Survey and Analysis of Transportation Investment Models in Other Countries

Stage 3 Supplementary Report: Survey and Analysis of Investment through Government-Sponsored Lending Institutions

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Abbreviations and Acronyms

Acronym	Definition *[Jurisdiction in which acronym is used]*
ATIMOC	Analysis of Transportation Investment Models in Other Countries
COP	Corporate Operational Plan *[Europe]*
CPF	Corporate Private Finance *[United Kingdom]*
DOT	U.S. Department of Transportation
EIB	*[Europe]*
EIF	European Investment Fund *[Europe]*
EPA	U.S. Environmental Protection Agency
EU	European Union *[Europe]*
FHWA	U.S. Federal Highway Administration
FTA	U.S. Federal Transit Administration
GARVEE	Grant Anticipation Revenue Vehicles
GDP	Gross Domestic Product
HM Treasury	Her Majesty's Treasury *[United Kingdom]*
HUD	U.S. Department of Housing and Urban Development
IUK	Infrastructure UK *[United Kingdom]*
KPI	Key Performance Indicator
LGTT	Loan Guarantee Instrument for Trans-European Transport Network Projects *[Europe]*
LIBOR	□ondon Interbank Offered Rate
NAO	National Audit Office
OPIC	Overseas Private Investment Corporation
OST	Office of the Secretary of Transportation
PAB	Private Activity Bond
PFI	Private Finance Initiative *[United Kingdom]*
PPP	Public Private Partnership
PSC	Public Sector Comparator
PwC	PricewaterhouseCoopers LLP
RRIF	Railroad Rehabilitation and Improvement Financing
SBA	Small Business Administration
SME	Small- and Medium-Sized Enterprise
TARP	Troubled Asset Relief Program
TEN	Trans-European Network *[Europe]*

Acronym	Definition *[Jurisdiction in which acronym is used]*
TIFIA	Transportation Infrastructure Finance and Innovation Act
TIFU	The Infrastructure Finance Unit *[United Kingdom]*
TIGER	Transportation Investment Generating Economic Recovery
UK	United Kingdom
U.S.	United States
VfM	Value for Money

1.0 Executive Summary

This Supplementary Report (the Report) provides a summary of the research and key observations and provides supplementary information on topics related Stage 3 of the Analysis of Transportation Investment Models in Other Countries: Survey and Analysis of Investment through Government Sponsored Lending Institutions.

This Report provides an overview of how government-sponsored lending institutions have been utilized internationally to address market gaps and leverage substantial private co-investment by providing flexible credit-assistance. The Infrastructure Finance Unit (TIFU) in the UK and the European Investment Bank (EIB) in the European Union (EU) are two different types of lending institutions and are the focus of this Report.

A government-sponsored lending institution is a government agency or program that provides credit assistance to support projects that have a public, social, and economic benefit and purpose. As illustrated in Figure 1, government-sponsored lending institutions play a role throughout most of the investment decision making process, from selecting projects and making investment decisions in the feasibility stage to holding oversight roles during implementation, monitoring and evaluation.

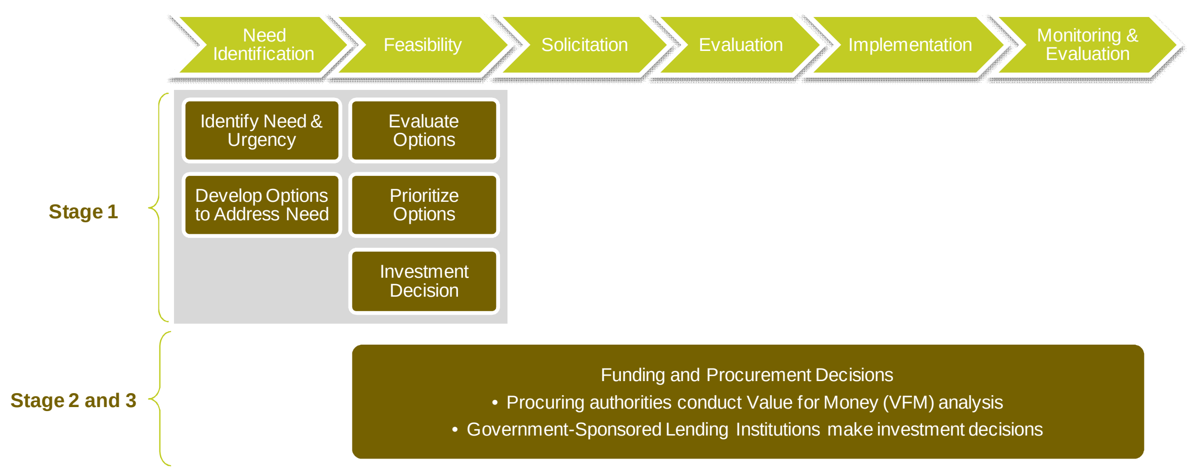


Figure 1: Investment Decision Making Process

Government-sponsored lending institutions can be created to support and fund projects that the private sector may not otherwise be able to fully realize, due to a lack of market confidence or reduced lending capacity brought about by market conditions, such as the recent Global Financial Crisis.[1]

Government-sponsored lending institutions, acting as a central entity, often cover multiple sectors and may help to promote consistent investment prioritization and coordination in investment and project monitoring. Based on the research outlined in this Report, international experience indicates that a coordinated approach can maximize the impact of the government's investment in projects, optimize staff and funding resources, and encourage long-term, integrated project planning across multiple sectors.[2]

Government-sponsored lending institutions can raise capital for their selected investments by combining funding from government contributions and/or markets.[3] U.S. DOT may consider utilizing market rate products to complement the use and effectiveness of Federal funding resources.

Government-sponsored lending institutions conduct an accurate assessment of relevant risks before lending federal funds to projects. Research into the lending practices of TIFU and the EIB indicates that commercial experts and commercial lending processes are utilized to review project risks and lending decisions, which has helped to establish private sector confidence in investing alongside these public sector institutions.[4] Several U.S. groups, such as the U.S. Federal Highway Administration's (FHWA) Office of Innovative Program Delivery[5] and the U.S. Treasury Department's Office of Financial Stability[6], have deep capabilities and capacity in these practices. Increased coordination between and within departments may further strengthen the U.S. government's skills in conducting commercial risk assessments and analysis for federal government credit programs, building market confidence and strengthening the public-private sector relationship.

Purpose of Government-Sponsored Lending Institutions

Government-sponsored lending institutions can serve a variety of purposes to reflect the requirements of the government and market. TIFU was created as a market stabilization tool to address the absence of capital market (e.g., stock market, or bond market) funding and the reduced number of bank lenders in the Private Finance Initiative[7] (PFI) market. TIFU's goal is to act as a market catalyst and help PFI projects obtain financing in a tight credit market, which came as a result of the recent Global Financial Crisis.[8]

In 1958, the EIB was established to create a long-term financing institution for continued post-WWII rebuilding and development among a union of independent sovereign states that would eventually become the EU. Today, EIB investments support political and economic cooperation with non-EU partner countries and further EU policy objectives.[9]

Governance Structure of a Government-Sponsored Lending Institution

The type and structure of a government-sponsored lending institution can impact the degree of regulation and oversight, as well as the focus and execution of its activities. Government-sponsored lending institutions can be established under existing government department agencies or as standalone financial institutions.

For example, TIFU is a sub-agency within Her Majesty's (HM) Treasury, working in conjunction with other Treasury sub-agencies (e.g., PPP Policy Team and Project Review Group)[10]. In contrast, the EIB is autonomous on an administrative and budgetary basis, with funds raised from contributions from member states and capital markets. The EIB is led by a Board of Governors which is appointed by the EU member states. The EIB Board of Governors has the responsibility of overseeing and selecting the leadership of a Management Committee, Board of Directors, and Audit Committee. The key governance roles for the EIB include:

- The Board of Governors that sets policy guidelines, lending priorities, and leadership;
- The Management Committee that oversees day-to-day operations;
- The Board of Directors that serve as the lending decision making body; and
- The Audit Committee that serves as an independent auditor with annual reports on bank compliance and risk monitoring and a review of financial statements and financial reporting.[11]

Policy and Financial Objectives of a Government-Sponsored Lending Institution

Government-sponsored lending institutions can have objectives to correct market or other information failures, to act as a short-term measure to counteract temporary credit market difficulties, to reduce inequalities in access to credit, or to support the government's broader strategic objectives.[12] The policy and financial objectives of TIFU and EIB differ by a short-term and long-term perspective.

In 2009, TIFU was established in response to the Global Financial Crisis to finance key PFI infrastructure projects and support job and economic growth. The main objective of TIFU is to provide a centralized, cross-departmental approach to public sector lending that can supplement bank or capital market funding when it is not readily available. TIFU addresses the government's need for an urgent response to financial crisis in such a way that retains the government's flexibility to offer loans as a temporary solution.[13]

The primary objective of the EIB is to contribute to long-term goals of integration, balanced development, and economic and social cohesion of EU Member States. The EIB promotes investment in information and communication technologies, human and social capital development, and environmental advancements.[14] Since its inception in 1958 to June 2010, the EIB has provided nearly €800B (US$1.1Tr[15], 2010) for projects in EU member states, candidate countries, and partner non-EU countries to meet the long-term investment needs and policy and political goals of the EU.[16]

Project Eligibility for Credit Assistance and Level of Credit Assistance Available

Projects may be eligible for credit assistance based on existing criteria, programs, or specific policy objectives. TIFU loans are considered for PFI projects that have successfully completed the investment selection process and Value for Money (VfM) analysis, and have made reasonable efforts to obtain private sector financing. Such projects are eligible for up to 100% of senior debt financing.[17] Unlike TIFU, which selects projects based on existing project eligibility criteria under PFI, the EIB's project eligibility is linked to a more broadly defined objective of integration and balanced development of the EU. The EIB funds projects that contribute to and further EU policy objectives such as promoting economic and social cohesion and developing a competitive and innovative knowledge-based economy.[18] EIB lends no more than 50% of funds required for project implementation.

Project Selection and the Competitive Process for Allocating Resources of a Government-Sponsored Lending Institution

Government-sponsored lending institutions utilize a unique process to select and fund projects. The project selection and lending process can be summarized in three main stages:

- **Application:** Assessment of a project's eligibility and suitability for financing
- **Evaluation and Selection:** Review of the project's technical and financial application to assist the investment decision-making process
- **Implementation and Monitoring:** Oversight and execution of project activities[19]

While TIFU builds on the existing PFI processes, the EIB follows a project-by-project approach where projects are evaluated on their intent and potential to contribute to EU policy objectives:

TIFU[20]

Stage	Description
Application	PFI projects are eligible for TIFU loans if they: • Commenced procurement process by March 3, 2009 • Were approved by the Project Review Group and project procurement initiated after March 3, 2009; or • Meet the standard VfM and affordability criteria, and are subject to obtaining HM Treasury approval prior to starting the procurement process.
Evaluation and Selection	Key focus is on project's ability to demonstrate that they have been unable to obtain sufficient financing from private capital markets
Implementation and Monitoring	Project monitoring can include documents and tasks such as project credit analysis and due diligence and providing regular project reports to TIFU.[21]

EIB[22]

Stage	Description
Application	Eligible projects can cross a wide range of sectors, and must contribute to EU policy objectives, which include development of trans-European networks and investment in education and research and development.
Evaluation and Selection	Two key steps in the project evaluation process include reviewing the project proposal for compliance with EU objectives and assessing the economic, technical, and financial merits of the project, as well as its impact on the environment.
Implementation and Monitoring	The EIB monitors projects from loan award through project implementation until the loan is paid back. Monitoring requirements can include tracking the servicing of the loan and checking that funds are being used for the stated project objectives.

Evaluation and Selection: Livability & Sustainability

The EIB has a particular focus on livability and sustainability criteria during project evaluation and selection. During project selection, environmental and social screenings are carried out to identify the extent and complexity of the project's environmental and social impacts and risks. The EIB also aims to identify, quantify, value, and mitigate direct and indirect environmental and social externalities where their influence on the socio-economic viability of the project is expected to be significant.[23]

Financial Products Offered by a Government-Sponsored Lending Institution

Government-sponsored lending institutions may provide credit assistance through a wide array of financial products including loans, guarantees, lines of credit, and equity. While TIFU has a single product of loans for defined and qualified PFI projects,[24] the EIB offers multiple financial products, each with its own purpose and criteria for approval.

Although TIFU may provide up to 100% of senior debt[25] financing required by an eligible PFI project, loans are anticipated to supplement negotiated loans from commercial banks, the EIB, and capital market lenders. The EIB offers a wider array of financial products, including:

- **Grants:** Typically used for social development projects or to cover costs of technical assistance in the form of project development and in applying for EIB financial assistance
- **Guarantees:** Used for senior and subordinated debt
- **Loans**: Various types of loans used to cover up to 50% of total project costs.
- **Equity:** Venture capital investment funds generally used for high-technology small- to medium-enterprises and the development of renewable energy[26]

Lending Terms of a Government-Sponsored Lending Institution

Lending terms offered by a government-sponsored lending institution can often be classified under two types of lending:[27]

- **Market Rate:** The borrowing rate for debt on the open-market, similar to the rate offered by commercial banks.
- **Preferential Terms:** The borrowing rate is below market rate and/or subsidized by policy driven programs (e.g., home ownership), although the government assumes at least as much risk as the lender through market rate lending.

TIFU and EIB each provide examples of various lending terms that can be offered. TIFU lending terms are comparable to market rates. TIFU can offer fixed or floating interest rate loans over 15 to 30 year periods with terms similar to those of commercial lenders.[28] EIB lending is usually over 4 to 20 year terms at competitive fixed, convertible, or floating interest rates.[29] These floating interest rates are available under preferential terms, *at* a rate below the London Interbank Offered Rate (LIBOR). EIB lends to projects and national and regional banks, which is emblematic of its status as a bank.[30]

Summary

Based on the research conducted, the following findings may be of interest to U.S. DOT:

- Government-sponsored lending institutions can be created to serve both short-term needs (e.g., providing rapid response to tight credit markets) and long-term objectives (e.g., acting as a financing institution).
- The level of independence and government oversight of government-sponsored lending institutions can ranges from sub-agencies under the national government to independent banks. The institution's level of independence is often linked to the short-term and long-term objectives of the institution and can also be a key determinant in how the market views the institution when it is acting on the lending side of a transaction.
- The objectives for government-sponsored lending institutions may include providing financing to projects that are unable to raise sufficient private capital, or investing in projects that fulfill countries' economic and social development goals.
- The types of projects eligible for assistance from government-sponsored lending institutions align with the government's policy objectives, which may be directly expressed or incorporated into existing processes, such as the Value for Money (VfM) analysis in the UK.
- Projects are generally selected through a competitive processes based on their capacity to meet the eligibility requirements and the financing need.
- The financial products offered by government-sponsored lending institutions may include various types of loans, in addition to grants, loan guarantees, lines of credit or equity.
- The lending terms offered by government-sponsored lending institutions can reflect the type of project and the financial products that the institution has available.

2.0 Introduction

The United States Department of Transportation (U.S. DOT) Office of the Secretary of Transportation (OST) recently requested the development of research materials for transportation officials and other stakeholders to learn more about the infrastructure investment models used in other countries. The analysis includes three stages:

- Stage 1: Survey and Analysis of the Frameworks that Govern Transportation Investment in Other Countries
- Stage 2: Survey and Analysis of the Use of Public Sector Comparator (PSC) and Value for Money (VfM) Analyses in Developed Countries with Mature PPP Programs
- Stage 3: Survey and Analysis of Investment through Government-Sponsored Lending Institutions

The purpose of Stage 3 is to provide DOT with an understanding of how government-sponsored lending institutions are utilized internationally to address market gaps and leverage substantial private co-investment by providing flexible credit-assistance. In addition to providing an overview of government-sponsored lending institutions, this document discusses and analyzes the following topics:

Topic	Summary of International Approach
Purpose of a Government-Sponsored Lending Institution	Section 4.1 introduces the purpose behind creating TIFU and EIB
Governance Structure of a Government-Sponsored Lending Institution	Section 4.2 highlights TIFU's and EIB's governance structure and type of institution
Policy and Financial Objectives of a Government-Sponsored Lending Institution	Section 4.3 highlights the financial and policy objectives of TIFU and EIB
Project Eligibility for Credit Assistance and Level of Credit Assistance Available	Section 5.1 details the type of projects eligible for credit assistance, including the amount of credit assistance each project is eligible for
Project Selection and the Competitive Process for Allocating Resources of a Government-Sponsored Lending Institution	Section 5.2 summarizes the process used to select projects and allocate government-sponsored lending institutions resources
Financial Products Offered by a Government-Sponsored lending Institution	Section 5.3 discusses the types of financial products TIFU and EIB offer to provide credit assistance
Lending Terms of a Government-Sponsored Lending Institution	Section 5.4 highlights the lending terms offered by TIFU and EIB, including the use of any favorable lending terms

The document concludes with an analysis of key observations relevant to U.S. DOT in Section 6.0.

2.1 Summary of Report Research Analysis Questions

The following table summarizes the key research questions for Stage 3. The table briefly summarizes the research conducted for each question and provides references to where the questions are addressed in this Report:

Research Question	TIFU	EIB	Report References
i. Why was a government-sponsored lending institution created?	To provide a rapid response to tight credit market and bolster lending to Private Finance Initiative (PFI) projects where insufficient private sector funding was available on acceptable terms to allow the project to reach a timely financial close.	To become the long-term financing institution for a union of independent sovereign states that would become the EU.	Section 4.1
ii. What are the objectives of the government-sponsored lending institution (policy and financial) and how are results achieved?	Provide financing to PFI projects unable to raise sufficient private sector financing and negotiate lending terms and monitor and manage loans for PFI projects.	Invest in projects that contribute toward integrated balanced development, and economic and social cohesion.	Section 4.3
iii. What type of financial products does the government-sponsored lending institution offer?	Loans	Grants, loans, loan guarantees, lines of credit, equity	Section 5.3
iv. Does the government-sponsored lending institution offer any favorable lending terms?	No, loans are over 15 to 30 year terms on fixed or floating interest rates, matching those of commercial lenders.	Yes, lending is usually over 4 to 20 year terms at competitive fixed, convertible, and variable interest rates. Variable interest rates are available at rate below LIBOR[31] Subsidized below market rates.	Section 5.4
v. What types of projects are eligible for credit assistance from the government-sponsored lending institution, and how much credit assistance is each project eligible for?	Approved projects under the PFI that have undergone investment selection process and VfM analysis. Projects that have made reasonable attempts to obtain private sector financing. TIFU provides up to 100% of senior debt financing.	Projects that contribute to policy objectives such as promoting economic and social cohesion; production, transfer, and distribution of alternative energy; and development of a competitive, innovative, and knowledge-based economy. EIB lends no more than 50% of funds required for project implementation.	Section 5.1

Research Question	TIFU	EIB	Report References
vi. Is there a competitive process in place for allocating the government-sponsored lending institution's resources, and if so, what factors drive project selection?	No, projects are selected mostly on financing need and difficulty in obtaining ready and affordable credit from capital markets.	No, as long as a project is in line with eligibility requirements and further contribute to policy objectives.	Section 5.2
vii. What type of institution is the government-sponsored lending institution and what type of governance structure does it employ?	Sub-agency housed under and governed by the Treasury that works in conjunction with other Treasury sub-agencies such as the PPP Policy Team and the Project Review Group.	Independent non-profit policy-driven bank governed by a Board of Governors that oversee the work of a Board of Directors, Management Committee, and Audit Committee.	Section 4.2

3.0 Summary of the Institutions Selected for this Report

TIFU and the EIB were selected by U.S. DOT from a pool of lending institutions and programs across Europe, Asia, and multi-lateral institutions due to their product offerings, lending models, and relevance to the U.S. The key determinants in selecting these institutions are summarized in the table below:

Institution	Rationale
TIFU	• Recently introduced a direct lending arm of government, established within HM Treasury • TIFU is able to make direct loans to project companies involved in Private Finance Initiative (PFI)/Public Private Partnership (PPP) transactions, sitting along-side commercial banks.
EIB	• The EIB is a major lender to infrastructure projects across Europe • The EIB raises funds in the commercial market, to support the development of infrastructure projects across Europe. • The EIB acts as a regional lending institution and is supported by member states through the contribution of equity and, effectively, guarantees of liabilities. • The EIB also has a specific focus on livable and sustainable communities in their project eligibility guidelines, which provides useful insight into how the programs of a lending institution can be utilized to support livability and sustainability policies.

4.0 Overview of Government-Sponsored Lending Institutions

To provide an overview of government-sponsored lending institutions, this section discusses the purpose, governance structure and policy and financial objectives of TIFU and the EIB. A brief discussion on experiences in the U.S. with government-sponsored lending programs and institutions is also provided.

4.1 Purpose of a Government-Sponsored Lending Institution

In general, **a government-sponsored lending institution is a government agency or program created with the purpose of providing credit assistance to both public and private sector entities in order to support projects that have a public, social, and economic benefit and purpose**.[32] Its creation may be to fulfill short-term goals driven by the condition of the economy and lending market, as in the case of TIFU, or to meet longer-term financing needs, such as the EIB.

4.1.1 TIFU

TIFU was established in 2009 by HM Treasury with the purpose to lend to Private Initiative (PFI) projects unable to raise sufficient financing, negotiate the terms of loans for PFI projects, and to monitor and manage loans for PFI projects. TIFU was created as a **stabilization tool** to address the absence of capital market funding and the reduced number of active bank lenders in the PFI market. It was intended to act as a market catalyst to help PFI projects obtain financing in a tight credit market.[33] PFI is an arrangement whereby the public sector contracts to purchase services from the private sector on a long-term basis, often between 15 to 30 years.[34]

4.1.2 EIB

Established in 1958, the purpose of the EIB was to create a **long-term financing institution** through the Treaty of Rome for a union of independent sovereign states that would eventually become the EU. The treaty required the agreement and consent of the European Member States, who became joint shareholders and governors of EIB through their contribution of funds to capitalize the bank. The EIB finances a wide range of investments in all sectors of the economy to support external cooperation and to further policy objectives.[35]

In the U.S., TIFIA and TIFU may appear similar in that they both provide credit assistance to projects to address market gaps and to encourage private co-investment. However, TIFIA differs in that its assistance is exclusively for transportation projects,[36] while **TIFU provides support for cross-sector infrastructure projects**.

4.1.3 U.S. Experience

The idea of a long-term infrastructure bank for the U.S. has been introduced in various economic proposals and legislative acts, including: the Dodd-Hagel National Infrastructure Bank Act of 2007[37], the DeLauro-Ellison-Weiner-Israel National Infrastructure Development Bank Act of 2009[38], the President's FY2010 Budget, and as a part of the President's Labor Day 2010 economic proposal[39]. In the U.S., an independent national infrastructure bank, whether it serves short-term or long-term objectives within a small or broad set of sectors, requires consensus and legislation by Congress to be created. This may prove to be a challenging task, as in recent years, there has been a policy debate over how an infrastructure bank might be governed, its scope and purpose, and how projects are selected.[40] The introduction of a national infrastructure bank has raised concerns that it may be either duplicative or an expropriator of political and budgetary authority of existing programs.[41] In addition, the bank is expected to focus on projects that have a significant national impact. States and rural areas with smaller populations and low population densities have expressed concerns that projects in their particular communities may not be competitive.[42] This may impact the level of consensus to pass the infrastructure bank legislation.

4.2 Governance Structure of a Government-Sponsored Lending Institution

Government-sponsored lending institutions may be established under existing government department agencies or as standalone financial institutions.

4.2.1 TIFU

TIFU is a sub-agency within HM Treasury. TIFU coordinates and works closely with the Project Review Group, the Corporate and Private Finance Team, and the PPP Policy Team within HM Treasury.[43] TIFU's governance structure is illustrated in Figure 2 below.

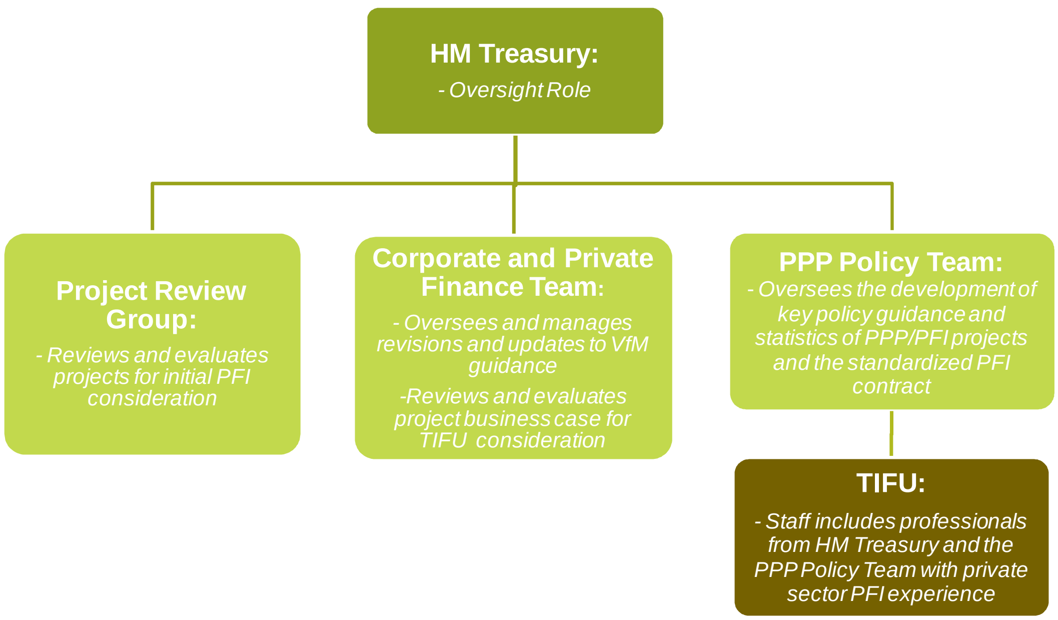


Figure 2: TIFU Governance Structure[44]

The Project Review Group is responsible for reviewing and evaluating projects for initial PFI consideration. The Corporate and Private Finance Team oversees and manages revisions and updates to Value for Money (VfM) guidance. It also reviews and evaluates project business cases for TIFU consideration. The PPP Policy Team oversees the development of key policy guidance and statistics of PPP/PFI projects and the standardized PFI contract.[45]

In addition, TIFU has due diligence procedures built on private sector experience of its staff and an internal credit committee composed of HM Treasury officials that advises the Treasury Minister to lend or not to lend based on the PFI project potential and viability. **TIFU requires applicants to submit project evaluation data and the results of analyses by private commercial lenders whom the applicant approached prior to applying for TIFU loan**. Evidence of prior interactions with private commercial lenders to seek financing is essential and must be well-documented in order to meet TIFU requirements.[46]

HM Treasury's reporting standards and laws govern TIFU's reporting requirements. Projects may also be subject to review by independent bodies such as the National Audit Office (NAO).[47]

TIFU Staffing

The Director of TIFU is formally of Partnerships UK, the former UK national government PPP advisory authority, with a number of years of commercial lending experience. Senior staff were hired from the private sector with experience at major international banks. Three staff came were recruited from the private sector on a temporary assignment with experience in banking, law, and project finance.[48]

4.2.2 EIB

The EIB is **an independent non-profit policy-driven bank** governed by a Board of Governors that oversees work of a Board of Directors, Management Committee, and Audit Committee.[49] EIB's governance structure is illustrated in Figure 3 below.

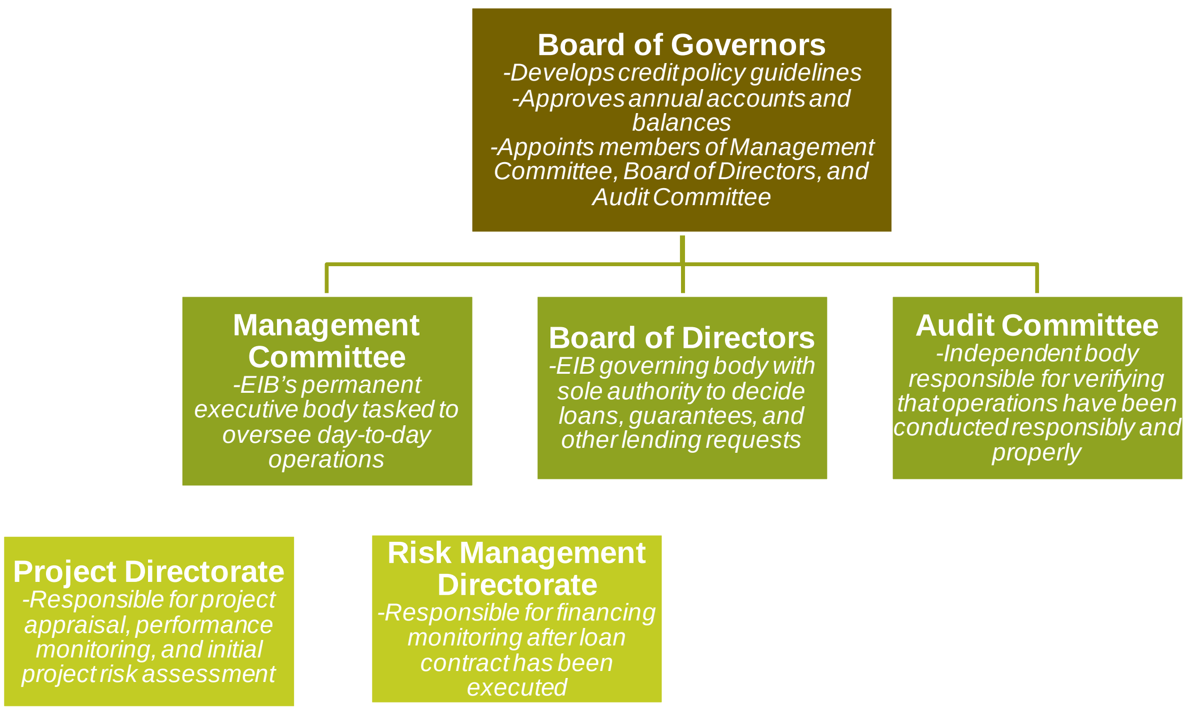


Figure 3: EIB Governance Structure[50]

The EIB is led by the Board of Governors and has the responsibility of overseeing and selecting the leadership of the Management Committee, Board of Directors, and the Audit Committee. The EIB Board of Governors is appointed by the EU member states. The Board of Directors contains 28 members with representatives from each member state and the European Commission. There are 16 alternates, which are shared by groupings of member states.[51]

While the Board of Governors sets policy guidelines, lending priorities, and leadership, the Management Committee oversees day-to-day operations. The Board of Directors serves as the lending decision making body and the Audit Committee serves as an independent auditor with annual reports on bank compliance and risk monitoring and a review of financial statements and financial reporting. The Audit Committee also monitors how the EIB carries out policies and regulations established by the EU.[52]

As the EIB is part of the EIB Group, which includes the European Investment Fund, and the broader family of EU governing institutions and bodies, it is important to note that not only are these governing bodies separated by geography, being in different cities, but politically as well.[53] The European Parliament based in Strasbourg, France and the Council of the EU and the EU Commission based in Brussels, Belgium represent the EU's primary policymaking and decision-making bodies and devise the laws that apply throughout the EU.[54]

The EIB is owned by the EU Member States rather than the EU Commission, Council or Parliament (referred to as the EU "institutional triangle"). The EIB Board of Directors in coordination with the Board of Governors are the sole decision-makers for lending and borrowing. It may receive policy guidance from and work closely in coordination with the EU institutional triangle, however there are no formal reporting responsibilities or commitments to these institutions.[55]

The EIB maintains a portfolio management approach similar to that of a commercial bank with some characteristics of government (e.g., selection of its leadership by country Ministers). Unlike a commercial bank, it is not structured to handle bad debt often, if at all.[56]

EIB's Portfolio Management

There are **three major departments or directorates** that fall under the Management Committee and manage investments:[57]

- **Finance Directorate** - maintains and oversees EIB lending and borrowing
- **Project Directorate** - project assessment and monitoring
- **Risk Management Directorate** - reviews project financial and operational risks

Based on the EIB's Three-year Corporate Operational Plan 2010-2012, these three directorates work to monitor and maintain the EIB's seven key performance indicators (KPI):[58]

1) **Value added index** - composite index of project rating based on contribution of EU objectives, quality and soundness of investment, and EIB contribution
2) **Disbursements** - year-over-year changes in total annual disbursements
3) **Achievement of Lending Objectives** - percentage achievement of six priority lending objectives: economic and social cohesion, knowledge economy, trans-European networks, improving and promoting the environment and sustainable communities, small- and medium-enterprises, and sustainable energy
4) **Signatures in Co-operation with Commission** - total amount and percentage of total lending agreements in co-operation with the European Commission and using special financial instruments such as risk sharing funds or guarantees
5) **Net Funding Result** - economic indicator that measures the cost of the EIB's borrowing
6) **Cost Coverage** - expected revenue divided by outgoing lending costs
7) **Net surplus before provisions** - net reserves less other obligations

The KPI's are used by the EIB to gauge the overall performance of its investment portfolio. The EIB's operational goal is “to support and ensure sound investments with well managed increased risk and ensure long-term financial self-sufficiency through the promotion of banking best practices”. For example, the EIB adheres to the Basel II Accords for risk management in continuously assessing credit risk, solvency ratios, and asset quality distribution for existing and new investments.[59]

U.S. Experience

Although such a staffing approach and governance structure may not be immediately practical in the U.S. Federal Government, there may be opportunities to build capability and capacity through internal government transfers or temporary assignments, that seek to place knowledgeable personnel from other departments or agencies across U.S. DOT. For example, risk management and financial analysts from the U.S. Treasury Department's Office of Financial Stability might be rotated through U.S. DOT on temporary placement to help develop an institutional investment framework based on their knowledge and experience in establishing the Troubled Asset Relief Program (TARP).[60]

4.3 Policy and Financial Objectives of a Government-Sponsored Lending Institution

Government-sponsored lending institutions can **address market gaps** that private sector lenders are not able to fill, **encourage private co-investment** by spurring private lending that otherwise would not occur, and **provide a de-facto level of competition** to help stabilize debt prices and make borrowing more affordable.[61] The objectives of institutions such as TIFU and the EIB are relevant across a number of different market sectors. The policy and financial objectives can also influence the institution's operational activities and strategic priorities.[62]

4.3.1 TIFU

The main policy and financial objective of TIFU is to provide a centralized, cross-departmental approach to public sector credit provision that supplements bank or capital market funding when it is not readily available. Additional objectives for TIFU include ensuring PFI infrastructure projects move forward despite poor financial market conditions, and support job and economic growth. For example, when there is limited market liquidity, a TIFU loan may be offered as a temporary solution to support an infrastructure project. As market conditions improve, HM Treasury retains the flexibility to sell the loan and exit the market.[63]

4.3.2 EIB

The EIB's mission is to further the objectives of the European Union by making long-term finance available for sound investment. As displayed in Figure 4, this is achieved by enabling their staff with adequate tools and process to achieve the objectives of the EIB's mission. EIB contributes toward the integration, balanced development, and economic and social cohesion of the EU Member States. The EIB also promotes a knowledge-economy through investment in information and communication technologies, as well as human and social capital development.[64]

To further illustrate their strategic objectives, the EIB Group develops a rolling three-year Corporate Operational Plan (COP)[65]. This document describes the EIB's priority strategic objectives for lending in the European Union, which reflect EU policy objectives and include:

1. Economic and Social Cohesion and Convergence;
2. Implementation of the Knowledge Economy (previously known as Innovation 2010 initiative);
3. Development of Trans-European Networks (TENs);
4. Protecting and Improving the Environment and Promoting Sustainable Communities;
5. Support for small- and medium-sized enterprises; and
6. Supporting Sustainable, Competitive and Secure Energy.

These priority strategic objectives define medium-term policy and operational priorities, and is an instrument evaluating the EIB's activities. The strategic projections are reviewed and updated annually to adjust to new policy and the economic climate.

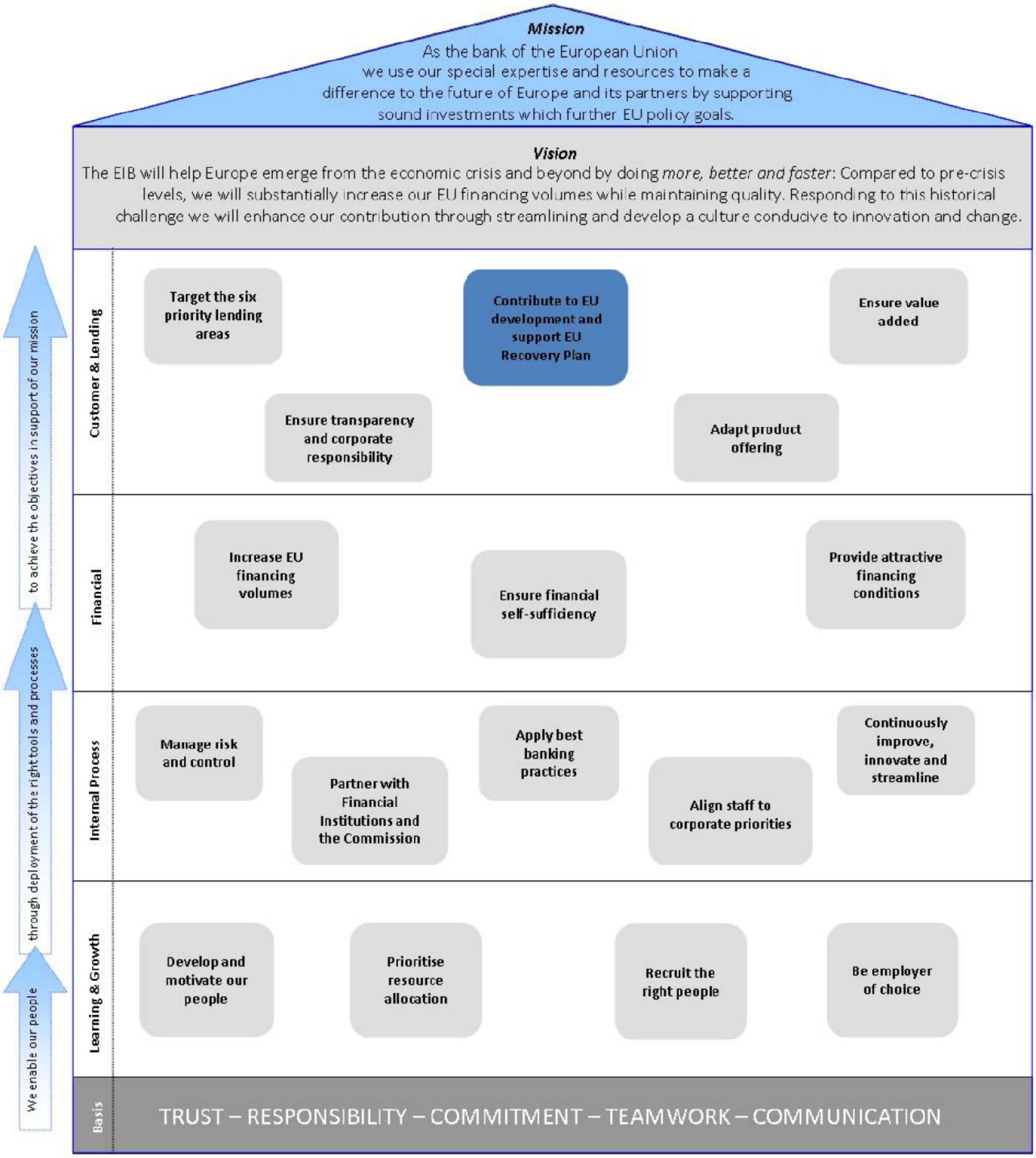


Figure 4: EIB's Strategy Map
Source: EIB Corporate Operational Plan for 2010-2012

4.3.3 U.S. Experience

Most U.S. government-sponsored lending institutions and programs have an underlying policy objective focused on the services that the department or agency provide. For example, Fannie Mae and Freddie Mac have worked to improve access to mortgages and home ownership in the U.S., which focuses on the housing sector.[66] The objectives of the EIB and TIFU are based on broad government objectives that could be delivered across a number of sectors, such as the EIB's objective to provide economic and social cohesion across the EU.

Key Observations: Overview of Government-Sponsored Lending Institutions
• Collaboration and consensus are important when establishing a government-sponsored lending institution. For example, the EIB was established through a treaty, which required the agreement and consent of the European Member States. • The governance structure of TIFU provides an example of how the infrastructure bank may be established in the short-term, as it operates within a government department and is staffed with experienced professionals with significant market experience. • The financial and policy objectives of government-sponsored lending institutions can help to focus the operational activities and strategic priorities of the institution. • Institutions implementing multi-sector objectives can better coordinate and prioritize projects, budgeting, and project monitoring. This may also allow for several projects to be planned and implemented as a single investment, with the higher priority elements of the investment to be delivered first, and an assessment of the required level of financial support (grants, loans, guarantees) for each element.

5.0 Project Selection and Financial Products of Government-Sponsored Lending Institutions

This section outlines the project eligibility and selection requirements of government-sponsored lending institutions, as well as the level of credit assistance, financial products and lending terms. The discussion focuses on TIFU and the EIB, and also describes U.S. examples where relevant.

5.1 Project Eligibility for Credit Assistance and Level of Credit Assistance Available

Projects are eligible for credit assistance based on existing criteria or programs or driven by specific policy objectives and typically can qualify for complementary or supplemental assistance alongside private sector financing.[67] In the U.S., the Federal Register notice for a program establishes the minimum criteria for projects to be eligible for funding. The criteria often reflect the department's key objectives.

5.1.1 TIFU

The PFI program in the UK has a specific project selection process, which includes a **Value for Money (VfM) analysis** being performed to assess the potential value or benefit that may be provided if the project is delivered under the PFI. TIFU is available only to those projects that have completed the VfM analysis and have been selected as PFI projects. The projects that have made reasonable attempts to obtain private sector financing are eligible for **up to 100% of senior debt** financing under TIFU.[68] The reasons projects may have difficulty obtaining private sector financing vary. Investor interest can be impacted by many factors, including the proposed risk allocation, the level of volatility in the capital markets, and the level of competition between projects globally for private capital.[69]

TIFU is funded by HM Treasury and its leadership are appointed by HM Treasury in coordination with the PPP Policy Team. It considers applications for loans to PFI projects at the direction of the Corporate and Private Finance Team and in cooperation with the Projects Review Group. TIFU negotiates the terms of loans for PFI projects on a commercial basis and monitors and manages TIFU loan portfolio and conducts due diligence procedures as necessary.[70]

5.1.2 EIB

The EIB funds projects that contribute to policy objectives such as: promoting economic and social cohesion; production, transfer, and distribution of alternative energy; and the development of a competitive, innovative, and knowledge-based economy. Projects aligned to these criteria may be eligible for EIB assistance. **EIB lends no more than 50% of funds** required for project implementation, which requires the project sponsor to identify how it plans to obtain the remaining funds to deliver the project.[71] In the U.S., TIFIA funding is available up to 33% of a project's anticipated eligible costs.[72]

The EIB makes lending decisions on the basis of a project's merits. Major projects over €25M (US$35M, 2010) are generally financed by direct loans. Small and medium-sized ventures or projects less than €25M are generally financed through credit lines established in cooperation with national and regional banks.[73]

5.1.3 U.S. Experience

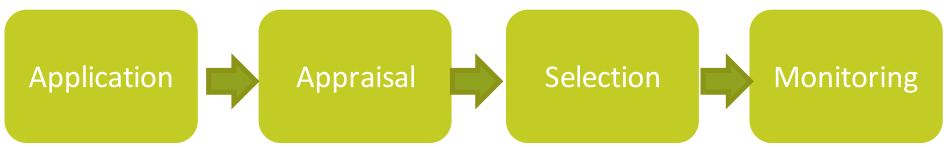
In the U.S., project eligibility and credit assistance limits are set for each grant or funding program. For example, a key eligibility criterion to issue Private Activity Bonds (PABs) is for projects that have already secured other federal assistance.[74] TIFIA also has specific eligibility requirements that project sponsors often pursue in parallel with other funding options, including other DOT funds such as New Starts or PABs.[75]

Eligibility and funding limits also exist within the U.S. on a program specific basis. For example, DOT has also recently sought to combine programs, by allocating TIGER and TIGER II Discretionary Grant funding to projects that can use this funding to leverage TIFIA loans.[76]

5.2 Project Selection and the Competitive Process for Allocating Resources of a Government-Sponsored Lending Institution

The process in which projects are selected and receive allocations from government-sponsored lending institutions can vary significantly. While TIFU builds on the existing PFI, the EIB follows a more project-by-project approach where projects are evaluated on their intent and potential to contribute to EU policy objectives to promote economic and social cohesion.[77]

The project selection and lending process can be broken down into four main stages: Application, Appraisal, Selection, and Implementation and Monitoring. The Application Stage addresses the project's eligibility and suitability for financing. The Appraisal Stage consists of a financial review and application review that informs the decision-making conducted during the Selection Stage. Finally, the Implementation and Monitoring Stage can include project review, project credit analysis, and construction progress reports.



5.2.1 TIFU

TIFU projects are selected primarily **on the financing need based on the difficulty in obtaining ready and affordable credit from the capital markets**. As described previously, TIFU serves to support PFI projects that are unable to obtain sufficient financing for a project to achieve a timely financial close.[78]

Application

The Application stage focuses on project eligibility. PFI projects are eligible for TIFU loans if they meet at least one of three criteria:[79]

1. Began the procurement process by March 3, 2009, which is the date of the HM Treasury letter announcing TIFU's creation.
2. Initiated project procurement after March 3, 2009 and were approved by the Project Review Group.
3. Meet the standard VFM and affordability criteria and are subject to obtaining HM Treasury approval prior to starting the procurement process.

All eligible projects are included in the HM Treasury's database of PFI projects, which is published on the Treasury website. As of February 2010, there were 115 PFI projects under procurement.[80]

HM Treasury intends to lend to projects only where appropriate funding is not available from the capital market in order to help PFI projects reach financial close on a timely basis. HM Treasury requires that each project team present a business case for TIFU loan, which includes:[81]

- Structuring and financing options considered by the project team before applying for TIFU loan
- Responses from commercial banks on loan applications
- A written summary explaining why the terms offered by commercial banks were not representative of the terms generally available for PFI transactions and a verification of this view by the project's financial advisor
- A description of the nature and causes of the funding gap and the amount of funding required

Appraisal

The evaluation criteria for TIFU loans is **based solely on the financial need of the particular PFI project and the availability of commercial and other funding sources**. PFI projects must demonstrate and prove to HM Treasury that they have tried and been unable to obtain sufficient financing from private capital markets after a post-preferred bidder funding competition has been held.[82]

Selection

The Corporate Private Finance (CPF) Team of HM Treasury formerly reviews and evaluates the application. If the CPF Team selects and approves the application, it can invite TIFU to meet the procuring authority to discuss the project and arrangements for TIFU involvement. The Private Finance division of CPF, which was involved in project review, was recently moved under Infrastructure UK (IUK). Today, CPF remains an entity within HM Treasury, but not as a part of the project evaluation and selection process.[83]

Implementation and Monitoring

Once projects are selected, TIFU can conduct a review of the project including an assessment of project structure and risks. Project monitoring can include documents and tasks such as[84]:

- Project credit analysis and due diligence
- Maintaining accurate loan documents
- Arrangement fee received by TIFU
- TIFU receives regular, quarterly, semi-annual project reports
- Construction progress reports

The TIFU application, evaluation and selection, and implementation and monitoring process is not unlike the New Starts project cycle, which begins with project development and then progresses to project evaluation and selection, and finally, implementation and monitoring with ongoing reporting requirements. While TIFU provides loans that may be self-replenishing through loan repayment, the New Starts Program awards grants, which requires an annual budget appropriation and is dependent on the availability of government funds and possibly in conflict with other funding priorities.[85]

5.2.2 EIB

The EIB can select projects as long as a project is in line with eligibility requirements and further contribute to policy objectives. The EIB lends to projects largely based on their ability to meet EU policy objectives such as social and economic cohesion.[86]

Application: Loan Application and Project Eligibility

The EIB finances projects across a wide range of sectors from transportation to telecommunications to health care. **Eligible projects must contribute to EU policy objectives**, which include promoting economic and social cohesion, and improvement of EU transport and telecommunications infrastructure. In addition, projects should work to secure production, transfer, and distribution of energy and alternative energy and the development of a competitive, innovative, and knowledge-based economy. Projects should invest in human capital development through the construction of schools, labs, and research centers and natural and urban environmental schemes such as water sanitation and clean air. Finally, projects should support the development of small and medium-sized enterprises and external cooperation and development policies.[87]

In 2008, EIB lent €9.8B (US$14.3B, 2008) for transport projects linked to trans-European networks, with more than half of this spending in countries that are economically depressed. An additional €3.2 billion went to priority projects as defined by the European Commission. The increased spending in the transport sector by EIB in 2008, up from €7.2B in 2007, was caused by increased demand from project sponsors as a result of adverse market conditions.[88]

The EIB requires prospective lending recipients to prepare and submit documents that detail and describe the:[89]

- **Borrower** - loan applicant and project sponsor with legal status, list of principal partners and stakeholders, and organizational structure
- **Project** - technical and environmental data outlining its general purpose, environmental impact, and a detailed cost estimate; financial data breaking down operating and maintenance costs and a financing plan and schedule of projected expenditure
- **Financing Structure** - description of the project's commercial structure and risk allocation, detailed breakdown of financing sources, and proposed role of the EIB in the actual financing structure; a financial model including cashflow forecasts to enable analysis of underlying assumptions

The project sponsor/promoter, who can include public and private sector participants such as banks, are responsible for submitting the necessary application documents. As the EIB finances up to 50% of total project capital required, a plan is required to outline the EIB's role as a lender and/or technical advisor and to account for the balance required, which may be sourced from the project sponsor or a loan from a country government.[90]

Appraisal

The review of the project proposal for compliance with EU objectives and **assessment of the economic, technical and financial merits of the project and its impact on the environment** are two key steps in the project appraisal process. Project appraisal is conducted by the EIB's teams of engineers, economists, and financial analysts, employed and hired as external consultants by the Projects Directorate, in cooperation with the project team.[91]

During the project appraisal, the Project Directorate is responsible for working with the project team to detect risks and issues and enable necessary corrective action.

Project evaluation is based on eight quality factors used to inform the financing decision by the Board of Directors, highlighted in Figure 5 below.[92]

Quality Factors	Description
Technical Scope	Soundness of technical scope, use of innovative technology, completeness of risk and mitigation measures, capacity for products/services
Implementation	Capability of project team to implement the planned project, quality of timing and employment estimates during implementation
Operation	Capability of project team to operate and maintain the project, quality of operating and maintenance cost and employment estimates
Procurement	Compliance with applicable legislation and EIB guidelines
Environmental Impact	Compliance with applicable legislation and results of environmental impact assessment
Market and Demand	Results of analysis on the demand for products/services over the life of the project, with reference to sector studies completed by the Projects Directorate
Investment Cost	Quality of project cost estimates and detailed components, and comparison with costs of similar projects
Profitability	Quality of financial profitability estimates and related indicators (e.g., rate of return), and information on economic profitability

Figure 5: EIB's Project Evaluation Quality Factors[93]

Livability & Sustainability: Sustainable development has been a fundamental objective of the EU since 1997. The Renewed EU Sustainable Development Strategy was adopted by the European Council in June 2006, and outlines seven key issues that focus on overall sustainable development:[94]

1) Climate Change and Clean Energy - carbon credits and development of alternative energy such as wind firms
2) Sustainable Transport - transportation systems that contribute to the reduction of greenhouse gas emissions and other local pollutants including updates and modernization of ports to increase capacity and intermodal transport linkages
3) Sustainable Consumption and Production - boost demand and improve overall environmental performance and impact of consumer products and help consumers make more informed environmentally friendly choices
4) Conservation and Management of Natural Resources - incorporating aspects of biodiversity in an environmental impact assessment
5) Public Health - providing state of the art health care to help improve the social and urban environment through the expansion and refurbishment of hospital and clinics
6) Social Inclusion, Demography, and Migration - development of social and human capital and equitable economic development such as a study on the economic and social impact of labor force out-migration from acceding EU nations
7) Global Poverty - poverty reduction strategies to support the UN's Millennium Development Goals

During project appraisal, environmental and social screenings are carried out to identify the extent and complexity of the project's environmental and social impacts and risks. Location and issue-based risk checklists are prepared to answer questions concerning consultation of affected people, degradation of critical natural habitats, financing of commercial forestry, impact on indigenous communities, and impact on cultural and historic properties.[95]

The EIB also aims to **identify, quantify, and value direct and indirect environmental and social externalities** where their influence on the socio-economic viability of the project is expected to be significant, and promotes measures to internalize such impacts. For example, the EIB discourages projects that may have significant negative externalities such as endangering public health and quality of life by an increase in air or water pollution. Projects that proactively reduce these external costs through regulation and other measures are looked upon more favorably.[96]

When considering sustainable transportation projects, the EIB adheres to the following guiding principles developed by the European Commission:[97]

- **Mobility** - pursue an approach that strives for the most efficient, economic, and sustainable way of satisfying transport demand
- **Trans-European Networks** - encourage the development of an efficient and cohesive community-wide transport network and system
- **Freight Transport** - fund railways, inland waterways, and maritime projects to help reduce greenhouse gas emissions per transport energy unit expended
- **Research & Innovation** - emphasize funding research development and innovation activities to focus on energy efficiency, emissions reduction, and safety enhancement
- **Environmental Impact** - identify consequences of projects it funds in terms of energy consumption and environmental impact

Selection

The criteria for a typical EIB evaluation is tailored for each specific project with evaluation results passed on to the Board of Directors in a project report. The report contains an evaluation of the project's consistency with EU objectives. It also provides an assessment of the overall quality and soundness of the project based on a number of factors including technical scope, implementation plan, operation capability, and the project's environmental impact.[98]

The Board of Directors has the sole authority in the EIB to decide whether or not a project is granted a loan, guarantee, or other lending product. Decisions are taken on a majority vote to decide the loan amount, interest rate, and other related charges. These decisions by the Board of Directors are informed by reports compiled and developed by the Management Committee.[99]

Project Implementation and Monitoring

The Risk Management Directorate, which reports to the Management Committee, is responsible for the financial monitoring of the loan and the structuring of operations as needed. The Project Directorate, which also reports to the Management Committee, is responsible for project performance monitoring. **The EIB conducts a review of the overall project, project structure, and risks and conducts its financial due diligence and credit analysis of the project**.[100]

The EIB monitors projects from loan award through project implementation until the loan is repaid. Monitoring requirements can include[101]:

- Tracking the servicing of the loan
- Monitoring that funds are being used for the stated project objectives
- Assessing that physical project construction is in accordance with the contract
- Regular monthly, quarterly, or semi-annual project reports and construction progress reports
- Maintaining loan documentation

The EIB also monitors the environmental and social performance of the projects it finances, especially the fulfillment of any specific obligations described in the contract. Monitoring is typically conducted through periodic reports by the government procurement project team and site visits by the EIB. At the completion of a project, the EIB conducts an ex-post evaluation to capture lessons learned and to better inform future projects. These reports are available on the EIB website.[102]

5.2.3 U.S. Experience

In the U.S., project selection is provided for each program. For example, the TIGER Discretionary Program was established to select projects based on the long-term economic and sustainability outcomes and near-term job creation and economic recovery.[103] Other U.S. DOT programs, such as New Starts and TIFIA, adopt a specific project selection process that reflects the objectives of the particular program.

The principals of livability issued in the U.S. by the Partnership for Sustainable Communities follow similar themes of sustainable transportation, mobility, and social inclusion as the EU.[104] While DOT, HUD, and EPA refer to neighborhoods and communities, the EU holds a broader focus with an emphasis on trans-European networks and a level of social inclusion that impacts global poverty and trade through sustainable consumption and production.

5.3 Financial Products Offered by a Government-Sponsored Lending Institution

Government-sponsored lending institutions may provide credit assistance across a wide range of financial products including loans, guarantees, and lines of credit.

5.3.1 TIFU

TIFU receives the resources it requires to finance its lending activities through HM Treasury's national budget appropriations. TIFU provides assistance solely to public sector entities such as local governments, which in turn provide funds to private entities in their role as project sponsors for PFI projects. TIFU offers long-term loans on either a fixed rate or floating rate basis, and provides standard ancillary lending facilities for PFI projects. **TIFU provides loans to eligible PFI projects** and expects loans to be provided alongside those from commercial banks, the EIB, or capital market lenders.[105]

5.3.2 EIB

The EIB raises capital through a combination of two sources. Each member country contributes funds to the EIB in amounts based on the country's gross domestic product (GDP) relative to the EU. For example, Germany contributes the largest amount since the country accounts for the largest percentage of the EU's GDP. Additionally, the EIB also finances its lending activities by selling bonds on the capital markets. The EIB provides assistance to both public and private entities.[106] For example, the EIB establishes lines of credit and loan facilities for developing private banks in Eastern Europe.[107]

The EIB offers a variety of financial products and services to further policy objectives of the EU, including:[108]

- Grants: Typically for social development projects (e.g., public relations campaign for refugee re-settlement) or to cover costs of technical assistance in the form of project development and in applying for EIB financial assistance
- Guarantees: Used for senior and subordinated debt similar to 'monoline' insurers (i.e., insurance company that specializes in insuring the performance of financial instruments)
- Loans: Various types of loans (e.g., fixed, revisable, and convertible rate loans) and used to cover up to 50% of total project costs. Lines of credit through an intermediary bank, may be used for primarily for projects with a total estimated cost less than €25M ($35M, 2010)
- Equity: Venture capital investment funds generally used for high-technology small- to medium-enterprises and renewable energy
- Microfinance: Funding and technical support to microfinance institutions (e.g., organization that provides financial services to the poor) in the form of loans, guarantees and equity participations
- Technical Assistance: Services provided by EIB's team of expert economists, engineers and industry specialists

Each of the EIB's main financial products and services is discussed below.

Grants

The EIB typically does not provide programmatic grants. This role is assumed primarily by the European Commission and is for support activities such as environmental preservation, information and communication technologies development, and youth education.[109] The main uses of available EIB grants are to finance interest rate subsidies, cover the costs of project-related technical assistance and to support initiatives of 20 to 30 EU and EU partner non-profit organizations.[110]

Interest rate and project-related technical assistance subsidies are targeted to lending for developing nations in Africa, the Caribbean, and the Pacific. Financial subsidies totaling €400M (US$560M, 2010) that were provided by the EU Member States are to be used over a five-year period from 2008 to 2013. Up to €40M (US$56M, 2010) of the total can be allocated to technical assistance.[111]

Support to non-profit organizations is relatively small at €100,000 (US$140,000, 2010) annually for 20 to 30 initiatives. Examples of past initiatives funded include: the Slovenian Ministry of Finance Conference on Education and Economic Policy, the Kenyan Red Cross for a program for internally displaced people, and the International Polar Foundation to support exhibits of Arctic research.[112]

Guarantees

The EIB provides guarantees for senior and subordinated debt and serves as either a standard guarantee or a debt service guarantee similar to monoline insurers.[113]

One type of guarantee that the EIB issues is the Loan Guarantee Instrument for Trans-European Transport Network Projects (LGTT). This is jointly set up by the European Commission and the EIB to facilitate greater private sector financing of multimodal EU transportation network integration. It received a €1.0B (US$1.5B, 2008) capital contribution in 2008 to support up to €20B (US$29.3B, 2008) of senior loans in order to encourage the reduction of risk margins applied to senior loans for the project. In the event that the borrower becomes insolvent, the LGTT guarantees and provides full repayment, becoming a subordinated lender to the project.[114]

Another type of guarantee that the EIB provides is the Small- and Medium-Sized Enterprise (SME) Corporate Lending Guarantee. These guarantees are provided by the European Investment Fund (EIF) to support SME loan guarantees for mid- to long-term debt finance, equity guarantees to cover a portfolio of investments for small- and medium-sized enterprises in start-up phases, and securitization to support securitization transactions to mobilize additional SME debt financing.[115]

Loans

The EIB provides individual loans with fixed, revisable, and convertible rates for projects in all sectors of the economy for projects €25M (US$35M, 2010) or larger. For projects less than €25M, the EIB offers intermediated loans or lines of credit through an intermediary regional bank or financial institution. Intermediated loans are generally directed toward small- and medium-sized enterprises.[116]

Loans are issued on **proof of supporting co-investment provided by a commercial bank or banking syndicate with a solid credit rating**. Although commitment and non-utilization fees are not typically charged, projects may be required to pay evaluation and legal fees.[117]

EIB loans have flexibility in holding financial accounts in more than 7 different major currencies including the Euro, British Pound, Japanese Yen, Swedish Krona, Danish Krone, Swiss Franc, and currencies of EU candidate countries and other EIB partner nations.[118]

Equity: Small- and Medium-sized Enterprises

The EIB provides **equity in the form of venture capital funds** through intermediary financial institutions for high-technology small- and medium-sized enterprises with strong growth potential. EIF is responsible for the management of the venture capital portfolio.[119]

One example of EIB project equity is the Middle East Venture Capital Fund, which invests in early stage IT companies in the Palestinian Territories. The EIB's main objective is to support the development of the financial and private sectors by providing equity or quasi-equity financing to export oriented IT companies based in the Palestinian Territories. The projected total investment is US$35M to $50M, with €5M from the EIB (2009).[120]

Another example of EIB project equity is the Bullnet Capital Fund II, which invests in early stage IT hardware and software firms in Spain. The objective of the fund is to invest in early stage companies that develop unique technology (software and/or hardware) with applications in several industries including telecommunications, media, and healthcare. The projected total investment is €25M (US$34.7M, 2009), with €2.7M from the EIB (over 2007-2009).[121]

Small- and medium-sized enterprises must meet all social requirements identified by the EIB, including requirements around labor standards, occupational and community health and safety, population movement (including involuntary resettlement issues), minority rights, public consultation, and cultural heritage in order to receive funding from the EIB.[122]

Equity: Infrastructure

The EIB also provides equity financing through several sector and region specific targeted **infrastructure funds and renewable energy products**.

The Argan Infrastructure Fund invests in energy, transportation, logistics, waste management, and telecommunications projects in Mediterranean countries such as Morocco, Algeria, Tunisia, Libya, and Egypt, and also certain projects in Sub-Sahara Africa. Equity financing is for infrastructure projects that contribute to EU objectives and follow EIB environmental guidelines, which encourage the use of clean and renewable energy. The projected funding target is €75M (US$104.2M, 2009) on the first project with up to €20M financing from the EIB.[123]

The InfraMed Infrastructure Fund invests in sustainable urban, transport, and energy infrastructure in Mediterranean countries such as Libya, Mauritania, and Turkey. Equity financing is for infrastructure projects that contribute to EU objectives. The project funding target is €400M (US$555.6M, 2009) with up to €50M EIB financing.[124]

The Marguerite 2020 Fund invests in transport and renewable energy projects throughout the EU. Equity financing is for the implementation of strategic European policy objectives and projects in transport and renewable energy via regional and national European banks. The project funding target is €1.5B (US$2.1B, 2009) with €600M to €700M invested in the first project and up to €100M in EIB equity.[125]

Microfinance Initiatives

Microfinance is the provision of **basic financial services to the poor**, typically those living in developing nations with limited access to affordable financial products and services such as loans, insurance, and money transfers. According to the EIB Group, microfinance in the EU is an array of products and services for individuals who wish to become self-employed but do not have access to traditional banking services. It consists of those making small loans of less than €25,000 (US$35,000, 2009).[126]

From 2000 to 2009, the EIB Group committed €654M (US$908.4M, 2009) to microfinance initiatives including €26M for technical assistance. The EIB Group offers a similar array of products in the form of loans, equity, and guarantees, but on a smaller scale.[127]

Technical Assistance

The EIB offers a range of upstream technical assistance from EIB staff economists and engineers who may **assess and advise on individual projects**. For project applicants within the EU, the EIB performs detailed due diligence prior to investment and all projects must comply with environment and procurement directives of the EU. For project applicants from designated non-EU developing partner countries in Africa, the Caribbean, the Pacific, and around the Mediterranean, the EIB provides technical assistance for project preparation, which can include feasibility and market studies, project management, and business case development.[128]

In particular, technical assistance for non-EU developing partner countries has three main objectives:[129]

- To enhance project quality and success rate
- To increase project efficiency and success rate
- To complement other available financial products

5.3.3 U.S. Experience

The current federal government programs and lending institutions in the U.S. offer a variety of loans, including student loans from the Department of Education,[130] small business loans from the Small Business Administration (SBA),[131] and surface transportation project loans through TIFIA from

DOT.[132] While student and small business loans may not include and/or encourage private co-investment in all cases, TIFIA has a primary goal of encouraging substantial co-investment from both the private sector and non-Federal government entities.[133] A major program objective of TIFU and the EIB is to complement, rather than supplement, commercial lending.

There are a small number of programs and institutions that offer equity products in the U.S. The Overseas Private Investment Corporation (OPIC) Investment Funds program invests in emerging market companies in developing countries across a wide range of sectors from agribusiness to financial services to media and telecommunications.[134]

5.4 Lending Terms of a Government-Sponsored Lending Institution

The lending terms offered by a government-sponsored lending institution may be categorized as[135]:

- **Market Rate:** The borrowing rate for debt on the open-market, similar to the rate offered by commercial banks.
- **Preferential Terms:** Where lending is below market rate and/or subsidized policy driven programs (e.g., home ownership). Although borrowing rates may be lower, the government as the lender assumes as much risk, if not more, than through market lending.

Government-sponsored lending institutions may offer lending periods similar to that of commercial lenders on order of 15, 20, and 30-year terms.

5.4.1 TIFU

TIFU offers loans over **15 to 30 year terms on fixed or floating interest rates, matching the same fees, pricing and period of commercial lenders**.[136]

If loans are provided on a fixed rate basis, TIFU is entitled to receive interest rate break costs on early pre-payment, and ranks alongside commercial swap counterparty break costs. If loans are provided on a floating rate basis, they may be subject to hedging arrangements, which c entered into by either co-funders or other swap counterparties as agreed by TIFU and the recipient project team. While TIFU has been given such lending authority in the way it was established, in practice, TIFU is anticipated to provide floating-rate loans alongside commercial banks and the EIB. This is due to the fact that for projects to be delivered under the PFI, a market assessment is required to assess the potential interest for private investment. If this cannot be established, then a project is unlikely to be delivered as a PFI and ineligible for TIFU assistance.[137]

TIFU loans share in security and rank pari passu, or equitably, with commercial lenders both pre-enforcement (before the contractor is insolvent) and post-enforcement (after the contractor becomes insolvent). TIFU loans have full, unencumbered, syndication and sale rights. In the event that the project is refinanced, TIFU loans are pre-payable along with the project's commercial bank loans.[138]

5.4.2 EIB

EIB lending is usually over **4 to 20 year terms at competitive fixed, convertible, and variable interest rates**. These variable interest rates are available at a spread below LIBOR.[139]

EIB variable rate loans are usually **at a rate preferential to normal commercial debt**. The EIB may or may not include an additional risk margin on their base lending rate, depending on the specifics of the loan including potential corporate insolvency. The EIB holds a simulated 'sovereign credit rating' that is based on the sovereign backing of the EU Member States. Through the EIB, EU Member States assume more of the lending risk by subsidizing lending with sub-market rates in order to support strategically important projects.[140]

Historically, the EIB has not experienced high rates of loan defaults. Recently, however, the EIB has taken on greater risks due to the global financial crisis, increasing the chances for corporate default. The EIB closely follows the activity of its loans with higher risks of default, which make up approximately 0.4% of all its loans.[141] In the case of a loan default, the EIB would follow commercial lending practices by trying to resell the assets to another institution, such as a private entity or bank, to recover some of the funds it lost in the transaction.[142]

5.4.3 U.S. Experience

U.S. government lending programs offer mostly subsidized rates to address market gaps and to deliver on the department's objectives. The results of a for fee application pilot for TIFIA is expected later this year. This pilot was initiated as a result of the growing number of applicants and limited federal resources and it designed to see if applicants are willing to pay a fee to contribute to the program's overhead cost, so that a greater amount of the government's funds can be allocated to investing in projects.[143]

Key Observations: Project Selection and Financial Products of Government-Sponsored Lending Institutions
• The approach for TIFU is unique and specific to its objective of delivering PFI projects that have not been able to secure private finance. Similarly, the eligibility requirements of the EIB reflect its objectives, which are broad policy objectives for the EU. • The administration of TIFU is streamlined to focus on the investment fundamentals of the PFI project, rather than assessing if a project should be delivered and the preferred procurement method. • TIFU selects projects based on access to sufficient financing. It provides an example of how existing eligibility requirements and funding limits for grant and financing programs can be leveraged to establish financial products offered by a national infrastructure bank, which may enable the bank to be established in a short period of time. • The EIB is a singular body applying a uniform set of evaluation criteria and project monitoring. Standardized evaluation criteria may have the benefit of allowing U.S. DOT, HUD, and EPA to coordinate project investment, encourage collaboration between project applicants to make best use of available funding. • The EIB offers a spectrum of financial products. Establishing a national infrastructure bank that provides a number of different products may provide a dedicated institution to assess if federal grants are the most efficient and effective mechanism to provide federal support and leverage the federal government's support to a project. • The EIB is a single institution that offers a spectrum of financial assistance, with financing terms dependant on the merits of each project. This allows cross-subsidization to occur within the institution. The current approach to federal assistance in the U.S. makes this approach difficult to implement, as each program is implemented to address a specific market gap or objective and is administered separately.

6.0 Conclusion and Key Considerations for the U.S.

6.1 Conclusion

Insight from how TIFU and the EIB provide credit assistance, including key aspects such as the project selection process and financial products, provide potential practices for the U.S. Below is a summary of the key topics covered in this Report:

- **Purpose:** Government-sponsored institutions serve both public and private sector entities in order to support projects that have public, social, and economic benefit and purpose through credit assistance. Such assistance can include financial products such as loans, guarantees, and lines of credit and can be used to finance developments such as subway lines, utility grid upgrades, manufacturing plants, and hospitals.

- **Governance Structure***:* Government-sponsored lending institutions can be established within an existing government agency such as TIFU in HM Treasury in the UK or a standalone independent bank such as the EIB in the EU. In both cases, the institutions require the appropriate skills and staff to make lending decisions, review projects and monitor them during operations, and know how to interact with project sponsors and partners such as commercial banks. An institution operating with the appropriate staff may build market confidence and trust in the institution to manage major transactions and to act as a project lender.

- **Scope of Eligible Projects:** Government-sponsored lending institutions often cover multiple sectors to help promote consistency of overall investment prioritization. TIFU and EIB invest in projects across sectors and are administered by a central entity. This can result in coordination in project selection, investment and monitoring.

- **Project Selection Process:** Commercial risk assessment and structuring risk analysis can be critical in selecting projects that receive government financing and for managing the government lending portfolio. TIFU utilizes commercial experts and commercial lending processes to review project risks and lending decisions. The EIB uses commercial processes and experienced staff to review project risks and lending decisions, removing these decisions from a single national government. Knowledgeable and experienced staff following similar commercial lending practices has established a level of confidence from the private sector in working and investing alongside the public sector.

- **Financial Products:** Government-sponsored lending institutions can be utilized to pursue common programs and objectives across government and shareholders, which drives the type of financial products offered. TIFU builds on the UK's existing government PFI program and provides loans. The EIB supports broader EU objectives, provides grants, loans, lines of credit, guarantees, and equity.

- **Lending Terms:** Government-sponsored lending institutions combine funding from government contributions and/or markets to raise capital. TIFU is funded from the UK Treasury while the EIB relies on contributions from member states and capital markets. With TIFU, the benefit of using funds from the UK Treasury is flexibility in their use. The EIB's reliance on contributions and capital markets supports it operating similar to a commercial bank, as it anticipates revenue streams in the form of borrower repayment that can be used to reconstitute future potential lending.

6.2 Key Considerations for the U.S.

Based on the research conducted for Stage 3 of the Analysis of Transportation Investment Models in Other Countries, the approach of government-sponsored lending institutions in the UK and the EU to address market gaps and leverage substantial private co-investment highlights some important considerations for U.S. DOT in establishing a national infrastructure bank.

U.S. DOT is encouraged to carefully consider the role of the federal and state transportation and funding agencies, the public and other key stakeholders such as the private investment market in reviewing the key considerations.

- **Purpose:** Establishing a multi-sector lending institution that provides a variety of financial assistance to projects may be of benefit to U.S. DOT in seeking to maximize the value from its investments and adopting a merit based approach to its investment decisions. One option may be to build on the multi-sector approach adopted by the TIGER Discretionary Grant Program and the Partnership for Sustainable Communities in clarifying the purpose of the national infrastructure bank.
- **Government Structure:** The governance structure of TIFU resembles the TIFIA program in that it operates within a national government department and is funded through government appropriations. The EIB represents a governance structure that is independent of the region's political system and raises funds through the capital markets as well as contributions from the Member States. A governance structure similar to the EIB does not presently exist in the U.S. and this may be due to the relationship between the federal and state governments as well as the structure of the U.S. political system. The governance structure of the EIB may represent a potential longer term structure for the national infrastructure bank, which may evolve over time once the bank is operational and all stakeholders (federal, state, the public and the market) have had an opportunity to assess the merits of the institution. In the near term, there may also be opportunities to build capability and capacity within U.S. DOT through greater intra-department coordination and inter-department government transfers and temporary placements. For example, staff from the FHWA's Office Innovative Program Delivery in DOT and the U.S. Treasury's Office of Financial Stability may be temporarily placed within the bank, where their relevant lending knowledge and experience is required. This coordination and knowledge transfer may encourage market confidence in establishing a U.S. national infrastructure bank.
- **Scope of Eligible Projects:** As the availability of grants declines and competition for funding allocations increases, U.S. DOT may establish eligibility requirements for the national infrastructure bank that are based on an evaluation of whether or not grants or financial assistance may be more cost effective for particular projects. For example, this evaluation may include consideration of the type of assistance that the bank may provide to encourage greater private sector investment or leverage state or local funding.
- **Project Selection Process:** In the U.S., the project selection process is provided for each program. A coordinated approach to the project selection process under a national infrastructure bank may allow for the comparison of projects across different sectors, streamline the application process for federal financial support and reduce the administration costs of U.S. DOT. One approach in institution a coordinate project selection process may be to build on the project selection process utilized for the TIGER Discretionary Program and the TIFIA program and develop a process that accommodates the selection of projects for either funding or financial support.
- **Financial Products**: In the U.S., a national infrastructure bank offering a variety of financial products may help to maximize the value of the federal government's investment in transportation projects, utilize staff and funding resources and encourage long-term,

integrated project planning across multiple sectors. U.S. DOT may look to prioritize investments and efficiently allocate scarce resources of existing funding and financing programs, such as TIFIA, New Starts, Railroad Rehabilitation and Improvement Financing (RRIF), and PABs and coordinate these programs in an effort to increase the efficiency and effectiveness of the financial support provided to transportation projects.

- **Lending Terms:** Given the current fiscal constraints in the U.S., consideration of how and if market rate products may be offered, potentially under new or existing programs to maximize the use and effectiveness of federal resources may prove beneficial. One approach may be to request that borrowers cover a portion of the government overhead costs by way of a loan application or interest rate subsidy. The current TIFIA pilot that requires applicants to pay an up-front fee to cover the Government's subsidy costs is likely to indicate the acceptance of such approaches for federal lending programs.

Appendix A: Glossary

- Capital market: Market where financial securities are traded by individuals or organizations. Examples include the stock market where stocks are bought and sold typically by private entities and the bond market where private entities may purchase and trade debt
- Convertible rate loans: Loans that allow for changes to the interest rate formula during the life of the loan at predetermined points or periods in time
- Debt prices: Cost associated with obtaining financing or credit typically captured in interest rates and associated bank service fees
- Fixed interest rate loans: Loans that maintain a fixed interest rate over the life of the loan. For example, a 30-year fixed home mortgage in the U.S. provides the same interest rate over the 30-year lifespan of the loan typically with a fixed monthly payment expected by the borrower. The benefit of such a loan is that the rate and expected repayment schedule are fixed over the life of the loan.
- Floating interest rate loans: Loans that have a changing interest rate over the life of the loan. This rate may be indexed to a standard rate such as the London Interbank Offered Rate (LIBOR) and may follow a minimum and maximum allowable range. In this case, the borrower assumes more risk since the rate fluctuates with the market, but has the added potential benefit of paying a lower interest rate than someone on a fixed long-term loan for a period of time.
- Monoline insurer: Insurance Company that specializes in insuring the performance of financial instruments such as municipal and private bonds, and mortgages and mortgage-backed securities. For example, in the event a municipality defaults or is unable to make interest and/or principal payments to a holder of a municipal bond or other similar financial instrument, the insurance company can step-in and guarantee that repayment is made. The municipality pays an insurance fee to the insurance company for this service.
- Revisable fixed rate loans: Loans that have a fixed rate that may change at predetermined points in time over the life of the loan
- Senior debt: Debt that is paid before any other debt obligation
- Subordinate debt: Debt that is paid after any senior or other debt obligations

Appendix B: Task 3 Source List

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[29] Refer to Appendix A: Glossary for a definition of these interest rates
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[142] (Based on Survey of PwC Country Office Staff)
[143] Federal Register Notice, TIFIA Upfront Fee, December 2009: http://www.fhwa.dot.gov/ipd/pdfs/tifia/fy2010_tifia_nofa.pdf