for Member States to do so for specific sectors/priorities within an OP at a later stage.

As in the case of the flat-rate method, the decreased co-financing rate is applied to the amount of eligible costs. Equally, all net revenue generated during implementation (i.e. construction) and after completion (of construction) of the project is considered to be taken into account already, so subsequent changes should not reduce the grant amount.⁷⁵

7.2.6 The discounted net revenue method

The calculation of the discounted net revenue method⁷⁶ is the most complex of the three approaches but allows for a funding gap to be determined in accordance with the specificities of the project.

Details on the method to be used for calculation of the funding gap can be found in the CPR, RGDR and Implementation Guidance. The fragmentation of the rules and

⁷³ See CPR, fourth sub-paragraph of Article 61 (3).

⁷⁴ See CPR, Annex V and Delegated Act C (2015) 3759 of 10/06/2015.

⁷⁵ See CPR, Article 61 (3). See also Implementation Guidance, page 5.

⁷⁶ It is the method referred to in Article 61 (3) (b) of the CPR and in Articles 15 to 19 of the RGDR. It is the same method used in the 2007-2013 period for revenue-generating projects falling under Article 55 of Regulation 1083/2006.

their interpretation in these different regulation texts, however, makes it difficult for potential beneficiaries to have an overall view of the applicable principles and rules. For example, the Implementation Guidance sets out the formulae to be applied for the calculation but is silent on how to derive some key elements necessary for the calculation of the funding gap (such as determination of net revenues, including the consideration of the residual value, eligibility of costs, pro-rating of revenues in case not all costs are eligible and discounting methodology). For these key elements, the RGDR⁷⁷ and the CPR⁷⁸ need to be referred to. A useful reference is also the CBA Guide, which complements the provisions of the RGDR and the CBA IR concerning the funding gap calculation and the analysis required for Major Projects.

The following section provides a step-by-step explanation of the discounted net revenue method.

Step 1 – Determine the discounted net revenue

The first step requires the beneficiary to determine the expected net project revenue. According to the RGDR,⁷⁹ this involves deducting the discounted value of expected operating costs from the discounted value of expected project revenues. To this must be added, if applicable, the discounted residual value of the investment recognising that at the end of the reference period of the project (see below), the asset may still have an economic value that needs to be taken into account.

$$\text{Disc. Net Revenue} = \text{Disc. Revenue} - \text{Disc. Operating Costs} + \text{Disc. Residual Value}$$

For the avoidance of doubt, the discounted net revenue in this context does not (yet) include the capital costs of the project, but only takes into account operating expenses.

If a project's revenue is less than its operating costs (i.e. negative net revenue), the project is no longer considered a revenue-generating project (independent of whether or not the infrastructure asset has a positive residual value).

Project revenues comprise cash inflows from private users (i.e. not including availability payments made by the procuring authority) for the use of the service (or part of the service) provided by the project, as well as any cash from the sale or rent of buildings. User charges should be fixed in compliance with the 'polluter pays' principle, and, if appropriate, take account of the affordability of the service and considerations of equity (i.e. fairness) linked to the relative prosperity of the Member State or region. The CBA provides guidance on polluter pay and equity issues as these can be complex assessments.⁸⁰

In the case of a project that involves the addition of new assets to complement a pre-existing service or infrastructure asset, contributions from both new users and

⁷⁷ See RGDR, Articles 16–19.

⁷⁸ See CPR, Article 61.

⁷⁹ See RGDR, Article 15 (1).

⁸⁰ This may require, among other things, beneficiaries to question whether the actual user tariff reflects these concepts, potentially leading to a user tariff which differs from the one used for grant calculations.

additional contributions from existing users for the new or enlarged service or infrastructure asset are taken into account. However, any subsidies such as transfers from national or regional budgets or national public insurance systems should be excluded. All other cash inflows, such as contractual penalties and forfeiture of tender deposits, should be excluded⁸¹ as should non-cash accounting items such as depreciation, reserves for future replacement costs and contingency reserves.^{82 83}

Project operating costs comprise: (i) replacement costs of short-life equipment ensuring the technical functioning of the project; (ii) fixed operating costs, including fixed maintenance costs, such as staff, general management and administration and insurance costs; and (iii) variable operating costs, including variable maintenance costs, such as consumption of raw materials, energy, other process consumables and any maintenance and repair costs needed to extend the life of the project.⁸⁴

The *residual value* of the investment is defined in the RGDR⁸⁵ as the discounted cash flows in the remaining years of the project's life (i.e. for the period of the project's design life (if any) after the relevant reference period for the project - see Table 2). Other methods of calculating residual value are also allowed.⁸⁶

Discounting revenues and costs. A major factor in the context of this calculation is the discount factor applied for deriving the discounted cash flows.

As a general rule, a 4% financial discount rate in *real terms* (i.e. assuming constant prices) is the benchmark indicated in the RGDR for public investment projects using grants from ESI Funds.⁸⁷

Values other than the suggested 4% may be justified by Member States based on (i) the Member State's specific macroeconomic conditions and international macroeconomic trends and state of affairs; (ii) the nature of the investor or the implementation structure, such as a PPP; or (iii) the nature of the sector concerned.⁸⁸ The explicit mention of the possible use of a different discount rate for PPP projects is a new addition for the current programming period.

Reasons, other than those set out in the RGDR and mentioned above, can be put forward by a Member State to justify its choice of a different discount rate than the suggested 4%. The Commission requires that any argument used is robust and solid, for in the presence of weak arguments, the Commission will interrupt the assessment

⁸¹ See CPR, Article 65 (8).

⁸² See RGDR, Article 16.

⁸³ See COCOF, Article 55 Note number 07/0074/03 of 18/06/2008 provides good background information on what constitutes 'revenue' for the purposes of the funding gap calculations. While the note was prepared in relation to the old funding gap provisions under Article 55 in the prior financial perspective, it probably remains relevant as the provisions of CPR, Article 61, do not seem to depart from the previous approach in this respect. The Implementation Guidance also provides useful additional direction on the subject.

⁸⁴ See RGDR, Article 17.

⁸⁵ See RGDR, Article 18.

⁸⁶ See CBA Guide.

⁸⁷ See RGDR, Article 19.

⁸⁸ See RGDR, Article 19 (5).

procedure of the project. To underline this point, a different discount rate may be used but the reason to use it must be fully justified.

As a basis for calculating the alternative discount rate, the regulations make reference to the use of an average return of a risk-free basket of investments deemed most relevant. This indication however would benefit from some further clarification, especially given the impact that different discount rates may have on the calculation – a rate that is higher than 4% real could materially decrease the discounted revenue and subsequently lead to a higher grant amount (see section 8.4.1 and Annex II). Further clarifications and examples of how to calculate the discount rate are provided in Annex I to the CBA Guide.

If a discount rate other than the proposed benchmark is used, this rate should be applied consistently across similar operations in the same sector under the OP. The RGDR also prescribes that beneficiaries should be provided with information on the different available discount rates, but it is silent on how this information should be provided and when.

Finally, except where it is non-recoverable under national legislation, VAT should be excluded from the net revenue calculations.

Period over which the revenues and costs should be determined. The RGDR has established reference periods for different sectors over which the project's revenues and costs should be determined⁸⁹ (see Table 2). These include the implementation period of the project (i.e. in addition to the operational period of the project). It should be noted that the reference periods set out in the RGDR are binding for Managing Authorities.

⁸⁹ See RGDR, Annex 1.

Table 2 – Reference periods for the funding gap analysis

Sector	Reference period (years)
Railways	30
Water supply/sanitation	30
Roads	25-30
Waste management	25-30
Ports and airports	25
Urban transport	25-30
Energy	15-25
Research and innovation	15-25
Broadband	15-20
Business infrastructure	10-15
Other sectors	10-15

The CPR⁹⁰ makes a distinction between projects generating net revenue during implementation (i.e. construction) and during and after implementation. However, the distinction made by different articles in the CPR on the timing for the generation of net revenue does not appear to be material in the context of Blended Projects.

Subsequent changes in net revenue. If significant changes in the circumstances of the project materialise (e.g. subsequent sources of revenue arise that are not taken into account in the original funding gap calculation or actual net revenues turn out to be higher than those originally projected as a result of a tariff policy change), a downward adjustment of the grant amount may then be required.⁹¹ For example, if a road was not planned to be tolled at the time of making the application and at a later stage a decision is made to impose a toll, then tolling revenue might require a new funding gap calculation.⁹² On the other hand, if the increased revenue was a result of higher than forecast demand, this should not lead to a grant reduction/reimbursement. This issue does not arise if the flat-rate method is used, as mentioned above.⁹³

⁹⁰ See CPR, Article 61.

⁹¹ See last sentence of CPR, Article 61 (3). Also relevant is Section 4.4 of COCOF, Article 55, Note number 07/0074/03 of 18/06/2008 on refunding.

⁹² Provided that the Managing Authority has decided that for this sector and type of operation the calculation of discounted net revenue method was to be used. See CPR, Article 61 (3).

⁹³ As Article 61 of the CPR applies to projects that generate net revenue after their completion, Article 65(8) is established for projects generating revenue only during implementation. The similar principle of deducting net revenue not taken into account at the time of approval, but this time only over the implementation period, applies with the exception where the ESI funds are provided in the form of technical assistance, Financial Instruments,

Apportioning net revenues to eligible and non-eligible costs. Given that some project costs are not eligible for grant funding, not all net revenues should be taken into account when calculating the funding gap. It is only fair that if some of the investment costs are not eligible for grant funding, then some of the revenue generated by the project notionally linked to such costs should be allocated to fund these costs. This reduces the level of revenue netted off from the costs that are eligible. Thus, if an operation has eligible and non-eligible costs, net revenues are allocated pro rata to the eligible and non-eligible parts of the overall investment costs.⁹⁴ This basic principle is generally applicable independently of the method chosen for calculating the net revenue.

Step 2 - Determining the funding gap rate

Once the discounted value of the net revenue (**DNR**) is determined, as above, the discounted investment costs (**DIC**) are deducted from this to arrive at the funding gap (**FG**). For this calculation, the investment costs are discounted at the same rate as that used to determine the discounted net revenue (see above).

$$\text{FG} = \text{DIC} - \text{DNR}$$

The Implementation Guidance then expresses the funding gap as a proportion of the discounted investment costs or as a funding gap 'rate':

$$\text{Funding gap rate} = 1 - \frac{\text{Discounted Net Revenue}}{\text{Discounted Investment Costs}}$$

This brings the calculation to the same point as in the flat-rate method, with the funding gap expressed as a rate that can be applied to eligible costs.

As can be seen, the discounted net revenue method involves a much higher degree of analysis than the other two available methods. This was the only approach available in the previous programming period. Given the number of variables involved, determining the funding gap rate was, unsurprisingly, cited as one of the most challenging components of the grant application process for revenue-generating projects.

7.2.7 Determining the EU grant

This final stage in the grant determination process involves different steps depending on whether the flat-rate, decreased co-financing rate or discounted net revenue method has been used. These steps are explained below, based on the Implementation Guidance.

repayable assistance subject to an obligation for full repayment, prizes, operations subject to the rules on state aid, when public support takes the form of a lump sum, standard scale units (provided net revenue has been taken into account ex ante), eligible costs below EUR 50 000 or the other specified cases.

⁹⁴ See CPR, Articles 61 (1) and 65 (8).

Flat-rate method

If the flat-rate method has been used, the eligible project costs (**EC**) are first adjusted by applying the pre-established flat rate (**FR**) (see Table 1 above) to determine what is referred to as the 'decisional amount' (**DA**):

$$\text{DA} = \text{EC} \times (1 - \text{FR})$$

The EU grant amount is then determined by applying the relevant maximum 'co-financing' rate for the priority axis that applies to the project (**maxCRpa**) to the DA (see section 7.2.4 above):

$$\text{EU grant} = \text{DA} \times \text{maxCRpa}$$

Decreased co-financing rate method

If the decreased co-financing rate method has been used, the maximum co-financing rate is simply adjusted downwards by the flat rate that has been determined to be applied across the chosen priority axis. This produces a reduced co-financing rate (**Reduced maxCRpa**):

$$\text{Reduced maxCRpa} = \text{maxCRpa} \times (1 - \text{FR})$$

The EU grant amount is then determined by applying this **Reduced maxCRpa** to the eligible costs (**EC**):

$$\text{EU grant} = \text{EC} \times \text{Reduced maxCRpa}$$

Discounted net revenue method

If the discounted net revenue method has been used, the eligible project costs (**EC**) are adjusted by applying the funding gap rate (**FGR**) (as calculated above) to determine the 'decisional amount' (**DA**):

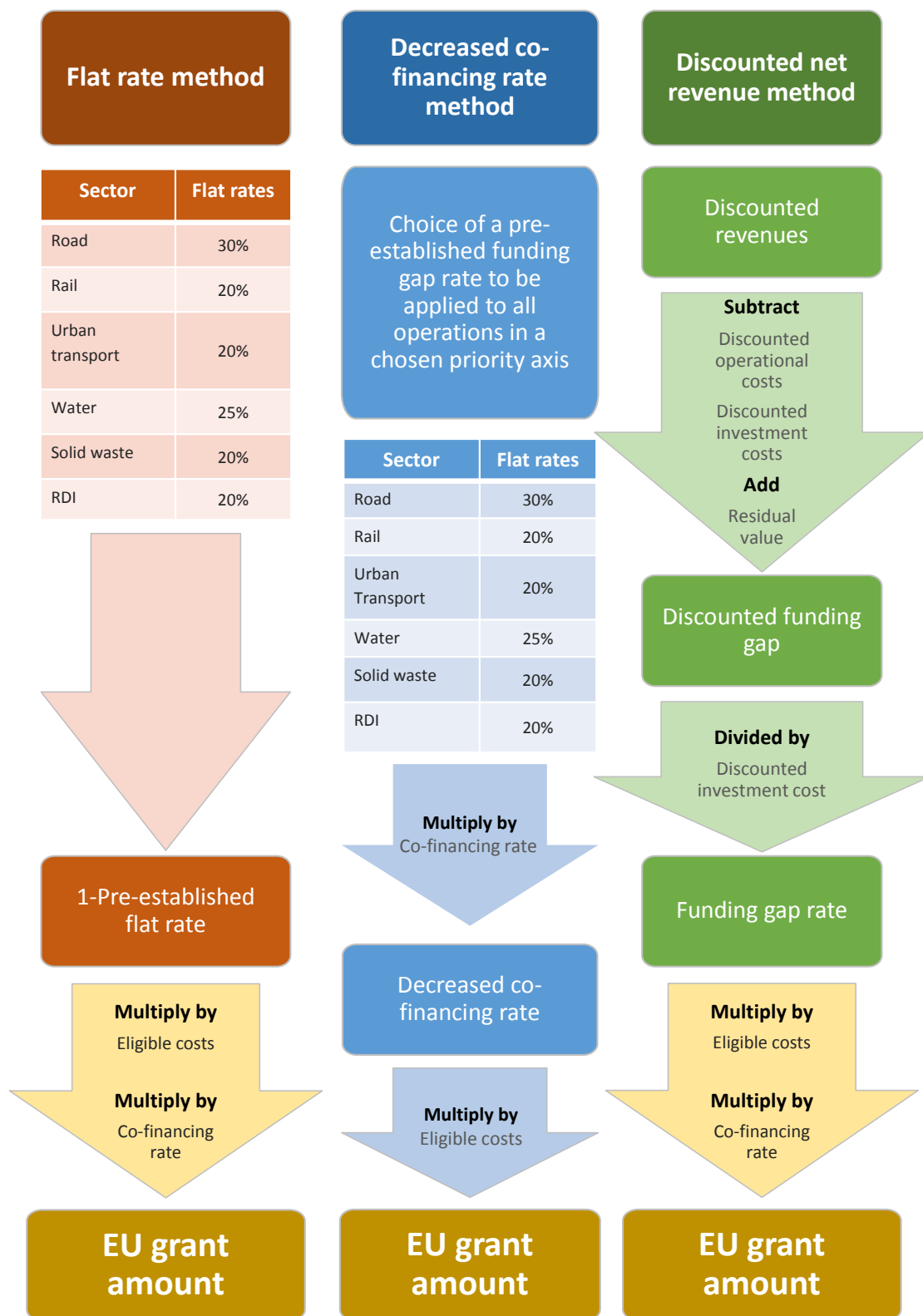
$$\text{DA} = \text{EC} \times \text{FGR}$$

The level of EU grant is then determined by applying the maximum co-financing rate of the priority axis (**maxCRpa**) to the **DA**:

$$\text{EU grant} = \text{DA} \times \text{maxCRpa}$$

Figure 8 sets out a comparative summary of the three processes.

Figure 8 – Summary of the possible processes for the determination of the EU grant amount



8 Practical considerations in planning, procuring and managing a Blended Project

This Chapter considers some of the practical issues that are likely to arise in a Blended Project. The various options and critical decisions that procuring authorities may need to consider in planning their approach are highlighted. Using an illustration case, this Chapter looks at some of the practical issues associated with:

- the timing of the grant application in relation to the PPP process;
- the impact of different PPP structures on the level of the grant;
- calculating the grant amount based on the rules for revenue-generating projects; and
- decisions around whether the procuring authority or the private partner should be the beneficiary of the grant.

As the regulations and associated delegated acts have only recently been published, real project examples are not yet available upon which to draw experience on the application of the new regulations. Therefore, a theoretical Blended Project illustration case is used in this Chapter to help explain the various issues arising.

As and when Blended Projects are developed by procuring authorities and Managing Authorities under the new regulations and with the help of its Members, EPEC will seek to share experience and any practical lessons learned. This guidance note may be further refined accordingly from time to time.

8.1 Description of the Blended Project illustration case

The regional road agency (the procuring authority) of a fictional Member State with a large ESI Fund allocation wishes to proceed with the implementation of a 30 km road between cities A and B (the Project). The Project is located in a mountainous area of the country. The two cities are currently linked by a long, winding and dangerous road. There is no rail connection. Studies demonstrate that the economic benefits of the Project are likely to be significant as the lack of safe and fast road transport between the two cities is holding back their economic development, not to mention the high accident rates on the existing road. In accordance with government policy, the conclusion of initial VfM, affordability and bankability assessments point toward potential PPP solutions. The Project also fits along an important mobility axis of the Transport and Mobility OP agreed between the Commission and the Government for the current programming period.

Although many of the technical details for the preparation of the Project are well advanced, advisers have only recently been hired and different contractual, funding and financing options are now being considered.

While the Government has agreed to make available to the procuring authority some funds for its capital contribution to the Project, the authority is under strict instructions to limit this up-front capital contribution and to seek final Government approval before

entering into any PPP agreement (or otherwise committing the Government to a funding contribution).

Due to the mountainous terrain, the Project's technical designers have included several bridges in the Project scope, implying some significant construction costs and risks. Furthermore, a study of potential users' willingness and ability to pay a toll has demonstrated a low toll affordability threshold for users. This, combined with the limited availability of up-front Government funding, has led the procuring authority to conclude that the Project is only likely to be affordable if it can benefit from significant grant funding, although the exact amount of funding has yet to be determined.

The Managing Authority has confirmed that the Project is identified as a Major Project within the 'Transport and Mobility OP'.

The procuring authority now needs to determine:

- when the grant application should be prepared and submitted and at what point it would be best to have the grant approval in place in relation to the PPP process;
- what PPP structure is best suited for the Project and what this might mean in terms of the grant amount it can apply for; and
- whether it should be the beneficiary of the grant or whether the private partner should be the beneficiary.

8.2 When to secure the grant approval?

The procuring authority is not in a position to fund any shortfall as a result of the national grant or a grant from the ESI Funds not being confirmed as anticipated. The central government has made it clear that it will not be able to increase the amount of any central funding contribution from national resources once this contribution has been approved.

At the same time, the PPP project advisers have indicated that it would be unrealistic to expect potential bidders for the Project to take a risk on the grant element not materialising and that it would be important to present the expected funding sources (both the national grant and any grant from the ESI Funds) to bidders as early on in the procurement process as possible.

This means that the procuring authority must have clarity on the availability and maximum amount of the grant available from ESI Funds as soon after launching the procurement process as possible and certainly well before the Project reaches financial close (a point at which all sources of funding and financing need to be committed to by the various parties contributing to the funding and financing of the Project).

Given these constraints, the procuring authority concludes that the ESI Fund grant application needs to be prepared before launching the procurement process. A conditional grant Decision must then be secured early on in the procurement process before concluding the bidder pre-qualification stage. This is to ensure that pre-

qualified bidders have a clear basis on which to prepare their bids, including their financing proposals. It would also avoid the use of potentially costly cancellation clauses in the event that the grant Decision turns out to be negative or for a lesser amount than anticipated. It will then seek final confirmation of the grant when the bidder is known but just before financial close, towards the end of 2017.

As the Project is classified as a Major Project, the procuring authority will use the Major Project application form as the basis for submitting the information required for the grant application. In this instance, the assessment procedure selected by the Managing Authority for the relevant OP is the Independent Quality Review (IQR) (see Chapter 9) by independent experts. In this option, if the assessment from independent experts is positive, the grant will be deemed to be approved in the absence of an explicit objection from the Commission.

The timetable for the Project phases is expected to be as follows:

- the procurement phase (ending in financial close) completed by end-2017;
- the construction phase (3 years) starting in 2018, completed by the end of 2020; and
- the road available in 2021, with a 25-year operational period under the PPP agreement, concluding at the end of 2045. The reference period for the analysis is therefore set at 30 years (5 years for project procurement and construction, plus 25 years of operation).⁹⁵

In establishing its overall budget for the Project, it is important for the procuring authority to take note of the timing of expenditure for each phase of the Project in relation to the grant application date. Any Project expenditure that takes place after the expiry of the programming period (cut-off date 2023) will not be eligible for grant funding.⁹⁶ Table 3 summarises the key Project dates.

⁹⁵ The 30-year reference period is therefore in line with the provisions of the RGDR.

⁹⁶ Payment applications are the declarations of expenditure submitted to the Commission under every OP. The OP Certifying Authority draws up and submits to the Commission the payment applications. It also reviews the accounts, certifying their completeness, accuracy and veracity and certifies that the expenditure entered in the accounts complies with applicable EU and national rules.

Table 3 Summary of key Project dates

Expenditure item	Date	Eligibility period for the purpose of costs that may be covered by the grant
Grant application	2016	Yes
Procurement and grant approval	2016-2017	
Construction period	2018-2020	Yes
Operating period	2021-2045	Yes (2019-2023) No (2024-2045)
Duration of operation (years)	25	-
Reference period (years)	30	-

8.3 What is the impact of different PPP structures on the level of the grant?

The procuring authority is considering a number of PPP options and associated funding options, including the following:

- (a) transferring the traffic risk to the private partner and having it charge and collect a toll from users which may need to be complemented by a performance-based subsidy;
- (b) transferring the traffic risk to the private partner and paying the private partner a shadow toll funded from the national budget;
- (c) paying the private partner wholly through an availability fee (hence not transferring the traffic risk) funded from the national budget; and
- (d) paying the private partner an availability fee (hence not transferring the traffic risk) funded by toll charges, collected from users by the operator on behalf of the procuring authority, complemented if necessary by a subsidy from the national budget.

The choice of option will be driven by considerations of issues of VfM, affordability and bankability of the different risk allocation profiles for each option, existing policies on user charging and other factors. As the level of grant is reduced by the extent to which a project is able to generate revenue from users (after taking into account operating costs), it is important for the procuring authority to understand the revenue-generating potential of the different options:

- option (a) above may potentially be revenue-generating assuming the level of revenues collected exceeds the operating costs of the road;
- options (b) and (c) would not be revenue-generating as revenue is not being collected from users; and

- option (d) is potentially a revenue-generating project. Who collects the user charge is not relevant for the purposes of determining whether or not the project is revenue-generating. As the user is charged a toll to help pay for the road, this is enough to conclude that it is revenue-generating (depending of course on the level of revenues in relation to the operating costs of the road).

There may be other options where the link between the user payment and the operation is not so direct but may still be considered linked. For instance, a specific tax may be considered sufficiently directly linked to the provision of the service to treat the operation as revenue-generating (even if not linked to volume usage). This may be less obvious if a general road tax for the use of motor vehicles throughout the country is applied which is not linked to the use of the specific road. It may therefore be important for the procuring authority to check early on with the Managing Authority that the expected treatment of the Project for grant calculation purposes is clear.

The scenarios above illustrate how policy decisions (in this case around how the road will be paid for) influence the grant calculation and amount. As these are policy-based decisions, there is no intrinsic right or wrong option.

For the purposes of this Blended Project illustration case, the private partner is assumed to have the right to charge and collect a toll from users. The Government has decided that it will ask users to contribute to the costs of the project and that the private sector partner will assume traffic risk. However it recognises that the level of toll that is affordable for users will need to be supplemented by availability-based payments to the private partner. This payment will be funded from EU and national sources.⁹⁷ Accordingly, option (a) is chosen as the preferred option.

8.4 What is the expected grant amount if the project is expected to be revenue-generating?

For illustration purposes, the co-financing rate for the OP is already established at 75% of any net revenue-adjusted eligible expenditure for the Project.

If the Project is expected to generate net revenues, then further adjustments to the grant amount will need to be calculated in accordance with at least one of the methods set out in the CPR, chosen by the procuring authority and as described in Chapter 7. The procuring authority has decided to assess the potential level of grant using both the flat-rate method and the funding gap method.

At the programming stage, the Managing Authority had not decided that a flat rate (as specified in Annex V to the CPR) would be applied to all operations that are supported under a chosen priority axis. For this reason, the 'decreased co-financing rate' method is not available.

⁹⁷ For the avoidance of doubt, this scenario has been chosen simply to illustrate the different calculation considerations in relation to revenue-generating operations under the CPR and it does not reflect EPEC's view on the acceptability, bankability or VfM of projects where traffic risk is transferred to the private sector nor does it claim to illustrate best practice in relation to risk allocation.

8.4.1 Calculation of the grant using the flat-rate method

If the procuring authority decides to use the flat-rate method, it only needs to apply the standard flat rate of 30% for the road sector (see Table 1) to the eligible costs to establish the decisional amount:

$$\begin{array}{rclcl} \text{Decisional amount} & = & \text{Eligible costs} & \times & (1\text{-flat rate}) \\ 399 & = & 570 & \times & (1\text{-30\%}) \end{array}$$

The EU grant is calculated in a similar way to the discounted net revenue method by applying the maximum co-financing rate of 75% to the decisional amount:

$$\begin{array}{rclcl} \text{EU grant} & = & \text{Decisional amount} & \times & \text{Maximum co-financing rate for the priority axis} \\ 299 & = & 399 & \times & 75\% \end{array}$$

8.4.2 Calculation of the grant using the discounted net revenue method

Step 1 – Determining the discounted net revenue

Project revenue: Project revenues will come from the tolls to be paid by the road users which are assumed initially to be set at EUR 0.1 per km. In the first year of operation, the traffic projections are estimated at 19 000 cars per day. The procuring authority estimates that traffic will grow by 2% per year during operation. Consistent with the cost-benefit analysis methodology set out in Annex II to the CBA IR, the funding gap analysis is carried out in constant (real) prices and thus revenue and costs are not adjusted for inflation. Based on these assumptions, toll revenues (in real terms) are estimated at EUR 625m over the Project's operational period (see Annex I for detailed Project cash flows).

Project operating costs: Periodic maintenance and other operating costs are estimated at EUR 150 000/km p.a., totalling EUR 113m throughout the operational period. As in the case of revenues, operating costs are also expressed in real terms.

Period over which revenue and costs should be determined: The reference period for the Project is established at 30 years. This is compliant with the provisions of the CPR (see Table 2 in section 7.2.6),⁹⁸ which prescribes a reference period of 25-30 years for the calculation of the discounted net revenue for projects in the road sector.

Residual value: For the sake of demonstration, the procuring authority assumes that the asset does not have an economic life in excess of the reference period, so no residual value is calculated.

Discounting the revenue and costs: The funding gap calculation must be based on discounted values. In the example, the 4% benchmark discount rate, as suggested by the RGDR, is used by the procuring authority. Applying this to the undiscounted

⁹⁸ As based on Annex I to the RGDR.

revenues of EUR 625m (see above) leads to a discounted value of EUR 379m. However, as mentioned in section 7.2.6, discount rates other than the suggested 4% may be applied, as the Project is a PPP. If the authority were to choose an alternative discount rate, the result could be very different. For example, using a discount rate of 6%, instead of 4%, leads to an increase of EUR 30m in the EU grant amount (an 11% increase) in this particular example. See Annex II for the detailed calculation of this result.

It is also possible to apportion net revenues between eligible and non-eligible costs (see section 5.2.3) reducing the effect of net revenues on the grant amount. In this instance, eligible costs are 83% of total costs. This same proportion is applied to the total discounted net revenue of EUR 379m, reducing the net revenue amount to be used for the grant calculation to EUR 317m.

Subtracting the total discounted operating costs of EUR 70m from the total discounted revenues and adding the zero residual value gives a discounted net revenue estimate for the Project of EUR 247m:

Disc. net revenue	=	Disc. revenue	-	Disc. operating costs	+	Disc. res. value
247	=	317	-	70	+	0

Step 2 – Determining the funding gap rate

Investment costs: Once the discounted net revenue is calculated, the discounted investment costs are determined and subtracted from the net revenue to establish the funding gap.

The cost for the construction of the 30 km road is estimated at EUR 15m per km with expected construction costs being spread over the 3-year period. Development costs related to project design and other early costs amount to EUR 10m. Land purchase is estimated at EUR 90m. Other investment costs (e.g. general expenses, security of the construction site, costs related to unforeseen events) amount to EUR 5m. Total initial capital costs are therefore estimated at EUR 555m. In line with the methodology in the CBA IR, these costs are expressed in real terms.

Heavy maintenance is forecast to take place in years 3, 10 and 15 of the operational period at a cost of EUR 1.5m per km, totalling EUR 135m (in real terms) for the entire operating period before adjusting for inflation. Overall capital costs, including heavy maintenance, therefore amount to some EUR 690m (see Table 4).

VAT on investment costs is not included in the model as it is assumed to be recoverable as a transfer payment with public funds.⁹⁹

⁹⁹ See CPR, Article 59 (3)(c). For more detail on key issues arising in the context of VAT and PPPs, see also the EPEC paper '[VAT and PPP contracts](#)' (July 2013).

Table 4 - Amount and distribution of projected investment costs over time

Investment costs	2016	2017	2018	2019	2020	2021 to 2045	Total
Design costs	7 000	3 000					10 000
Land purchase costs		50 000	40 000				90 000
Construction costs			135 000	180 000	135 000		450 000
Heavy maintenance costs						135 000*	135 000
Other investment costs	2 000	3 000					5 000
Total investment costs	9 000	56 000	175 000	180 000	135 000	135 000	690 000

Values in EUR '000s - * years 3, 10 and 15 of the operational period

Applying the same discount rate of 4% in real terms to investment costs as to the net revenues (both expressed in real terms) gives a discounted total investment cost of EUR 680m.

Calculation of the funding gap rate: The funding gap is determined by subtracting the discounted value of the net revenue from the discounted value of investment costs:

Funding gap	=	Disc. investment costs	-	Disc. net revenue
433	=	680	-	247

Or, expressed as a rate:

Funding gap rate	=	1	-	<u>Disc. net revenue</u> Disc. investment costs
63.71%	=	1	-	<u>247</u> 680

Step 3 – Determining the EU grant amount by applying the funding gap rate

With the funding gap rate now calculated, the next step is to determine the eligible costs to which the rate can be applied (see section 5.2.3). In the Project example the eligible costs would include:

- total investment costs (including heavy maintenance over the operating period);
- expenditure incurred within the current programming period and excluding expenditure related to the period beyond the cut-off date of 2023;
- the cap of 10% of total eligible costs applied to land purchase costs; and

- exclusion of other non-eligible costs (such as recoverable VAT, depreciation, interest).

As can be seen from Table 5, total eligible costs amount to EUR 570m (83% of total investment costs).

Table 5 - Determination of eligible costs over time

Items	Total	2016	2017	2018	2019	2020	2021	2022 to 2045
Total investment costs (incl. heavy maintenance)	690 000	9 000	56 000	175 000	180 000	135 000	45 000	90 000
A. of which, expenditure within the programming period	600 000	9 000	56 000	175 000	180 000	135 000	45 000	-
B. of which, land costs	90 000	-	50 000	40 000	-	-	-	-
C. cap on land costs (10% of eligible costs)	60 000	-	-	-	-	-	-	-
Total eligible costs (A-B+C)	570 000	-	-	-	-	-	-	-
<i>Ratio eligible costs/total costs</i>	<i>83%</i>	-	-	-	-	-	-	-

Values in EUR '000s

The so-called 'decisional amount' is then calculated by applying the funding gap rate to the eligible costs. Note that in this calculation, such costs are *not discounted*:

$$\begin{array}{rclcl}
 \text{Decisional amount} & = & \text{Eligible costs} & \times & \text{Funding gap rate} \\
 363 & = & 570 & \times & 63.71\%
 \end{array}$$

The final step involves applying the maximum co-financing rate, which in this case is 75%, to the decisional amount. Therefore the grant amount will be:

$$\begin{array}{rclcl}
 \text{EU grant} & = & \text{Decisional amount} & \times & \text{Maximum co-financing rate for the priority axis} \\
 272 & = & 363 & \times & 75\%
 \end{array}$$

The discounted net revenue method therefore indicates a grant amount of EUR 272m for the Project.

When compared to the flat rate method (EUR 299m), the discounted net revenue method generates a slightly lower grant amount (EUR 272m) in this particular case.

However, this outcome is strongly dependent on the assumptions used in the discounted net revenue method regarding certain variables and the nature of the Project.

Taking the slightly higher grant amount into consideration, and as the added benefit of any subsequent changes in revenue would not have an impact on the grant amount (unlike the discounted net revenue method), the procuring authority decides to apply the flat-rate method in this instance.

8.5 Who will be the beneficiary of the grant?

Whether the procuring authority or the private partner will be the beneficiary (see section 5.1) is a decision that the procuring authority needs to make.

The authority could choose to use the grant to pay for eligible costs as and when they occur during the construction period. In this case, the authority might choose to designate the private partner as the beneficiary.

However, the procuring authority is keen to retain control over grant disbursements to the Project and use these to help pay for the long-term performance-based payments to the private partner. Accordingly, the procuring authority decides it will be the beneficiary of the grant.

The procuring authority therefore puts in place an escrow account where grant disbursements from the Managing Authority can be held and used for payments under the PPP agreement. In this instance, and based on a toll of EUR 0.1 per km, the authority and its advisers estimate that the annual availability payment will be around EUR 45m. Over the initial 10 years of the operating period, it will use the grant to pay for about 60% of the availability payments in each year.

The procuring authority ensures that the PPP documentation contains clear provisions requiring the private partner to provide information in a timely manner as required by the Managing Authority. This will help to ensure that there are no delays in grant disbursement and that reporting requirements will be met.

It is important to be aware that the private partner will pay close attention to the risks of any delay in payments that are due to it as a result of the grant disbursement processes, over much of which they may have no control. This may even form a part of their initial assessment as to whether or not to participate in the project. The extent to which the procuring authority can mitigate such risks, for example by clarifying the process and proving good management of the procedures, will be important.

9 Particular issues regarding Major Projects

Managing Authorities can select small projects for co-funding from ESI Funds over the course of the programming period, provided the projects are in line with the objectives of the relevant OP. However, larger projects that are expected to be implemented over the programming period are specifically identified up-front in the OP as 'Major Projects'.

Major Projects are usually large-scale infrastructure projects supported with funding from the ERDF and/or the CF. They are generally in the transport and environment sectors but may also be in other sectors such as culture, education, health, energy or ICT. A Major Project may comprise a collection of works, activities or services intended to deliver an indivisible task. A Major Project is also defined as a project exceeding EUR 50m or, in the case of a transport or other project designed to remove bottlenecks in network infrastructure, EUR 75m.¹⁰⁰ Many potential Blended Projects are likely to be Major Projects due to their size and sector.

As mentioned in section 2.6, ESI Funds not allocated to a Major Project are allocated under calls for proposals over the course of the programming period. This process adds complexity in the case of Blended Projects where, as shown above, aligning the grant amount with the financing resources available from the PPP process already requires careful coordination.

By contrast, grants set aside for specific Major Projects are better suited for Blended Projects given that they are already at least identified in the OP and therefore benefit from a higher level of predictability with regard to their availability for the project. Nevertheless, the timing for obtaining a final grant Decision is still not certain and its final quantum will still depend on a number of assessments (such as the funding gap calculation).

9.1 Relevant regulations

The relevant provisions specifically related to Major Projects can be found in the following documents:

- CPR, Articles 100-103, setting out the definition of a Major Project, the information necessary for approval and the Decision procedures involved;
- CBA IR, Annexes II and III, providing models for the submission of information on a Major Project and the methodology for carrying out cost-benefit analysis. The model set out in the CBA IR should be used for the information that is provided for the IQR or directly to the Commission, depending on the chosen appraisal procedure;
- DG Regio [Guide to Cost-Benefit Analysis of Investment Projects](#) published in December 2014, providing the methodology for financial and cost-benefit analysis of projects eligible for grants from ESI Funds; and

¹⁰⁰ The total eligible cost is the part of the investment cost that is eligible for EU co-financing. See CPR, preamble 92.

- [EC Implementing Regulation No 1011/2014](#), providing the standard format for notification to the Commission on Major Projects following a positive assessment by the IQR.

The information requirements and the procedures for the approval of Major Projects have changed from the provisions for the 2007-2013 programming period. Annex III sets out the key changes.

9.2 Securing a grant from ESI Funds for a Major Project

9.2.1 Grants application requirements

The first step for securing a grant from ESI Funds for a Major Project is the preparation of the grant application.¹⁰¹ The CPR sets out specific information requirements that the Managing Authority should ensure is included in the grant application, namely:¹⁰²

- details concerning the body responsible for implementation of the Major Project and its capacity to do so;
- description of the investment and its location;
- total cost and total eligible costs (taking account of the requirements set out in provisions regarding revenue-generating projects);
- feasibility studies carried out, including options analysis, and the results;
- cost-benefit analysis, including economic and financial analyses and a risk assessment;
- analysis of the environmental impact, taking into account climate change mitigation and adaptation needs and disaster resilience;
- explanation as to how the Major Project is consistent with the relevant priority axes of the OP(s) concerned and its expected contribution to achieving the specific objectives of those priority axes and its expected contribution to socio-economic development;
- financing plan showing the total planned financial resources and the planned support from ESI Funds and all other sources of financing and funding, together with physical and financial indicators for monitoring progress, taking account of the identified risks; and
- timetable for implementing the Major Project and, where the implementation period is expected to be longer than the programming period, the phases for which support from ESI Funds is requested during the programming period.

This information represents the basis for the appraisal of the Major Project and for the Decision on whether the required support from ESI Funds is justified. All the information should be provided in a standard format as set out in Annex II to the CBA IR, which has been adapted for Major Projects procured as PPPs (see Box 2). As

¹⁰¹ See CPR, Article 101 and CBA IR.

¹⁰² Subsequent, but previously identified, phases of a project are subject to slightly reduced approval requirements.

can be seen from the comprehensive nature of the information requirements, the preparation effort for a grant application for a Major Project should not be underestimated. It is advisable that the relevant Managing Authority and the procuring authority co-operate well in advance, so that the quality of information can be assured. This is crucial to ensuring timely and successful approval of the grant application (see also Chapter 6 on the possible interactions between the grant application and PPP preparation/procurement processes).

Box 2 – How the Major Projects standard form has been adapted to the requirements of Blended Projects

In order to account for some of the requirements of Major Projects procured as PPPs, the Commission has adapted the standard format for the submission of a grant application, provided for in Annex II to the CBA IR. This introduces specific information requirements in the case of PPPs or adjusts the standard information requirements where they may not be available in the case of PPPs (especially in the event that the procuring authority decides to procure the PPP and select the private partner beneficiary at a later stage).

The following table summarises how the standard model has been adapted to PPPs.

Section	Standard information	Information in the case of a PPP
A.2. Body/ies responsible for project implementation (beneficiary/ies)	Name and contact details of the grant beneficiary/ies	In the case of a PPP project where a private partner will be selected only after approval of the operation and which will be the beneficiary, information provided will be the indication of the public body initiating the operation (i.e. the procuring authority)
A.4. Capacity of the body responsible for project implementation	Information on the beneficiary's technical, legal, financial and administrative capacity	In the case of a PPP project where the private partner has not yet been selected, information provided will be: <ul style="list-style-type: none"> – the minimum criteria for pre-qualification and justification for these criteria – arrangements for the preparation, monitoring and management of the PPP project
B.3.1 Project description	Information required includes a map identifying the project area, geo-referenced data and the main project components with their individual total cost estimates	In the case of a PPP where the private partner has not yet been selected and is responsible for securing the location, the applicant does not need to provide the map identifying the project area.

Section	Standard information	Information in the case of a PPP
D.2.2 Options analysis	Criteria considered in selecting the best solution (with ranking of their importance and method of evaluation)	This section should include the rationale for the selection of the PPP procurement method, including a VfM analysis using a reasonable public sector comparator
E.3.3 Risk assessment	Summary of the risk assessment including a list of risks to which the project is exposed, the risk matrix, proposed risk mitigation strategy and the body responsible for mitigating the main risks such as cost overruns, time delays, demand shortfalls; special attention should be given to environmental risks, climate change-related risks, and other natural disaster-related risks	Information to be provided is the risk matrix as defined under the PPP arrangements (if the operation has already been tendered) or the intended risk allocation under the PPP arrangements (if the operation has not yet been tendered)

Other indications on how to adapt the standard requirements of the Major Project assessment, in order to take into account the specific features of PPPs, can also be found in Annex III to the CBA IR, providing for the methodology for the CBA of Major Projects (see, in particular, Sections 2.1.4 and 2.2.3 of Annex III).

It should be noted that the CBA methodology set out in the CBA IR is complemented by the broader Guide to Cost-Benefit Analysis of Investment Projects published by the Commission in December 2014.

9.2.2 Assessment of grant applications

Following preparation, the application for the grant can either be (i) reviewed directly by the Commission or (ii) assessed by independent experts who will carry out an IQR, with subsequent notification to, and no-objection from, the Commission. It is up to the Member State to decide between the two application options.

In the first option:¹⁰³

- information on the project selected by the Managing Authority can be submitted directly to the Commission on the basis of which the Commission will carry out its own appraisal; and
- the Commission will adopt its Decision no later than three months from the date of submission of the information.

In the second option:¹⁰⁴

- the independent experts will assess the information¹⁰⁵ provided on the Major Project. The Commission has indicated JASPERS as an appropriate body to

¹⁰³ See CPR, Article 102 (1).

¹⁰⁴ See CPR, Article 102 (2).

undertake the IQR; Member States however can appoint different independent experts, in agreement with the Commission;¹⁰⁵

- where the Major Project has received a positive appraisal, the Managing Authority may then proceed with the selection of the Major Project within the OP but must also notify the Commission; and
- the grant is then deemed to be approved by the Commission, in the absence of a Decision by the Commission to refuse the grant within three months from the date of the notification by the Managing Authority. The CPR also specifies that a refusal by the Commission can only be issued when '*significant weaknesses in the Independent Quality Review*' have been identified.

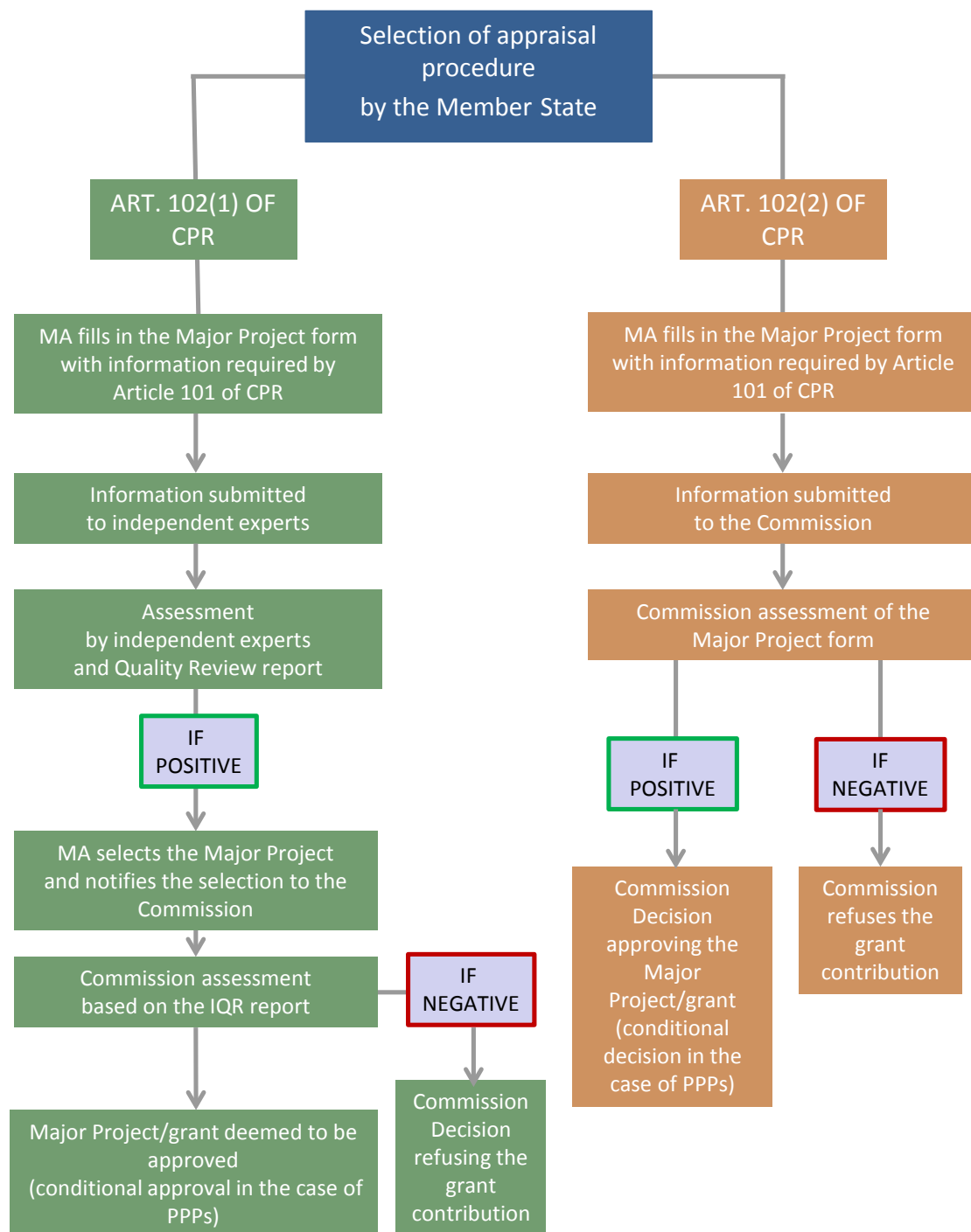
In both cases, the Commission's approval (or non-objection) is also conditional on the PPP agreement being signed within three years of the initial approval (a further two-year extension, but no more, may be granted in certain circumstances).

Figure 9 summarises the roles and responsibilities in the appraisal and approval process for a Major Project.

¹⁰⁵ The methodology for the IQR by independent experts is set out in the RGDR, Articles 22-23 and Annex II.

¹⁰⁶ See CPR, Article 101.

Figure 9 – Major Projects appraisal and approval process



10 Getting technical support

In order to promote the preparation and implementation of a Blended Project on a sound economic and technical basis, the use of expert advice at an early stage is strongly recommended. A range of Commission-funded initiatives can provide access to technical assistance and independent experts. This can support procuring authorities and Managing Authorities with guidance and clarity on the analysis and preparation of projects supported by ESI Funds.

The following are some examples of sources of support available at EU level for preparing Blended Projects that procuring and Managing Authorities should be aware of. This is not exhaustive and further forms of support may also be available at national levels.

10.1 JASPERS

Managing Authorities requiring technical assistance themselves, or for prospective beneficiaries, can apply to JASPERS. JASPERS is a technical assistance partnership between the Commission (DG REGIO), the EIB and the EBRD and acts as an instrument of EU Regional Policy. JASPERS is part of EIB's Advisory Services.

JASPERS provides independent advice to Managing Authorities in beneficiary countries to help prepare Major Projects for co-funding by EU Structural and/or Cohesion Funds. Assistance may cover:

- (i) *strategic support* - support to the formulation of strategies, identification of project pipelines and preparation of action plans and new OPs;
- (ii) *project preparation support* - from identification to submission of the EU grant application;¹⁰⁷
- (iii) *targeted support* - to help with specific project implementation issues;
- (iv) *horizontal assignments* - methodological papers and guidelines; and
- (v) *capacity building* - provision of external support teams, as 'embedded' experts, preparation of guidance documents and training.

With the new option for the approval of Major Projects involving appraisal by independent experts (see Chapter 9), the IQR is a recent task assigned to JASPERS by the Commission. The JASPERS quality review replicates the Commission procedure, consisting of an evaluation of strategic, technical, economic and financial aspects of a Major Project as well as the assessment of a Major Project's compliance with EU policies and legislation.

JASPERS' website (<http://www.jaspers-europa-info.org/>) provides more detailed information on its activities and how Managing Authorities can access its support.

¹⁰⁷ JASPERS project-related activities include, normally: review of terms of reference, concept studies, methodological approaches, interim reports, draft feasibility studies, environmental impact assessments, application documents both at draft and final stage and identification of areas for improvement to enhance the quality of the project.

10.2 EPEC

The European PPP Expertise Centre (EPEC) is a public sector membership-based expertise centre of the EIB involving, amongst others the Commission, EU Member States and (some) Candidate Countries. EPEC's mission is to help its Members (typically central PPP Units¹⁰⁸) strengthen their capacity to design and implement sound PPPs, mainly through sharing experience and expertise, analysis and best practice and by providing policy and upstream project support. EPEC is part of the EIB's Advisory Services.

With respect to Blended Projects, in addition to providing feedback from its Members to the Commission on the development of the recent regulations for Blended Projects, its stock-take of Blended Projects and case studies, EPEC will continue to help its Members and related public sector stakeholders gain awareness of the challenges inherent in blending PPPs with EU grants.¹⁰⁹ Also, EPEC will work with JASPERS to support Managing Authorities and potential EU grant beneficiaries in EU Member States in the preparation and implementation of Blended Projects.

EPEC's web site (www.eib.org/epec/) provides more detailed information on its activities, extensive PPP guidance materials and PPP market information.

10.3 The Connecting Europe Facility

Although this guidance note does not cover the specific separate regulations that govern the use of EU support through the CEF programme, it is worth highlighting that the CEF is another potential source of support for project preparation. The CEF provides financial support to part-fund preparation studies (as well as co-funding support for the investment costs of projects themselves) for key projects within the CEF framework of the trans-European networks (TEN) policy in the sectors of transport, energy and telecommunications.

Funding support for project preparatory studies, including projects considering the use of PPP procurement, can be accessed through regular annual calls for proposals, managed by INEA, the executing agency for CEF. Projects need to fall within the mandate of the CEF programme.¹¹⁰ Project proposals are normally submitted by one or more Member States. Member States also have the possibility to use support from JASPERS for CEF transport project preparation. With the agreement of the relevant Member States, proposals may be submitted by international organisations, joint undertakings or public or private undertakings or bodies established in Member States. As with grants from ESI Funds, the CEF has pre-defined co-funding rates per sector. For example, in the transport sector, the

¹⁰⁸ PPP Units (sometimes also referred to as 'agencies' or 'task forces') can serve a wide variety of purposes. A PPP Unit broadly refers to a unit that operates across sectors and projects at either a national or subnational/state/municipal government level. In this context, such a PPP Unit may be a division within a cross-sectoral ministry, established as a separate agency or an incorporated entity that is at least partly publicly owned. See [Establishing and Reforming PPP Units](#), EPEC report, August 2014.

¹⁰⁹ See '[Using EU Funds in PPPs - explaining the how and starting the discussion on the future](#)', EPEC report, May 2011.

¹¹⁰ CEF supports trans-European networks and infrastructure in the sectors of transport, telecommunications and energy. For more information, see the Regulation establishing the [Connecting Europe Facility](#).

rates vary according to whether the proposal involves studies (50% co-funding) or works.¹¹¹ It is possible to use CEF grants for the studies phase of a project and then undertake the investment phase using other ESI Fund sources of support. Further details on the CEF are available on the CEF website: (<https://ec.europa.eu/inea/en/connecting-europe-facility>).

¹¹¹ Co-funding for works varies between 20% and 50% depending on the sector and the nature of the project in transport and energy sectors, and can go up to 75% for projects in the telecommunications sector – see Article 10 of Regulation (EU) No 1316/2013, establishing CEF.

11 Conclusion

The revised regulations for the current programming period represent a considerable improvement in the terms and application of EU funding support for Blended Projects. PPPs are now explicitly recognised as a form of project delivery that can access grants from ESI Funds and the regulations are better tailored to the requirements of PPPs. One important development has been to allow such grants to support long-term performance-based payment mechanisms that are core to many forms of PPPs. Other areas of improvement include the availability of alternative and simpler ways to determine the grant amount for revenue-generating projects and the ability to obtain a grant approval ahead of identifying the private partner. These measures may both speed up the overall blending process and remove risks for procuring authorities to backstop grant awards.

The resources and time needed to prepare projects and grant applications properly should not be underestimated. The preparation requirements for a PPP project can reinforce those for a well-prepared grant application helping to improving the chances of successful grant award. ESI Funds may be accessed to help support the costs of project preparation. Technical sources of support such as JASPERS and EPEC are also readily available. It is clear that procuring authorities and Managing Authorities need to work closely together and from an early stage on the preparation of Blended Projects. Given the relevance of Managing Authorities in the grant application process, this is especially important where they may not be so familiar with the processes involved in preparing and implementing a PPP.

This guidance note should be treated as work in progress. At the time of its preparation, EPEC was not aware of any Blended Project concluded under the new regulations for the 2014-2020 programming period. However, as and when this takes place, EPEC is keen to help disseminate the practical lessons learnt from the experience and update this guidance note accordingly.

Annex I – Blended Project illustration case calculation tables

In this Annex, the reader will find the calculation tables for the Blended Project illustration case referred to in Chapter 8. The calculation model has been developed by EPEC solely for the purpose of illustration.

Table 1 – Investment inputs (2016-2025)

Year	Total	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Investment Inputs											
Road Construction Costs (in EURk)	450,000	450,000	-	-	135,000	180,000	135,000	-	-	-	-
Other Investments											
Planning/Design costs	10,000	7,000	3,000								
Land purchase	90,000		50,000	40,000							
Other	5,000	2,000	3,000								
Total Investment Costs	555,000	9,000	56,000	175,000	180,000	135,000	-	-	-	-	-
Long Term Heavy Maintenance (in EURk)											
Cost/km	1,500										
in ... th year of operation	3	45,000	-	-	-	-	-	-	45,000	-	-
	10	45,000	-	-	-	-	-	-	-	-	-
	15	45,000	-	-	-	-	-	-	-	-	-
		135,000	-	-	-	-	-	-	45,000	-	-
Total Investment Costs incl Heavy Maintenance	690,000	9,000	56,000	175,000	180,000	135,000	-	-	45,000	-	-

Table 1 cont. – Investment inputs (2026-2036)

Year	Total	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036
Investment Inputs												
Road Construction Costs (in EURk)	450,000	450,000	-	-	-	-	-	-	-	-	-	-
Other Investments												
Planning/Design costs	10,000											
Land purchase	90,000											
Other	5,000											
Total Investment Costs	555,000	-	-	-	-	-	-	-	-	-	-	-
Long Term Heavy Maintenance (in EURk)												
Cost/km	1,500											
in ... th year of operation	3	45,000	-	-	-	-	-	-	-	-	-	-
	10	45,000	-	-	-	45,000	-	-	-	-	-	-
	15	45,000	-	-	-	-	-	-	-	-	45,000	-
		135,000	-	-	-	45,000	-	-	-	-	45,000	-
Total Investment Costs incl Heavy Maintenance	690,000	-	-	-	-	45,000	-	-	-	-	45,000	-

Table 1 cont. – Investment inputs (2037-2045)

Year	Total	2037	2038	2039	2040	2041	2042	2043	2044	2045
Investment Inputs										
Road Construction Costs (in EURk)	450,000	450,000	-	-	-	-	-	-	-	-
Other Investments										
Planning/Design costs		10,000								
Land purchase		90,000								
Other		5,000								
Total Investment Costs		555,000	-	-	-	-	-	-	-	-
Long Term Heavy Maintenance (in EURk)										
Cost/km	1,500									
in ... th year of operation	3	45,000	-	-	-	-	-	-	-	-
	10	45,000	-	-	-	-	-	-	-	-
	15	45,000	-	-	-	-	-	-	-	-
		135,000	-	-	-	-	-	-	-	-
Total Investment Costs incl Heavy Maintenance		690,000	-	-	-	-	-	-	-	-

Table 2 – Funding gap calculation (2016-2025)

Year	Total	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Toll Revenues	625,461	-	-	-	-	-	20,805	21,117	21,434	21,755	22,082
Residual Value	-	-	-	-	-	-	-	-	-	-	-
Total Investment Costs	(690,000)	(9,000)	(56,000)	(175,000)	(180,000)	(135,000)	-	-	(45,000)	-	-
<i>Investment costs</i>	<i>(555,000)</i>	<i>(9,000)</i>	<i>(56,000)</i>	<i>(175,000)</i>	<i>(180,000)</i>	<i>(135,000)</i>	-	-	-	-	-
<i>Heavy maintenance costs</i>	<i>(135,000)</i>	-	-	-	-	-	-	-	(45,000)	-	-
Operating Costs	(112,500)	-	-	-	-	-	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)
<i>Periodic Maintenance</i>	<i>(112,500)</i>	-	-	-	-	-	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>
Derivation of the Funding Gap Rate											
Discounted Total Investment Costs (in EURk)	(680,393)	(10,529)	(62,992)	(189,280)	(187,200)	(135,000)	-	-	(40,005)	-	-
Discounted Net Revenues	246,927	-	-	-	-	-	12,199	11,968	11,740	11,516	11,294
<i>Discounted Residual Value (in EURk)</i>	-	-	-	-	-	-	-	-	-	-	-
<i>Discounted Toll Revenues (in EURk) - pro rata</i>	<i>317,226</i>	-	-	-	-	-	<i>16,526</i>	<i>16,128</i>	<i>15,741</i>	<i>15,362</i>	<i>14,993</i>
<i>Discounted Operating Costs (Periodic Maintenance)</i>	<i>(70,299)</i>	-	-	-	-	-	<i>(4,327)</i>	<i>(4,161)</i>	<i>(4,000)</i>	<i>(3,847)</i>	<i>(3,699)</i>
Funding Gap (in EURk)	(433,467)	(10,529)	(62,992)	(189,280)	(187,200)	(135,000)	12,199	11,968	(28,265)	11,516	11,294
Funding Gap Rate	63.71%										

Table 2 cont. – Funding gap calculation (2026-2036)

Year	Total	2026	2027	2028	2029	2030	2031	2032	2033	2034	2035	2036
Toll Revenues	625,461	22,413	22,749	23,090	23,437	23,788	24,145	24,507	24,875	25,248	25,627	26,011
Residual Value	-	-	-	-	-	-	-	-	-	-	-	-
Total Investment Costs	(690,000)	-	-	-	-	(45,000)	-	-	-	-	(45,000)	-
<i>Investment costs</i>	<i>(555,000)</i>	-	-	-	-	-	-	-	-	-	-	-
<i>Heavy maintenance costs</i>	<i>(135,000)</i>	-	-	-	-	(45,000)	-	-	-	-	(45,000)	-
Operating Costs	(112,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)
<i>Periodic Maintenance</i>	<i>(112,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>
Derivation of the Funding Gap Rate												
Discounted Total Investment Costs (in EURk)	(680,393)	-	-	-	-	(30,400)	-	-	-	-	(24,987)	-
Discounted Net Revenues	246,927	11,076	10,861	10,650	10,441	10,236	10,033	9,834	9,638	9,446	9,256	9,070
<i>Discounted Residual Value (in EURk)</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Discounted Toll Revenues (in EURk) - pro rata</i>	<i>317,226</i>	<i>14,633</i>	<i>14,281</i>	<i>13,938</i>	<i>13,603</i>	<i>13,276</i>	<i>12,956</i>	<i>12,645</i>	<i>12,341</i>	<i>12,044</i>	<i>11,755</i>	<i>11,472</i>
<i>Discounted Operating Costs (Periodic Maintenance)</i>	<i>(70,299)</i>	<i>(3,556)</i>	<i>(3,420)</i>	<i>(3,288)</i>	<i>(3,162)</i>	<i>(3,040)</i>	<i>(2,923)</i>	<i>(2,811)</i>	<i>(2,703)</i>	<i>(2,599)</i>	<i>(2,499)</i>	<i>(2,403)</i>
Funding Gap (in EURk)	(433,467)	11,076	10,861	10,650	10,441	(20,165)	10,033	9,834	9,638	9,446	(15,731)	9,070
Funding Gap Rate	63.71%											

Table 2 cont. - Funding gap calculation (2037-2045)

Year	Total	2037	2038	2039	2040	2041	2042	2043	2044	2045
Toll Revenues	625,461	26,401	26,797	27,199	27,607	28,021	28,442	28,868	29,301	29,741
Residual Value	-	-	-	-	-	-	-	-	-	-
Total Investment Costs	(690,000)	-	-	-	-	-	-	-	-	-
<i>Investment costs</i>	<i>(555,000)</i>	-	-	-	-	-	-	-	-	-
<i>Heavy maintenance costs</i>	<i>(135,000)</i>	-	-	-	-	-	-	-	-	-
Operating Costs	(112,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)	(4,500)
<i>Periodic Maintenance</i>	<i>(112,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>	<i>(4,500)</i>
Derivation of the Funding Gap Rate										
Discounted Total Investment Costs (in EURk)	(680,393)	-	-	-	-	-	-	-	-	-
Discounted Net Revenues	246,927	8,886	8,706	8,529	8,355	8,183	8,015	7,850	9,676	9,468
<i>Discounted Residual Value (in EURk)</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>	<i>-</i>
<i>Discounted Toll Revenues (in EURk) - pro rata</i>	<i>317,226</i>	<i>11,197</i>	<i>10,927</i>	<i>10,665</i>	<i>10,408</i>	<i>10,158</i>	<i>9,914</i>	<i>9,676</i>	<i>11,431</i>	<i>11,156</i>
<i>Discounted Operating Costs (Periodic Maintenance)</i>	<i>(70,299)</i>	<i>(2,310)</i>	<i>(2,221)</i>	<i>(2,136)</i>	<i>(2,054)</i>	<i>(1,975)</i>	<i>(1,899)</i>	<i>(1,826)</i>	<i>(1,756)</i>	<i>(1,688)</i>
Funding Gap (in EURk)	(433,467)	8,886	8,706	8,529	8,355	8,183	8,015	7,850	9,676	9,468
Funding Gap Rate	63.71%									

Table 3 – Standard funding gap calculation

Standard funding gap method	
Eligible costs (not discounted)	570,000
Funding gap rate (in %)	63.71%
Decisional amount (EC*FR)	(363,137)
Co-financing rate	75%
Union contribution	(272,353)

Table 4 – Application of the relevant flat rate

Flat rate method	
Eligible costs (not discounted)	570,000
Flat rate for Roads as specified in CPR Annex V	30%
Decisional Amount [EC*(1-FR)]	(399,000)
Co-financing rate	75%
Union contribution	(299,250)

Annex II – Worked example of the impact of change in discount rate

The RGDR allows for the possibility to apply a discount rate other than the suggested 4% benchmark in the case of a PPP. In the calculation of the grant amount based on the discounted net revenue method, the results of the calculation can vary significantly depending on the value of the discount rate applied.

A practical example can give an idea of the sensitivity of the funding gap and grant amount value to the level of the discount rate used in the calculation. In this example, a 6% discount rate is applied to the values of revenues and costs estimated for the Blended Project illustration case.

Following the same calculation as used in the theoretical Blended Project illustration case in Chapter 8, the first step is the determination of the discounted net revenue. This will be the difference between discounted revenues and discounted operating costs (keeping the assumption of a zero residual value). The resulting discounted net revenue is, in this case, lower than the amount of the Blended Project illustration case as a consequence of the higher discount rate.

$$\begin{array}{rclclcl}
 \text{Disc. net revenue} & = & \text{Disc. revenue} & - & \text{Disc. operating costs} & + & \text{Disc. res. value} \\
 197 & = & 255 & - & 58 & + & 0
 \end{array}$$

One can thus expect a higher value for the funding gap, resulting from the difference between the discounted investment costs and the discounted net revenue:

$$\begin{array}{rclcl}
 \text{Funding gap} & = & \text{Disc. investment costs} & - & \text{Discounted net revenue} \\
 484 & = & 682 & - & 198
 \end{array}$$

This translates into a higher *funding gap rate* than in the Blended Project illustration case:

$$\begin{array}{rclcl}
 \text{Funding gap rate} & = & 1 & - & \frac{\text{Discounted net revenue}}{\text{Discounted investment costs}} \\
 71.01\% & = & 1 & - & \frac{197}{682}
 \end{array}$$

The funding gap rate is then applied to the eligible costs which are *not discounted* in order to derive the 'decisional amount':

$$\begin{array}{rclcl}
 \text{Decisional amount} & = & \text{Eligible costs} & \times & \text{Calculated funding gap rate} \\
 405 & = & 570 & \times & 71.01\%
 \end{array}$$

Based on a 75% maximum co-financing rate, the grant amount for the Project will be EUR 304m:

$$\begin{array}{rcccc} \text{EU grant} & = & \text{Decisional amount} & \times & \text{Maximum co-financing rate for} \\ & & & & \text{the priority axis} \\ 304 & = & 405 & \times & 75\% \end{array}$$

This example shows that an increase in the discount rate by 2 percentage points could lead to an increase in the EU grant amount of 11% or some EUR 30m when compared with the Blended Project illustration case.

Annex III – Main changes in the rules for Major Projects compared to the 2007-2013 programming period¹¹²

Item	2007-2013 (Regulation 1083/2006)	2014-2020 (CPR)
Threshold	EUR 50m for all projects (based on total cost) – Article 39	EUR 50m (general rule) and EUR 75m (transport) - based on total eligible cost – Article 100
Identification of Major Projects in OPs	Indicative – Article 37	Compulsory and comprehensive – Article 102(5)
Appraisal of Major Project documents	<p>Full assessment by the Commission – Articles 40 and 41</p> <p>Assessment process: Managing Authorities submitted a Major Project application to the Commission. The Commission appraised the application based on the information set out in Article 40, if necessary, in consultation with external experts (including the EIB)</p> <p>Decision: the Commission adopted a Decision within three months. In case a project was non-compliant with the requirements of the regulation, the Managing Authority was requested to withdraw the application. Alternatively, the Commission may issue a negative Decision (Article 41)</p>	<p>Two possibilities – Articles 102 (1) and 102 (2)</p> <p>1. Notification: quality check by IQR before the submission of the Major Project to the Commission</p> <p>2. Commission's appraisal – as in the 2007-2013 programming period</p> <p>Simplified notification procedure under Article 103 for phased projects.</p>
Validity of Commission approval	A Commission Decision on a Major Project was valid for the entire programming period (Article 41)	The approval by the Commission will be conditional on the first works contract (or PPP agreement) being concluded within three years of the date of the approval of the project by the Commission. The deadline can be extended by a duly justified request of a Member State by no more than two years – Article 102(3)
Revenue-generating operations	<p>One option (Article 55):</p> <ul style="list-style-type: none"> - Funding gap (i.e. calculation of discounted net revenues and investment costs) 	<p>Three alternatives (Article 61):</p> <ul style="list-style-type: none"> - Funding gap - Flat rate - Decreased co-financing rate
Payment application	Expenditure relating to Major Projects could be included in payment applications before the project was approved by a Decision of the Commission (Article 56)	Expenditure relating to Major Projects can be included in payment applications only after the Managing Authority notifies the Major Project Decision to the Commission or following the submission to the Commission of the Major Project form for approval – Article 102(6)

¹¹² See also the DG REGIO presentation '[Major Projects in the 2014-2020 programming period](#)'.






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