

## III

*(Preparatory acts)*

## COURT OF AUDITORS

**OPINION No 7/2020***(pursuant to Article 287(4), TFEU)***accompanying the Commission's report on the implementation of the European Fund for Sustainable Development (COM(2020) 224 final)***(2020/C 353/01)***CONTENTS**

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THE COURT OF AUDITORS OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 287(4)(2) thereof,

Having regard to Regulation (EU, Euratom) 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union <sup>(1)</sup>,

Having regard to Regulation (EU) 2017/1601 of the European Parliament and of the Council of 26 September 2017 establishing the European Fund for Sustainable Development (EFSD), the EFSD Guarantee and the EFSD Guarantee Fund <sup>(2)</sup> ('the EFSD Regulation'), and in particular Article 17(1) and 17(2) thereof,

Having regard to the Commission's report to the European Parliament and the Council on the implementation of the European Fund for Sustainable Development <sup>(3)</sup> pursuant to Article 17(1) of the EFSD Regulation,

Whereas, pursuant to Article 17(1) and (2) of the EFSD Regulation, the Commission's report to the European Parliament and the Council on the evaluation of the initial functioning of the EFSD, its management and its effective contribution to the purpose and the objectives of the EFSD Regulation as well as the Commission's evaluation report on the EFSD Guarantee Fund, shall be accompanied by an Opinion of the Court of Auditors,

HAS ADOPTED THE FOLLOWING OPINION:

## INTRODUCTION

### Scope and timing of the Court's Opinion

1. On 28 May 2020, the Commission submitted a legislative proposal <sup>(4)</sup> to amend the existing EFSD Regulation, with a view to extending its duration and geographic scope and increasing the amount of the EU guarantee provided under it. On 2 June 2020, the Commission published a report on the implementation of the EFSD pursuant to Article 17(1) of the EFSD Regulation ('the implementation report') <sup>(5)</sup>. This report was accompanied by an independent implementation report ('the external assessment report') on the EFSD and the EFSD Guarantee Fund, dated 14 January 2020, which the Commission published on its website on 4 June 2020 <sup>(6)</sup>. In its special meeting of 17, 18, 19, 20 and 21 July 2020, the European Council decided that there would be no change to the 2014-2020 multiannual financial framework (MFF) <sup>(7)</sup>. In response to these developments, we decided to focus our Opinion on the implementation report, without referring further to the Commission's legislative proposal.

### The implementation report

2. Article 17(1) of the EFSD Regulation requires the Commission to evaluate 'the initial functioning of the EFSD, its management and its effective contribution to the purpose and objectives of [the] Regulation'. Referring to this regulatory provision, the Commission's implementation report describes itself as an 'initial assessment of the main evaluation criteria of relevance, efficiency, effectiveness, coherence and value added'.

### Our Opinion

3. This Opinion is structured around the following considerations:

- whether the implementation report fulfils the requirements of Article 17(1) of the EFSD Regulation,
- whether the implementation report fulfils the purpose of assessing the initial functioning of the EFSD, its management and its effectiveness,
- whether the EFSD has a comprehensive monitoring and evaluation framework.

4. Our Opinion has not been drawn up based on the same procedures that we would use when writing a special report.

<sup>(1)</sup> OJ L 193, 30.7.2018, p. 1.

<sup>(2)</sup> OJ L 249, 27.9.2017, p. 1 (referred to as 'the EFSD Regulation').

<sup>(3)</sup> COM(2020)224 final of 2.6.2020 (referred to as 'the implementation report').

<sup>(4)</sup> COM(2020)407 final of 28.5.2020.

<sup>(5)</sup> The Commission submitted its report to us on the same day.

<sup>(6)</sup> External assessment report with the following title: 'Implementation report of the EFSD and the EFSD Guarantee Fund, final report, 14 January 2020' (referred to hereafter as 'the external assessment report').

<sup>(7)</sup> Special meeting of the European Council (17, 18, 19, 20 and 21 July 2020) – Conclusions, EUCO 10/20, 21 July 2020, point A.31.

## THE IMPLEMENTATION REPORT DOES NOT FULFIL SOME BASIC REQUIREMENTS

### Criteria

5. Article 17(1) of the EFSD Regulation requires the Commission to evaluate the initial functioning of the EFSD, its management and its effective contribution to the purpose and objectives of this regulation by 31 December 2019, and to submit its evaluation report to the European Parliament and to the Council, containing an independent external evaluation of the application of the Regulation.

6. The better regulation guidelines provide that evaluations should follow a clearly defined, robust methodology intended to produce objective findings. As a minimum, evaluations must assess effectiveness, efficiency, relevance, coherence and EU added value, or contain an explanation of why this has not been done <sup>(8)</sup>.

### The implementation report results from a limited assessment rather than a full evaluation

7. While the implementation report refers to Article 17(1) of the EFSD Regulation, the Commission stops short of describing it as an evaluation report. The implementation report provides the Commission's assessment of the initial functioning of the EFSD, its management and its contribution to the purpose and objectives of the EFSD Regulation. It is based on an independent assessment carried out by external consultants.

8. The difference between an evaluation and an assessment is described as follows in the Commission's better regulation guidelines: 'Evaluation goes beyond an assessment of what has happened; it considers why something has occurred (the role of the EU intervention) and, if possible, how much has changed as a consequence. It should look at the wider perspective and provide an independent and objective judgement of the situation based on the evidence available' <sup>(9)</sup>.

9. The external assessment report explains that, although the methodology and structure used in the assessment followed the approach used for evaluations, it should be considered as an assessment and not an evaluation of the EFSD. This is because 'some EFSD activity [was] barely underway', and because 'an assessment needs on occasion to be more judgemental and indicative than would normally be the case for an evaluation' <sup>(10)</sup>.

10. Besides this issue, the consultants' external assessment report noted that their work was subject to several limitations:

- the assignment was undertaken with a small team and limited budget,
- there were no visits to EU Delegations or to projects receiving EFSD support, but phone interviews and consultations with staff from EU Delegations,
- few of the projects approved for blending grants had made significant progress in implementation and, at the end of the assignment, 25 of the 28 approved guarantee programmes remained unsigned and in a draft phase.

Because of these limitations, there was 'heavy reliance on interviews' and, on occasion, hard evidence was scarce <sup>(11)</sup>.

### The EFSD's business processes have not been reviewed

11. The external assessment report notes that the operational blueprint of the EFSD requires a more detailed review than was possible in the assessment report. Consequently, it recommends that a review be carried out, covering the business processes, roles and responsibilities of HQ and EU Delegations, their capacity, staff skills and training, and their knowledge management <sup>(12)</sup>. The Commission's implementation report welcomes the external assessment's recommendation that a review of the EFSD's business processes be carried out, and suggests that this will be covered by the ongoing review of the new financial architecture to be put in place for the EFSD+, the proposed successor to the EFSD <sup>(13)</sup>.

<sup>(8)</sup> Commission staff working document 'Better regulation guidelines' (SWD(2017) 350), July 2017 – Better regulation: guidelines and toolbox, see 'Guidelines on evaluation (including fitness checks)', Chapter VI.

<sup>(9)</sup> Better regulation: guidelines and toolbox, see 'Guidelines on evaluation (including fitness checks) and key requirements', Chapter VI, Introduction.

<sup>(10)</sup> External assessment report, Executive summary.

<sup>(11)</sup> External assessment report, Introduction.

<sup>(12)</sup> External assessment report, Recommendation 6.

<sup>(13)</sup> In June 2018, the Commission made a proposal for a regulation establishing the Neighbourhood, Development and International Cooperation Instrument (NDICI) (COM(2018) 460 final). Under the terms of this proposal, the existing provisions on the European Fund for Sustainable Development, the External Lending Mandate and the Guarantee Fund for external actions would be merged and replaced by new 'EFSD+ budgetary guarantees and financial assistance to third countries'.

12. We consider that a review of EFSD's business processes is a key element in assessing the initial functioning and management of the EFSD, which is missing from the Implementation Report.

### **The implementation report was published late**

13. The scope of both the implementation report <sup>(14)</sup> and the external assessment covered the period from 1 January 2017 to the end of September 2019. A first version of the external assessment report was submitted to the Commission on 15 November 2019 <sup>(15)</sup>; the final report, dated 14 January 2020, was published on 4 June 2020 <sup>(16)</sup>.

14. The Commission's implementation report, which is based on the results of the external assessment, was published on 2 June 2020, eight months after the end of the period covered by the external assessment and five months after the deadline set in Article 17(1) of the EFSD Regulation for the Commission evaluation.

## **THE INITIAL FUNCTIONING OF THE EFSD, ITS MANAGEMENT AND ITS EFFECTIVENESS HAVE NOT BEEN FULLY ASSESSED**

### **Little information is available on additionality and aspects of effectiveness**

#### *Criteria*

15. The EFSD Regulation itself contains the following statements about the goals of the EFSD:

'The purpose of the EFSD [...] shall be to support investments and increased access to financing, primarily in Africa and the European Neighbourhood, in order to foster sustainable and inclusive economic and social development and promote the socioeconomic resilience of partner countries [...] with a particular focus on sustainable and inclusive growth, on the creation of decent jobs, on gender equality and the empowerment of women and young people, and on socioeconomic sectors and micro, small and medium-sized enterprises, while maximising additionality, delivering innovative products and crowding in private sector funds' <sup>(17)</sup>.

"Additionality" means the principle ensuring that the EFSD Guarantee support contributes to sustainable development by operations which could not have been carried out without the EFSD Guarantee, or which achieve positive results above and beyond what could have been achieved without it. Additionality also means crowding in private sector funding and addressing market failures or sub-optimal investment situations as well as improving the quality, sustainability, impact or scale of an investment. The principle also ensures that EFSD Guarantee operations do not replace the support of a Member State, private funding or another Union or international financial intervention, and avoid crowding out other public or private investments. (...) <sup>(18)</sup>.

'The EFSD shall be guided by the objectives of the Union's external action as set out in Article 21 TEU and of Union policy in the field of development cooperation as set out in Article 208 TFEU and the internationally agreed development effectiveness principles. The EFSD shall contribute to the achievement of the Sustainable Development Goals of the 2030 Agenda, in particular poverty eradication, and, where appropriate, to the implementation of the European Neighbourhood Policy, thus addressing specific socioeconomic root causes of migration and fostering sustainable reintegration of migrants returning to their countries of origin, and strengthening transit and host communities' <sup>(19)</sup>.

'The EFSD shall contribute to the implementation of the Paris Agreement by also targeting investments to sectors that advance climate change mitigation and adaptation' <sup>(20)</sup>.

16. In addition, the recitals of the EFSD Regulation state the following:

'[I]n order to fulfil the political commitments of the Union on climate action, renewable energy and resource efficiency, a minimum share of 28 % of the financing under the EFSD Guarantee should be devoted to investments relevant for those sectors' <sup>(21)</sup>.

<sup>(14)</sup> Implementation report, section 2.

<sup>(15)</sup> External assessment report, Introduction.

<sup>(16)</sup> See footnote 5.

<sup>(17)</sup> Article 3(1) of the EFSD Regulation.

<sup>(18)</sup> Article 2(5) of the EFSD Regulation.

<sup>(19)</sup> Article 3(2) of the EFSD Regulation.

<sup>(20)</sup> Article 3(3) of the EFSD Regulation.

<sup>(21)</sup> Recital 10 of the EFSD Regulation.

*The EFSD's capacity to mobilise additional investments could be overestimated*

17. In our Opinion No 2/2016, we noted that it is not easy to determine the amounts mobilised by public investments<sup>(22)</sup>. The OECD Development Assistance Committee has proposed a method<sup>(23)</sup><sup>(24)</sup> for isolating the contribution of public investments in mobilising additional funds. The key elements are summarised below:

- If public funding is used to guarantee a loan which finances a project, it is the amount of the guaranteed loan which is deemed to have been mobilised by the use of public funding. Any additional financing, beside the loan, is not deemed to have been leveraged by the guarantee.
- If public funding is used as part of a loan extended by several parties – a syndicated loan – the contributions of each lender are taken into account on a pro-rata basis. In other words, instead of considering that the entire mobilised amount is due to the public funding, the contribution of the other parties is recognised.
- In equity investments, the amount deemed to have been mobilised by public funding excludes any prior investments. Where multiple public bodies have participated in an investment, the amounts mobilised from the private sector are attributable to each of these bodies on a pro-rata basis.

18. The Financial Regulation defines the leverage effect as 'the amount of reimbursable financing provided to eligible final recipients divided by the amount of the Union contribution'<sup>(25)</sup>. In our special report No 19/2016, we noted that the indicator of additional investment mobilised by the financial instruments is liable to be overstated, as not all sources of finance attracted by a project are the result of the EU's contribution<sup>(26)</sup>. In our special report No 16/2014, we observed that 'for 15 of the 30 [blending grant] projects examined by the Court, there was no convincing analysis to show that a grant was necessary in order for the loan to be contracted [...]. Depending on the case concerned, there were indications that the investments would also have been made without the grant'<sup>(27)</sup>.

19. The implementation report concludes that the EFSD is crowding in substantial amounts of other funding, including private co-financing<sup>(28)</sup>, and delivers 'financial additionality'<sup>(29)</sup>. The implementation report describes the extent to which the EFSD mobilises additional funds, referring to the EFSD's 'average financial leverage figure' calculated in the external assessment report. This figure is obtained by dividing the total amount of blending grants and guarantees approved under the EFSD by the total amount of investments from other sources, for all operations supported by the EFSD. On the basis of EFSD data as of September 2019, the external assessment estimated an average financial leverage figure of 10,04<sup>(30)</sup>. According to the implementation report, this 'demonstrate[s] the effectiveness of the EFSD model to attract more money'<sup>(31)</sup>.

20. We consider that the leverage figure featuring in the implementation report as an indicator of the EFSD's capacity to mobilise additional investments is insufficiently reliable, and could be overestimated. In particular, it is affected by the following issues:

- The estimation of the EFSD's leverage effect results from an over-optimistic calculation which assumes zero investment without the EFSD<sup>(32)</sup>.
- All of the data in the external assessment's calculation of the average financial leverage figure was provided by DG DEVCO<sup>(33)</sup>; it is unclear to what extent it was verified independently by the external assessment contractor.

<sup>(22)</sup> Opinion No 2/2016: 'EFSI: an early proposal to extend and expand', paragraph 47 (OJ C 465, 13.12.2016, p. 1).

<sup>(23)</sup> OECD, 'Methodologies to measure amounts mobilised from the private sector by official development finance interventions', DCD/DAC/STAT(2015)8, 24 February 2015.

<sup>(24)</sup> This methodology is currently being reviewed by the OECD.

<sup>(25)</sup> Article 2(38) of Financial Regulation (OJ L 193, 30.7.2018, p. 1).

<sup>(26)</sup> Special report No 19/2016: 'Implementing the EU budget through financial instruments – lessons to be learnt from the 2007-2013 programme period', paragraph 70 (OJ C 250, 9.7.2016, p. 2).

<sup>(27)</sup> Special report No 16/2014: 'The effectiveness of blending regional investment facility grants with financial institution loans to support EU external policies', paragraph 42 (OJ C 381, 28.10.2014, p. 13).

<sup>(28)</sup> Implementation report, section 5.2.

<sup>(29)</sup> Implementation report, Executive summary.

<sup>(30)</sup> External assessment report, section 3.1.

<sup>(31)</sup> Implementation report, section 5.2.

<sup>(32)</sup> External assessment report, section 3.2.

<sup>(33)</sup> External assessment report, footnote 29.

- While the external assessment report deems it ‘likely’ that the EFSD’s support catalysed the claimed amount of leverage, in the sense that the operations supported by the EFSD would not have happened without the EFSD’s support, it recognises that the counter-factual cannot be proven <sup>(34)</sup>.

*The implementation report lacks information on the EFSD’s performance in crowding in private sector funding*

21. Catalysing the investment of further funding from the private sector – ‘crowding in’ – is one of the EFSD’s key objectives. However, while the implementation report concludes that the EFSD is crowding in substantial amounts of additional funding, including private co-financing (see paragraphs 17 to 20), it does not contain any specific conclusions or information about the EFSD’s performance in terms of mobilising private-sector funds in particular.

22. The external assessment report provides more insight with regard to the EFSD’s performance in mobilising private-sector funds. The external assessment report refers to ‘pure’ private money in contrast to money from financial institutions which, according to the external assessment report, could be classified as private by virtue of these institutions’ major bond-issuing programmes on the capital markets. In particular, it notes that the proportion of ‘pure’ private money linked to blending grants tended to be relatively low. For example, in sub-Saharan Africa, it represented around 5-10 % of total other money <sup>(35)</sup>. The report also notes that guarantees could potentially mobilise much more ‘pure’ private money, although this remains a conjecture <sup>(36)</sup>. In this regard, it recommends that the private sector be broken down further into sub-segments, and that tailored risk-reduction packages be developed for specific investor groups <sup>(37)</sup>. In the implementation report, the Commission accepts these recommendations <sup>(38)</sup>.

*The implementation report’s conclusions on non-financial additionality and the EFSD’s performance in delivering innovative products are essentially based on predictions*

23. Referring to the external assessment report, the implementation report concludes that additionality at project level appears to be strong and qualitatively substantiated, but that it is rarely quantified <sup>(39)</sup>. However, more detailed information in the external assessment report indicates that this conclusion actually results from a survey of *ex-ante* information contained in a number of project sheets. On the basis of this survey, the external assessment report notes that, although most project sheets indicate a positive impact on many additionality criteria, which appears highly favourable, there seems to be some confusion between the additionality of projects themselves and the additionality of the EU’s contribution to them <sup>(40)</sup>.

24. Still referring to the external assessment report, the implementation report notes that, at policy level, there are examples where the EFSD has supported or reinforced a policy change <sup>(41)</sup>. But there is no solid evidence supporting such a conclusion. The conclusion appears to be based on a wording used in the external assessment report which does not in fact support that conclusion. The external assessment report states that ‘[t]here are some examples where policy additionality should also be achieved [...] i.e. where the project will lead to, or reinforce, or give expression to, a policy change’ <sup>(42)</sup>. But this is not evidence of policy changes occurring in reality as a result of the EFSD.

25. The implementation report also contains similarly unsubstantiated conclusions on the potential of the EFSD and, in particular, of its guarantees, to test and develop new financial products <sup>(43)</sup>. It does not otherwise explain or illustrate how this will be translated into practice.

26. The external assessment report notes that the EFSD is able to foster many forms of innovation at project level. It cites a number of examples of this <sup>(44)</sup>. However, it also notes that all these examples would also have been possible through the use of blending facilities before the EFSD came into existence <sup>(45)</sup>.

<sup>(34)</sup> External assessment report, section 3.1.

<sup>(35)</sup> In paragraph 39 of our special report No 16/2014, we observed that funding for projects that received support from the regional investment facilities was provided, in the main, by institutional development banks, while private sector lending had been low.

<sup>(36)</sup> External assessment report, section 3.1.

<sup>(37)</sup> External assessment report, Conclusions and recommendations.

<sup>(38)</sup> Implementation report, Conclusion and recommendations, Relevance.

<sup>(39)</sup> Implementation report, section 5.2.

<sup>(40)</sup> External assessment report, section 3.2.

<sup>(41)</sup> Implementation report, section 5.2.

<sup>(42)</sup> External assessment report, section 3.2.

<sup>(43)</sup> Implementation report, section 5.5.

<sup>(44)</sup> External assessment report, section 3.3.

<sup>(45)</sup> External assessment report, footnote 43.

*Since the EFSD is at an early stage of implementation, it is not possible to assess the contribution it has made to achieving the SDGs or to addressing the root causes of migration*

27. Among other things, the EFSD is aimed at contributing to the Sustainable Development Goals (SDGs). The implementation report concludes that the EFSD's approach is highly relevant in the 'new SDG-led global development finance model' and to the investment needs of the two regions concerned (sub-Saharan Africa and the EU Neighbourhood) <sup>(46)</sup>. It also concludes that the EFSD's policy focus and pipeline of projects are well aligned with SDG priorities and targets <sup>(47)</sup>. However, it does not provide any information with regard to any actual contribution made by the EFSD to the achievement of the SDGs. Also, the implementation report does not make any particular reference to poverty eradication.

28. The EFSD is also intended to contribute to addressing the specific socioeconomic root causes of migration, fostering the sustainable reintegration of migrants, and strengthening transit and host communities. The implementation report merely cites the first signed guarantee agreement as a good example of how the root causes of migration are being addressed (in that case, by addressing the high risks involved in lending to entrepreneurs in underserved communities in countries neighbouring the EU and in sub-Saharan Africa). It does not provide any other analysis or draw any further conclusions.

29. The EFSD is also intended to contribute to the implementation of the Paris Agreement by targeting investments to sectors that advance climate-change mitigation and adaptation. The implementation report does not provide any specific information about this. In particular, it does not provide any information about progress towards reaching the target set for the minimum proportion of EFSD Guarantee funding being used to finance projects devoted to climate action, renewable energy and resource efficiency (see paragraph 16).

30. The external assessment report notes that projects supported by the EFSD are not advanced enough to enable the EFSD's effectiveness to be measured, as blending projects still are in the early implementation stage and most guarantee programmes have not yet been signed <sup>(48)</sup>.

31. We note that the EFSD Regulation entered into force at the end of September 2017. The first guarantee agreement was signed 15 months later, in December 2018. In 2018, the External Investment Plan (EIP) operational board had identified 28 guarantee operations <sup>(49)</sup>. The EFSD Regulation's deadline for signing guarantee agreements is 31 December 2020 <sup>(50)</sup>. But by April 2020, only seven guarantee agreements had been signed with financial institutions <sup>(51)</sup>. According to the EFSD Regulation, once a guarantee agreement is signed, the eligible counterpart then has up to four years to conclude agreements with co-financing private sector partners, financial intermediaries or final beneficiaries <sup>(52)</sup>. In most cases, project implementation is then expected to take several years.

32. The EFSD is at too early a stage of implementation to enable the Commission to assess the contribution that the EFSD has made to achieving the SDGs or to addressing the root causes of migration.

*The implementation report does not explain the discrepancies between the EFSD Regulation deadlines and the actual pace of implementation*

33. The implementation report concludes that overall, the EIP and the EFSD are well on track, in spite of some challenges <sup>(53)</sup>, and that 'setting up a programme this large and innovative in such a timeline can be considered fast [...] compared to other similar mechanisms' <sup>(54)</sup>.

34. However, the current pace of implementation of the EFSD, in terms of concluding guarantee agreements with financial institutions, seems slow for the Commission to be able to sign all envisaged guarantee agreements before 31 December 2020, which is the deadline set in the EFSD Regulation (see paragraph 31) <sup>(55)</sup>. There is also a discrepancy between the requirement set in the EFSD Regulation for an evaluation to be drawn up by 31 December 2019 and the fact that such an evaluation could not be carried out due to the early stage of implementation of the EFSD (see paragraphs 7 to 10).

<sup>(46)</sup> Implementation report, Executive summary and section 5.1.

<sup>(47)</sup> Implementation report, Executive summary and section 5.2.

<sup>(48)</sup> External assessment report, footnote 28.

<sup>(49)</sup> External assessment report, Annex 3: Background on the EFSD and the EIP.

<sup>(50)</sup> Article 8(2) of the EFSD Regulation.

<sup>(51)</sup> Implementation report, Executive summary.

<sup>(52)</sup> Article 8(3) of the EFSD Regulation.

<sup>(53)</sup> Implementation report, Executive summary.

<sup>(54)</sup> Implementation report, Executive summary.

<sup>(55)</sup> Article 8(2) of the EFSD Regulation.

35. The external assessment report mentions some operational management issues raised during interviews with staff from EU delegations and financial institutions <sup>(56)</sup>, several of which have caused implementation delays:

- The Commission's 'horizontal' requirements' <sup>(57)</sup> caused a delay of up to 12 months in contracting investment programmes proposed to be covered by the EFSD Guarantee.
- Project cycles within the partner financial institutions and the Commission are not always synchronised, so projects may need to wait for a milestone to be reached in the partner institution before continuing, which causes delays.
- Five of the seven financial institutions which were interviewed brought up capacity issues – they said that there were too few banking and contract specialists at the Commission. As a result, certain processes took too long, especially for the new guarantee programmes.

### **Some issues related to the EFSD's functioning and management are insufficiently reflected in the implementation report**

#### *Criteria*

36. Article 17(1) of the EFSD Regulation provides that the Commission's evaluation report must contain an independent external evaluation of the application of the EFSD Regulation. The implementation report describes itself as being based on an independent external assessment, which was commissioned to provide an independent view of the initial stage of the implementation of the EFSD <sup>(58)</sup>.

37. The implementation report draws many of its conclusions from the external assessment report. However, we consider that the following issues raised by the external assessment report, which are significant in terms of assessing EFSD's initial functioning and management, are insufficiently reflected in the implementation report.

#### *Informal strategic orientation undermines transparency*

38. The EFSD's governance structure includes a Strategic Board. The Board was created 'to support the Commission in setting strategic guidance and overall investment goals, as well as in ensuring an appropriate and diversified geographical and thematic coverage for investment windows', and to 'support overall coordination, complementarity and coherence between the regional investment platforms, between the three pillars of the EIP, between the EIP and the Union's other efforts on migration and on the implementation of the 2030 Agenda' <sup>(59)</sup>.

39. Pursuant to Article 5 of the EFSD Regulation, the Strategic Board is composed of representatives of the Commission and of the High Representative, of all Member States and of the EIB, and is co-chaired by the Commission and the High Representative <sup>(60)</sup>. It must meet at least twice a year and, when possible, adopt opinions by consensus. Where consensus cannot be reached, voting rights apply. The voting rights are laid down in the rules of procedure of the Strategic Board. The minutes and agendas of the meetings of the Strategic Board must be made public <sup>(61)</sup>. The EFSD Regulation states that, '[d]uring the implementation period of the EFSD, the Strategic Board must, as soon as possible, adopt and publish guidelines setting out how conformity of EFSD operations with the objectives and eligibility criteria set out in Article 9 [of the EFSD Regulation] is to be ensured' <sup>(62)</sup>. These are referred to below as the 'eligibility guidelines'.

<sup>(56)</sup> External assessment report, section 4.2.

<sup>(57)</sup> These 'horizontal requirements' are a series of legal obligations to be fulfilled by financial institutions. For example, these concern the rights of the Court of Auditors, the Commission and the European Anti-Fraud Office's to access information held by EU budget beneficiaries, anti-money-laundering measures, non-cooperative jurisdictions, EU restrictive measures, international conventions, complaints mechanism, and reporting, publication, monitoring and evaluation obligations. See external assessment report, footnote 57.

<sup>(58)</sup> Implementation report, section 4.

<sup>(59)</sup> Recitals 16 and 17 of the EFSD Regulation.

<sup>(60)</sup> Article 5(4) of the EFSD Regulation.

<sup>(61)</sup> Article 5(5) of the EFSD Regulation.

<sup>(62)</sup> Article 5(7) of the EFSD Regulation.

40. Although the external assessment report concludes that the EFSD's governance structure facilitates transparent management and partnership and complies with the EFSD Regulation <sup>(63)</sup>, it notes that, judging from the available sets of minutes, only one meeting had taken place per year <sup>(64)</sup>.

41. In the course of our work, we noted that the adoption of eligibility guidelines was not mentioned in any of the Strategic Board meeting minutes <sup>(65)</sup>. When we asked Commission staff about these guidelines, they referred us to the following reference documents:

- guide to the External Investment Plan,
- strategic orientations as presented and discussed in the first Strategic Board meeting,
- presentation and adoption of areas on Investment windows in the first Strategic Board meeting,
- EFSD Guarantee Risk Guidelines presented to first Operational Board with a written opinion by the EIB as per Article 9(4) of the EFSD Regulation,
- investment windows Decision,
- Operational Board minutes.

While some of these documents do indeed provide some elements of guidance for ensuring that the EFSD's operations are in conformity with the objectives and eligibility criteria set out in Article 9 of the EFSD Regulation, it is not clear, on the basis of the Strategic Board meeting minutes, whether any of them were formally adopted. In addition, several of them were not made public.

*The current portfolio of programmes does not reflect the intention to ensure a diversified thematic coverage*

42. The Strategic Board of the EFSD '(...) shall also support the Commission in setting overall investment goals as regards the use of the EFSD Guarantee and monitor an appropriate and diversified geographical and thematic coverage for investment windows, while giving special attention to countries identified as experiencing fragility or conflict, LDCs [Least Developed Countries] and heavily indebted poor countries' <sup>(66)</sup>.

43. The external assessment report indicates that the portfolio of programmes supported by the EFSD was concentrated on a limited number of sectors and SDGs. In the particular example of the African Investment Platform, nearly 80 % of blending grant allocations in sub-Saharan Africa went to infrastructure projects, while only small amounts went to other sectors such as private-sector development, information and communication technology, agriculture, forestry, and urban development <sup>(67)</sup>. The external assessment recommends that the EFSD portfolio should be managed to give greater prominence to other SDG sectors such as digitalisation, sustainable cities and agriculture <sup>(68)</sup>.

44. The implementation report accepts this recommendation, but it considers that, by creating specific windows for agriculture, digitalisation and sustainable cities within the EFSD Guarantee, the Commission has made a substantive step towards encouraging investment in these areas. It also refers to the 'policy first' principle to be followed under the proposed EFSD+ <sup>(69)</sup> <sup>(70)</sup>.

*Risk-assessment tools for pricing guarantees need to be further developed*

45. The instruments that can be supported by the EFSD Guarantee, as listed in Article 10(1) of the EFSD Regulation, have various levels of inherent risk. In particular, loans in local currency and equity participation have a very high inherent risk.

<sup>(63)</sup> External assessment report, Executive summary.

<sup>(64)</sup> External assessment report, Annex 2.

<sup>(65)</sup> We consulted the published minutes of the four Strategic Board meetings held between 28 September 2017 and 22 January 2020.

<sup>(66)</sup> Article 5(2) of the EFSD Regulation.

<sup>(67)</sup> External assessment report, section 3.2.

<sup>(68)</sup> External assessment report, Executive summary, Recommendation 3.

<sup>(69)</sup> Implementation report, Conclusions and recommendations.

<sup>(70)</sup> See footnote 13 for more information about the EFSD+.

46. In our annual report concerning the 2017 financial year, we pointed out that, unlike the EFSI, where the EIB is effectively the sole intermediary, the EFSD allows other international organisations and private-sector bodies to transmit the benefits of the EU Guarantee, and eventually to call on it. The EFSD is thus the most far-reaching example yet, in terms of the range of partners, of the delegation of powers to assume liabilities on behalf of the EU budget <sup>(71)</sup>.

47. The external assessment report notes that early risk assessments of the proposed investment programmes used data that suggested a high risk and therefore a high guarantee price to be paid by financial institutions to the Commission. It recommends that the selection of the database used for risk assessment be reviewed <sup>(72)</sup>.

48. The implementation report notes that, with regard to the selection of the database for risk assessment, the Commission, working together with experts, is in the process of developing dedicated software that would help to model risks under the EFSD+ guarantee, recognising the specific challenges in developing and transition countries and building on data from the Global Emerging Markets Risk Database <sup>(73)</sup>.

49. As several guarantee agreements have already been signed with financial institutions (see paragraph 31), we consider that securing robust risk assessment tools, methods and expertise is a critical issue.

#### ADDITIONAL CONSIDERATIONS ON THE EFSD'S MONITORING AND EVALUATION FRAMEWORK

##### Criteria

50. According to better regulation principles <sup>(74)</sup>, the Commission is committed to rigorously assessing the impact of legislation in the making, including substantial amendments introduced during the legislative process, so that political decisions are well-informed and evidence-based <sup>(75)</sup>. To this end, the Commission has also committed to carrying out impact assessments of its legislative and non-legislative initiatives, delegated acts and implementing measures, which are expected to have a significant economic, environmental or social impact. In particular, initiatives included in the Commission's Work Programme or in the joint declaration must be accompanied by an impact assessment <sup>(76)</sup>. Some exceptions to this rule are set out in the Commission's better regulation guidelines, including cases where there is a political imperative to move ahead quickly or an emergency that requires a rapid response <sup>(77)</sup>.

51. Evaluations must assess all significant economic, social and environmental impacts of EU interventions (with particular emphasis on those identified in previous impact assessments) <sup>(78)</sup>.

52. In our review No 2/2020, we considered that the Commission should reduce the number of exceptions to the general rules on the need for public consultation, impact assessment and evaluation <sup>(79)</sup>.

53. In our special report No 21/2015, we argued that, in order to establish the credibility of development aid, in particular as regards the instruments used, aid delivery methods and the funds concerned, it is essential that the results achieved with this support can be demonstrated <sup>(80)</sup>.

<sup>(71)</sup> Annual report of the Court of Auditors on the implementation of the budget concerning the financial year 2017, together with the institutions' replies, paragraph 2.41 (OJ C 357, 4.10.2018, p. 1).

<sup>(72)</sup> External assessment report, section 4.3.

<sup>(73)</sup> Implementation report, section 6.

<sup>(74)</sup> Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions: 'Better regulation for better results – An EU agenda' (COM(2015) 215 final of 19.5.2015).

<sup>(75)</sup> Commission press release on the Better Regulation Agenda: Enhancing transparency and scrutiny for better EU law-making, 19 May 2015.

<sup>(76)</sup> Interinstitutional Agreement between the European Parliament, the Council of the European Union and the European Commission on better law-making, 13 April 2016 (OJ L 123, 12.5.2016, p. 1).

<sup>(77)</sup> Better regulation: guidelines and toolbox, see 'Better regulation guidelines – Better regulation in the Commission', Chapter I, Box 1.

<sup>(78)</sup> Better regulation: guidelines and toolbox, see 'Guidelines on evaluation (including fitness checks) and key requirements', Chapter VI, Box 'Key requirements'.

<sup>(79)</sup> Review No 2/2020: 'Law-making in the European Union after almost 20 years of Better Regulation', paragraph 9.

<sup>(80)</sup> Special report No 21/2015: 'Review of the risks related to a results-oriented approach for EU development and cooperation action', paragraph 4 (OJ C 428, 19.12.2015, p. 9).

### **The proposal for establishing the EFSD was not accompanied by an impact assessment**

54. Although the External Investment Plan, including the EFSD, appeared in the Joint Declaration on the EU's legislative priorities for 2017<sup>(81)</sup>, the Commission's proposal for a regulation on the EFSD was not accompanied by a full impact assessment<sup>(82)</sup>. According to Commission staff, this was an exception justified by the strong political imperative to move ahead quickly with the EFSD in response to the migration crisis.

55. According to the Commission's better regulation guidelines, evaluations must assess all significant economic, social and environmental impacts of EU interventions, with particular emphasis on those identified in previous impact assessments. We consider that the lack of an impact assessment for the EFSD Regulation reinforces the need for a full evaluation of the EFSD to be carried out<sup>(83)</sup>.

### **The use and the functioning of the EFSD Guarantee Fund have not yet been evaluated**

56. Article 17(2) of the EFSD Regulation requires the Commission to evaluate the use and the functioning of the EFSD Guarantee Fund by 31 December 2019 and every three years thereafter. To date, no such evaluation has been carried out.

57. When we asked about this evaluation, Commission staff referred us to the implementation report, the external assessment report, a Commission report on the management of the Guarantee Fund of the European Fund for Sustainable Development<sup>(84)</sup> and a communication from the Commission on the identity of the asset manager for the common provisioning fund in accordance with Article 212 of Financial Regulation 2018/1046<sup>(85)</sup>. However, none of these documents provides an evaluation of the use and functioning of the EFSD Guarantee Fund.

- The implementation report does not refer to Article 17(2) of the EFSD Regulation, and does not provide any information on the use or the functioning of the EFSD Guarantee Fund.
- Although the external assessment report concludes that the EFSD Guarantee Fund complies with the EFSD Regulation's requirements, it does not further evaluate its use or its functioning.
- The Commission's report on the management of the Guarantee Fund of the European Fund for Sustainable Development was published on 31 July 2020. It is a management report aimed at fulfilling the requirements of Article 16(3) of the EFSD Regulation.
- The Commission's communication on the identity of the asset manager for the common provisioning fund in accordance with Article 212 of Financial Regulation 2018/1046 does not provide any evaluation of the use or functioning of the EFSD Guarantee Fund.

58. For example, in our view, the following issues are ones which should have been raised in any evaluation of the EFSD Guarantee Fund but the documents listed above do not address them.

- the adequacy of the level of the EU funding allocated to the Guarantee Fund to cover EFSD-guaranteed operations in an efficient manner,
- the adequacy of the Guarantee Fund's target rate (currently set at 50 % of the total EU guarantee obligations) with regard to the risk profile of the Fund, and
- the adequacy of the Guarantee Fund's provisioning mechanism in terms of timeliness and cost-efficiency.

<sup>(81)</sup> Joint declaration of European Commission, Council and Parliament: 'Joint Declaration on the EU's legislative priorities for 2017, 13.12.2016.

<sup>(82)</sup> Proposal for a regulation of the European Parliament and of the Council on the European Fund for Sustainable Development (EFSD) and establishing the EFSD Guarantee and the EFSD Guarantee Fund (COM(2016) 586 final of 14.9.2016).

<sup>(83)</sup> Better regulation: guidelines and toolbox, see 'Guidelines on evaluation (including fitness checks) and key requirements', Chapter VI, Box 'Key requirements'.

<sup>(84)</sup> Report from the Commission to the European Parliament, the Council and the Court of Auditors on the management of the Guarantee Fund of the European Fund for Sustainable Development (COM(2020) 346 final of 31.7.2020).

<sup>(85)</sup> Communication from the Commission to the European Parliament and the Council on identity of the asset manager for the common provisioning fund in accordance with Article 212 of Financial Regulation 2018/1046 (COM(2020) 130 final of 25.3.2020).

### Weaknesses in the results framework

59. The EU International Cooperation and Development Results Framework, launched in 2015 and revised in 2018, is a Commission tool used to collect and measure results achieved against strategic objectives<sup>(86)</sup>. It serves, among other things, as a basis for reporting the results of indicators included in the strategic plans and management plans of the Commission's Directorate-General for International Cooperation and Development<sup>(87)</sup>.

60. The implementation report concludes that, while the EFSD monitoring framework design is aligned with the EU Results Framework for development cooperation, its ability to produce data that can be consolidated and aggregated should be improved, taking into account the following<sup>(88)</sup>.

- The methodology used for calculating some of the proposed indicators still needs to be decided on.
- Core sector indicators are not easily comparable, and add little value.
- Tensions between the Commissions' reporting needs and the financial institutions' own systems and approaches to monitoring increase costs and encourage a narrower focus on common ground (similar or comparable indicators).

61. In addition, the external assessment report indicates that the EFSD might not be able to monitor performance against gender and other cross-cutting indicators due to limitations in the monitoring framework<sup>(89)</sup>.

62. In our special report No 21/2015, we observed that the lack of harmonisation between development partners' aid-delivery instruments, results frameworks and accountability structures could generate inefficiencies and accountability gaps<sup>(90)</sup>. We consider that this risk is even higher for the EFSD, where the Commission's ability to account for the use of EU funds will mostly depend on data and reports provided by financial institutions and their private-sector partners.

### CONCLUSIONS

63. The implementation report does not fulfil some basic requirements of Article 17(1) of the EFSD Regulation. It is not the product of an evaluation, but rather one of a limited assessment of the initial functioning of the EFSD, its management and its effective contribution to the purpose and objectives of the EFSD Regulation. A review of EFSD's business processes still needs to be carried out. The implementation report was submitted eight months after the end of the period covered by the external assessment and five months after the deadline set in the EFSD Regulation for the Commission evaluation.

64. The average financial leverage figure featuring in the implementation report as an indicator of the EFSD's capacity to mobilise additional investments is insufficiently reliable, and could be overestimated. The implementation report does not provide any specific information about the EFSD's performance in crowding in private-sector funding or in delivering innovative products, and its conclusions on non-financial additionality are based on predictions.

65. The EFSD is at too early a stage of implementation for any contribution that it might make to the achievement of the SDGs to be accurately assessed. The implementation report does not provide any information about how the EFSD targets investments towards sectors that advance climate-change mitigation and adaptation. Nor does it contain information about progress made towards reaching the target set for the minimum proportion of EFSD Guarantee financing devoted to climate action, renewable energy and resource efficiency.

66. Though the implementation report assesses the speed of the EFSD's implementation positively, it does not acknowledge or explain the discrepancies between regulatory provisions and the actual pace of implementation.

67. Some issues raised by the content of the external assessment report, which are significant in terms of assessing the EFSD's initial functioning and management, are insufficiently reflected in the implementation report. These concern in particular the functioning of the Strategic Board with regard to the requirements of the EFSD Regulation, the consistency between the current portfolio of programmes and the intention to ensure a diversified thematic coverage, and the need to secure robust risk assessment tools, methods and expertise for pricing guarantees.

<sup>(86)</sup> Commission Staff Working Document 'A Revised EU International Cooperation and Development Results Framework in line with the Sustainable Development Goals of the 2030 Agenda for Sustainable Development and the New European Consensus on Development' (SWD(2018) 444, 11.10.2018), section 2.

<sup>(87)</sup> Idem, Introduction.

<sup>(88)</sup> Implementation report, section 5.3.

<sup>(89)</sup> External assessment report, Executive summary.

<sup>(90)</sup> Special report No 21/2015, paragraph 80.

68. Besides an evaluation of the EFSD's initial functioning, management and effectiveness, the EFSD's monitoring and evaluation framework is missing some key elements. In particular, the EFSD Regulation was not subject to an impact assessment, an evaluation of the EFSD Guarantee Fund is still missing and, as the implementation report recognises, the EFSD's results framework needs to be improved.

This Opinion was adopted by Chamber III headed by Ms Bettina JAKOBSEN, Member of the Court of Auditors, by exceptional procedure of 3 September 2020.

*For the Court of Auditors*

Klaus-Heiner LEHNE

*President*

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