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**COMMISSION STAFF WORKING DOCUMENT**

**Model for Financial instruments and grants with co-financing from the EIBG and others for affordable housing**

# Model for Financial instruments and grants with co-financing from the EIBG and others for affordable housing

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## Abbreviations

EU	European Union
CPR	Common Provisions Regulation – Regulation (EU) 2021/1060 of the European Parliament and of the Council of 24 June 2021
SPV	Special Purpose Vehicle
EIB(G)	European Investment Bank (Group)
EIF	European Investment Fund
HF	Holding Fund as defined in point (20) in Article 2 CPR
SF	Specific Fund as defined in point (21) in Article 2 CPR
MS	Member States
MA	Managing Authority
FI	Financial Instrument
NPBI	National Promotional Banks and Institutions
ERDF	European Regional Development Funds
JTF	Just Transition Fund
IFI	International Financial Institution
CPR	Common Provisions Regulation
FR	Final recipient
IRS	Interest Rate Subsidy
TA	Technical Assistance
AIRB	[bottom of p. 12 – “banks applying the AIRB approach”]

## Introduction

*Europe faces a housing crisis, with people of all ages and families of all sizes affected. Prices and rents are soaring. People are struggling to find affordable homes*

*The Commission will develop a European Affordable Housing Plan, to look at all the drivers of the crisis and to help unlock the private and public investment needed. If it matters to Europeans, it matters to Europe.*

President von der Leyen, at the European Parliament, 18 July 2024

*The momentum is here both for housing to be tackled as the top priority, and for deepening the Capital Markets Union.*

EIB President Calviño, at the Scaling up Support on Affordable and Sustainable Housing seminar, 18 July 2024.

Affordable housing is a fundamental pillar for delivering the UN's 2030 Agenda and achieving the Sustainable Development Goals related to energy efficiency, combatting poverty, achieving sustainable cities and health quality. The European Union also recognizes that access to affordable housing is a prerequisite for macro-economic performance, financial stability, mobility, functioning of the labour market, territorial cohesion, climate, energy and environmental policies. The European Pillar of Social Rights states that access to social housing or housing assistance of good quality shall be provided for those in need.

In recent time, the European Union is facing a widespread housing crisis. Across Europe, the challenge of finding affordable housing has reached a critical point, impacting economic stability and social cohesion. House prices and rents have grown in the last decade; from 2010 until 2023, in the EU, rents increased by 24.8% and house prices by 52.2%. with a significant acceleration during the pandemic. This sharp increase places homeownership and affordable renting out of reach for many families and individuals, particularly in major urban centres where 10.6% of residents now spend over 40% of their disposable income on housing<sup>1</sup>. In 2022 nearly 40 million Europeans spent 40 % or more of their household disposable income on housing and that the most affected are young people from the low and middle-class.

Income growth did not keep pace with house prices in Member States and the high inflation of recent years has also undermined the purchasing power of households. As a result, housing affordability for prospective homeowners and renters is lower than a decade ago. In addition, supply of affordable and social housing for lower income earners has been insufficient over the last decade in most Member States. The housing affordability shortage issue was highlighted in E. Letta report.. The report proposes different EU rules and tools are revised, to make sure that they incentivise socially inclusive and sustainable housing systems rather than exacerbate the current housing crisis. *“While housing policy falls within the purview of Member States, the EU possesses a range of instruments and policies that have a direct or indirect impact on the housing markets across the EU”*.

The decoupling of housing cost and income growth erodes social and territorial cohesion and contributes to political discontent at regional and local level. Rising house prices and rents may prevent young people from moving out of their family home to study or find a first job in line with their qualifications. Housing unaffordability also hampers labour mobility towards jobs located in metropolitan areas, in particular middle and low-wage jobs in essential sectors experiencing shortages (e.g., health, care and educational services). As such, the increasing gap between housing costs and incomes has an adverse impact on the functioning of the labour market and undermines competitiveness of the economy. In addition, unequal access to housing exacerbates existing inequalities of opportunity and social exclusion. The most vulnerable disproportionately suffer from this situation, while the risk of homelessness increases. As well as the effect on labour mobility, the current housing crisis also affects the right to stay where housing is inadequate on the areas where citizens have grown up forcing them to move away. At the same time, rural and remote regions also face diverse challenges related to housing and infrastructure.

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<sup>1</sup> Enrico Letta's Report on the Future of the Single Market.

The combined Financial Instruments<sup>2</sup> (FI) options, proposed and described in this document aim to help Member States address market failure and speed up the provision of affordable housing. The housing market in EU Member States (MS) has been characterized by an inelastic supply curve, meaning that change in demand usually results in substantial change in price but less substantial change in volume<sup>3</sup>. **Regulatory and public intervention therefore need to focus on housing supply.** Some Member States have successfully managed to create institutional structures for the sector that includes appropriate regulations and specialized entities to help ensure a steady supply of affordable housing for most social groups. Affordable housing, particularly new build, is characterised by significant development costs but with a longer-term economic life of the assets. In terms of financing, it therefore usually requires some form of up-front public support to moderate the ultimate costs for the target populations as well as longer term financing needs to match the economic life of the housing units.

Transfer of best EU practices - in terms of institutional structure, financing structures that combine grants with repayable forms of finance (including public and private finance) - can be replicated, adapted and accelerated using EU Cohesion Policy Funds, combined with European Investment Bank Group (EIBG), National Promotional Banks and Institutions (NPBI) and private financing and expertise under these FI options (including through the InvestEU Programme). Technical support for the preparation and implementation of housing reforms is also available under the Technical Support Instrument managed by the European Commission. This combination can be done in one of several ways:

- Managing Authorities, financial intermediaries or project promoters may borrow from EIB, NPBIs and other IFIs to co-finance the Cohesion policy funds, and their financing may be used in some cases, to ensure the co-financing part in the programmes.
- Financial intermediaries may cover the entirety of the funding of the financial products while Cohesion policy funds may be provided in the form of grants, in either one or two operations under the Common Provisions Regulation (CPR) or other relevant EU regulation.
- Apart from the contribution of Cohesion policy and other EU and national grant funding, public authorities and promoters may provide in-kind contributions, including land, to ensure the affordability of this housing supply.
- Financial instruments, including specialised investment and infrastructure funds, may also be created to combine and leverage these funds.
- Special Purpose Vehicles (SPVs<sup>4</sup>) collecting different sources of financing may be set-up at national/regional levels specifically to develop/finance new housing units and have external investors financing them directly either through equity shares or mezzanine/senior funding. These SPVs may also benefit from equity investment/capitalisation from the Cohesion policy funds to reduce the risk and cost of financing from these other private investors.
- Channelling financing through the MS compartment of the InvestEU Programme, benefitting from a single set of rules, established contracts and financial products already in place (EIBG, IFIs and NPBIs), as well as possibility to combine with support from InvestEU Advisory Hub or fi-compass<sup>5</sup> programme for advisory support, capacity building and supporting identification and development of investment projects. Combination with grants could be provided in two operations, where grants are directly provided by MA/NPBI.
- Once the Cohesion policy funds have potentially been used in the first instance to test or pilot these financing structures, these instruments may eventually be scaled up to attract other institutional and private investors,

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<sup>2</sup> For the purpose of this document, “financial instruments” means a form of support delivered via a structure through which financial products are provided to final recipients, as defined in Regulation (EU) 2021/1060, Article 2(16).

<sup>3</sup> For a recent analysis of the impact of inflexible housing supply on affordability in Euro Area Member States, see “Housing Market Developments in the Euro Area: Focus on Housing Affordability.” European Economy Discussion Paper 171 | September 2022.

<sup>4</sup> SPVs are separate legal entities created by a sponsor or a parent company to carry out a specific objective. SPVs have their own assets and liabilities and may enable to earmark funding from various sources for specific purposes and reduce final risk for sponsors.

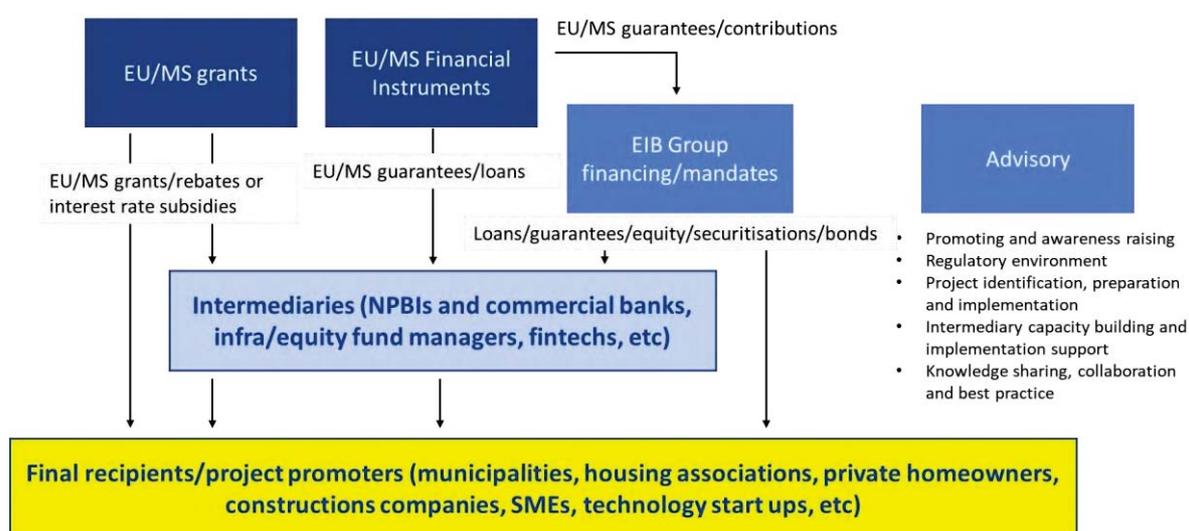
<sup>5</sup> [fi-compass | Financial instruments under EU shared management](#)

as well as banks and specialised financial institutions that finance this sector. This may be done using capital market instruments – including through securitisations and/or the issuance of green, sustainability-linked or social bonds.

Rules on eligibility will be needed for the operation of the model which should be common regardless of the form of financing (grants, loans etc.). The model should focus on interventions which enable the increase in supply of affordable housing. Eligibility should be confined to those final recipients who are genuinely subject to market failure. Market housing needs should not be supported. A more detailed eligibility section is below in this document.

To ensure the resilience against natural disasters, construction permits should be issued taking into account flood hazard and other natural disasters and risk maps, as prepared for national or regional disaster risk management plan(s), referred to in enabling condition “Effective disaster risk management framework”<sup>6</sup>.

**Given the heterogeneity of the market across the EU, in terms of how affordable housing is delivered, regulated, and funded, a number of financing combination options are proposed and can be further tailored as needed to the specific situation in the Member States, as follows:**



**To support Managing Authorities in developing the necessary framework for affordable investments, as well as the financing solutions, a range of advisory support may also be made available. This may include advice to establish an adequate regulatory framework needed for the deployment of the financing, support to investment project preparation, feasibility studies and design of investment strategies and instruments (including financial instruments).**

This paper complements the model FIs published in 2022 as part of REPowerEU<sup>7</sup> and the New European Bauhaus initiatives<sup>8</sup>. These models provided guidance on how to use Cohesion policy funds and national co-

<sup>6</sup>Enabling condition on disaster management : “A national or regional disaster risk management plan, established on the basis of risk assessments, taking due account of the likely impacts of climate change and the existing climate adaptation strategies, is in place and includes: 1. Description of key risks, assessed in accordance with Article 6(1) of Decision No 1313/2013/EU of the European Parliament and of the Council, reflecting the current and evolving risk profile with an indicative 25 to 35 years timespan. The assessment shall build, for climate-related risks, on climate change projections and scenarios. 2. Description of the disaster prevention, preparedness and response measures to address the key risks identified. The measures shall be prioritised in proportion to the risks and their economic impact, capacity gaps, effectiveness and efficiency, taking into account possible alternatives. 3. Information on financing resources and mechanisms available for covering the operation and maintenance costs related to prevention, preparedness and response”.

<sup>7</sup> [Model for a financial instrument with a grant component to support energy efficiency](#)

<sup>8</sup> [New European Bauhaus territorial development model \(NEB TDM\) financial instrument](#)

financing to establish FIs, in combination with grants and other financing, to support: (i) the renovation of buildings, owned by private individuals, housing associations, developers and/or municipalities, as well as (ii) urban development projects that may comprise the construction and/or renovation of affordable housing units as part of a wider set of investment interventions to regenerate and sustainably develop inner city areas, where the challenges of affordable housing supply are also usually more acute.

## Objectives of the model instruments

The aim of the model instrument options is to support investments in social and affordable housing by mobilising additional private resources. For this purpose, the instruments could:

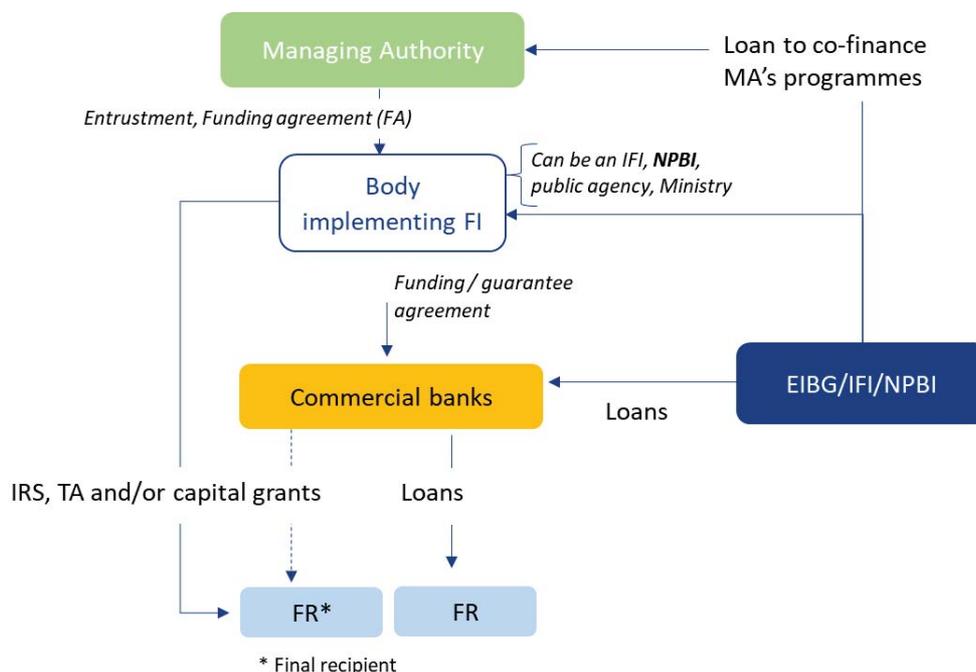
- **use Cohesion policy funds to:**
  - **deploy grant(s) in combination with financial products** - loan, guarantees, quasi equity and equity products- offered by the FI, for example, within a single investment strategy, to support the construction of affordable housing.
  - to mobilise/incentivise additional public and private investment to finance affordable investments by all types of project promoters.
  - Thanks to the funding model, incentivise reforms to improve and strengthen the regulatory framework for housing.
- **mobilise EIBG, IFIs and NPBI's co-financing** in or alongside the model instruments to enhance the volume of long-term and affordable funding and address the significant market gap in this area.

Given the diversity of market failure typologies, and **critical undersupply of affordable quality housing for lower- and middle-income citizens**, there is a general need for **non-repayable support** to cover (part of) construction and land acquisition costs. Grant components also help to keep house prices and rents at affordable levels by, for instance, covering part of the investment and/or borrowing costs of such projects. Therefore, grants remain, for most housing providers/owners, an indispensable part of the funding mix, to ensure these projects remain viable and affordable. Such grants may take the form of interest rate subsidies, capital grants, capital rebates or technical support subsidies (as outlined further below).

## Model instrument options

Five generic financing schemes are described below, comprising 1) a combined FI in one operation based on Art. 58(5) CPR; 2) and 3) two types of FIs combined with a grant in two separate operations based on Art. 58(4) CPR; 4) a combination of EIBG (or other sources of) funding and grants at final recipient level, into the same affordable housing projects; and 5) equity and quasi-equity financial instruments. The scope of the instruments shall be in accordance with the MA's programme priority under which it is implemented and, where applicable, in accordance with an ex-ante assessment, which covers the proposed investment strategy for an FI, as required under Article 58(3) CPR. In the case of a combination in one operation (option 1), this should also include the nature and indicative amount of grant support in accordance with Article 58(5) CPR.

## 1. Combined FI in one operation (guarantee or loan FI)



MA may decide to implement either a combined guarantee or loan FI as follows:

- Guarantee FI:** the MA may entrust a specific fund manager to provide and manage guarantees to banks providing underlying loans to affordable housing investment projects. A guarantee is more adapted to situations where financial institutions primarily require credit risk protection to support housing investment projects, rather than funding. Under this option, the guarantee fund manager will select financial institutions that will provide underlying loans, from their own resources, in line with the MA's investment strategy. The banks benefiting from the guarantee may also seek EIB, other IFI or NPBI funding where appropriate. The underlying loans will be provided to (or for the benefit of) final recipients in combination with grants. These grants may be managed by the guarantee fund manager (or the HF manager if there is one) as the combination is in one operation. Capped or uncapped types of guarantees will be implemented in combination with grants, depending on the needs.
- Loan FI:** The MA or a HF manager may be entrusted to select financial intermediaries to provide loans. In the absence of a HF, the MA may also directly select financial intermediaries to implement the loan FI. A combined loan FI will be more adapted to situations where financial institutions primarily require funding/liquidity to support housing investment projects. Financial institutions may in this case also access EIB funding (or other sources) to complement programme resources to cover their liquidity needs. The FI will provide affordable housing investment projects with loan products with a long tenor, affordable interest rate as well as a reduced collateral/security requirement. Grants may be directly managed by these financial intermediaries or the HF (where there is one). Senior or subordinated loans (e.g. risk sharing, direct or indirect loans) may be implemented depending on the identified needs.

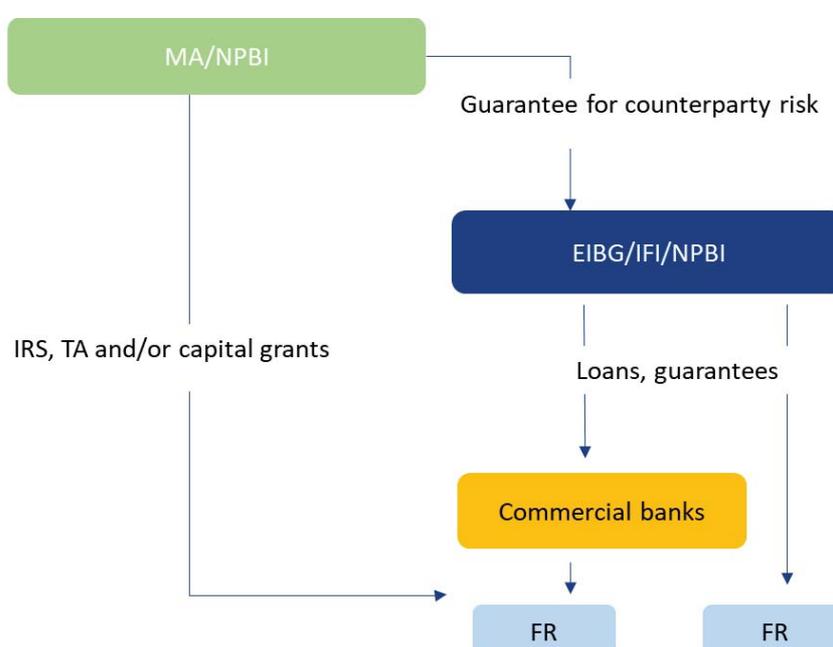
Under these two options, grants and financial instruments are combined in one operation and managed under FI rules based on Art. 58(5) CPR<sup>9</sup>. The latter requires the grants to be directly linked and necessary to the financial instrument. The necessity and the objective of the grant support shall be analysed and defined in the ex-ante assessment or other document. They may be related to the need to provide incentives to maximise policy impact,

<sup>9</sup> For more detail on combination of FI and grants in one operation, see: [Combination of financial instruments and grants under shared management funds in the 2021-2027 programming period](#)

support viability and mitigate risks or the enhancement of the consistency and efficiency of support schemes for final recipients. The total grant support shall not exceed the value of the investments supported by the financial product. This rule shall be verified at the level of the FI and not in relation to each individual investment, which may benefit from different grant intensities.

**Under this option, the programme resources may be used for the grant component of the combined financial instrument while financial intermediaries (e.g. public or commercial banks) may use EIB funding (or other sources) for the financial product part of the combination. The MA would thus leverage external funding resources while supporting investment projects' affordability with grants. Funding from EIBG, IFI and/or NPBI may therefore be recognised in the programmes as a source of national co-financing for this purpose.**

## 2. Guarantee to EIB, other IFI or NPBI, combined with grants in two operations

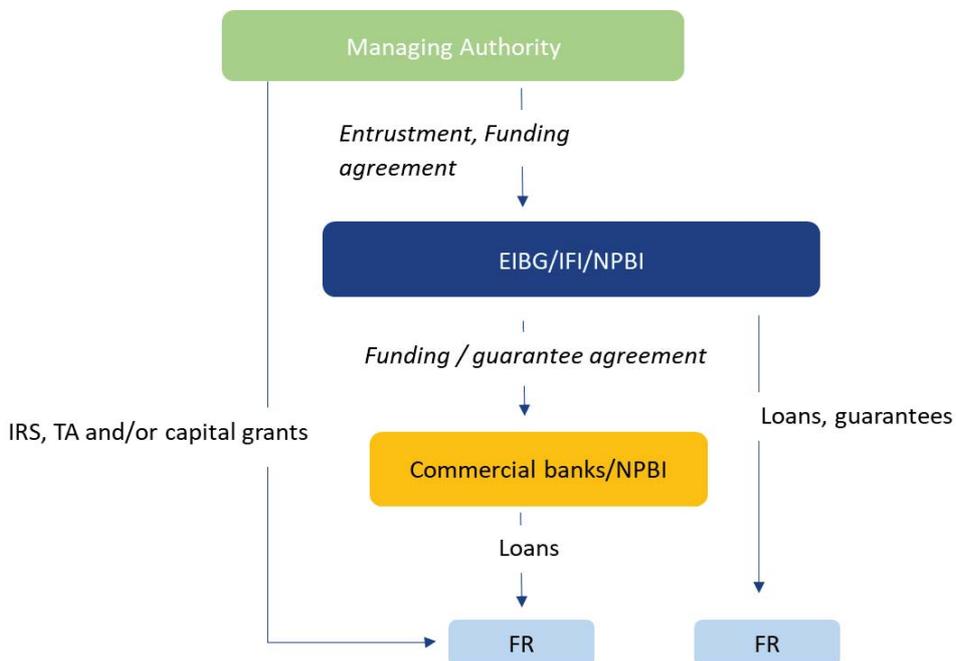


Under this option, the **MA would provide a guarantee to EIBG, IFIs and/or NPBI**s to enable it to lend to smaller/higher risk financial intermediaries on more affordable terms and conditions, which could then be passed on to final recipients. This would constitute a counterpart guarantee of the intermediary default on its financing. This counterpart guarantee also enables a wider range/diversity of the entities that could ultimately benefit from EIB (and other) funding support for affordable housing projects. Depending on the size of the investment projects and final recipients, **financing can be directly provided to final recipients or indirectly via commercial banks.**

Under this option, financial instruments and grants would each need to be the subject of a separate operation, at the level of the final recipients. Grants will be managed under a separate set of (grant) rules according to the CPR and ERDF Regulation and provided following separate grant calls issued by the MA.

**The MA provides grants to FRs (following grant rules), that are eligible in case they borrow from EIB, other IFI or NPBI directly or via financial intermediaries. This at least ensures an effective combination of the grants and loans at FR level for the same affordable housing investment projects.**

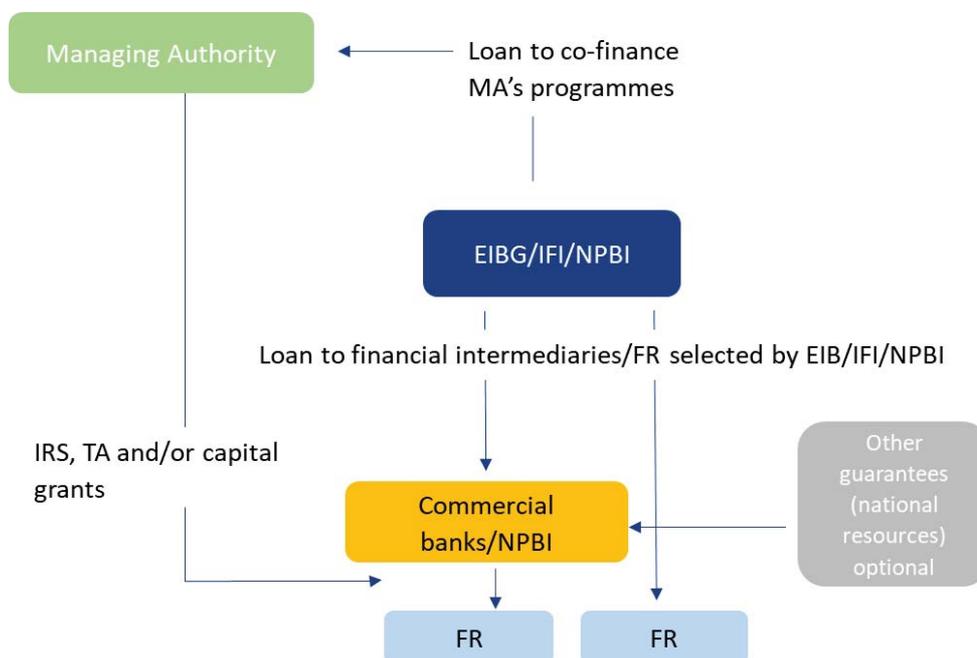
### 3. FI implemented by EIBG/IFI/NPBI, combined with grants in two operations



Under this option, a financial instrument is implemented by EIBG, other IFI or an NPBI and is combined with grants provided by a managing authority at the level of the final recipient, in two operations in the sense of the CPR. The FI may take the form of a loan or a guarantee and may provide financing directly to final recipient or indirectly, via financial intermediaries such as commercial banks, which are selected by the body implementing the FI.

**Final recipients need to apply separately to (i) the banks for FI support and (ii) to grant calls issued by MA. The two forms of support are combined at final recipient level and are managed under distinct set of rules, ie. CPR rules governing grants and CPR rules governing FI.**

#### 4. EIBG/IFI/NPBI funding combined with grants at final recipient level



There is no “financial instrument” - in the sense of the CPR - set up under this option. There is a form of a repayable support provided to final recipients. However, the MA provides grants to final recipients in close coordination with financing from EIB, other IFI or NPBI (directly or indirectly via intermediated loans originated by commercial banks or NPBI, depending on the size of the projects). The MA, which might borrow to co-finance its programme, will provide grants to final recipients alongside the financing from commercial banks (or other financial intermediaries) in a coordinated manner (i.e. ensuring the provision of both components to the same final recipient). Like in option 2, the grant and the repayable support operation are combined in two operations, at the final recipient level.

**Final recipients will be eligible for the MA grant programmes under the condition that they also borrow from banks funded by EIBG, IFIs and/or NPBI or that they would be directly financed by the latter. This condition would be enshrined in a specific clause of the grant calls.**

#### 5. Equity and quasi-equity Financial Instruments

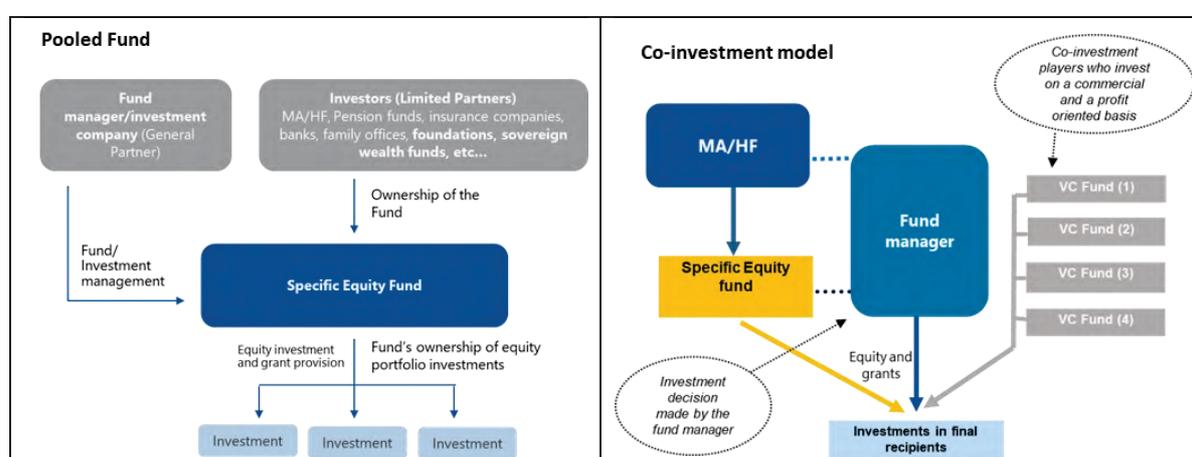
Equity and quasi-equity financing may be provided under the following delivery structures, in combination with grants.

##### Pooled Fund

A pooled fund is a type of investment fund where multiple investors combine their resources into a single fund managed by a professional fund manager or investment company, which is selected by the MA or the HF. Investors - including the MA directly or through a HF - typically contribute their resources buying shares or units in the specific equity fund. The fund manager or management team is responsible for making investment decisions on behalf of the fund, in line with the defined investment strategy. In this case, investors’ contributions in the Fund constitute co-financing in the sense of the CPR. Additional co-financing may come at project level from other investors external to the equity fund.

##### Co-investment model

This model foresees combination of different investors' resources on a project-by-project basis. Under a co-investment model, EU Funds resources are committed by a MA or HF into a specific equity fund managed by a fund manager, who may invest in companies alongside other investors through separately managed accounts. In this case, the investors' contribution (which would constitute national co-financing) is not provided at fund level but at company level by external investors as well as the fund manager's own resources to a lesser extent. In this case, usually a lead investor identifies an investment opportunity, commits funds to it and carries out the role of manager of the investment. Then other investors are invited to participate in the investment opportunity. Affordable housing investments may generate a relatively low return on equity as compared to other investments, due to the moderate level of rents they charge to their tenants. This yield may not be sufficiently attractive to private investors as compared to other equity of market financing instrument. Therefore, the FI may be structured so that private investors may benefit from an asymmetric sharing of the risks of the returns generated.



## Financial Products

Under the options described above, various financial products may be provided to final recipients. They may take different forms including senior loans, subordinated loans, capped, uncapped and counter guarantees. Equity and quasi-equity products may also be implemented. A single FI may deliver various types of financial product to support a range of different affordable housing projects and final recipients. Alternatively, one or more FIs may be developed to deliver a single product with a view to meeting a specific market failure in a region.

### Loans

Loans should not finance pure financial activities or real estate development when undertaken as a financial investment activity and should not finance the provision of consumer finance (e.g. subsidies for individual mortgages or rental costs).

Loans should be used for the following purposes:

- investments in tangible and intangible assets,
- working capital related to the eligible activities.

Loans included in the portfolio should:

- be newly originated, with the exclusion of the refinancing of existing loans.
- have a repayment schedule, including regular amortising and/or bullet payments.

### Senior long-term loans

Given the long-term economic life of the affordable housing assets to be constructed, there is a traditional need for (very) long term loans at affordable interest rates. Depending on the nature of the borrower and of the housing assets, these loans may have a tenor up to 30 years, and longer in exceptional circumstances.

In several MS, affordable housing providers pledge their housing assets (including land) to secure borrowing from lenders (mortgage approach). Under the FI component, long-term loans may be provided without any pledge on housing assets (i.e. unsecured) in order not to increase the encumbrance rate of borrowers' balance sheet and reduce admin burden (registering mortgages in some markets can be burdensome). The pledge on assets may also be replaced by a guarantee mechanism, using for example Cohesion policy funds, and which would provide the necessary level of security to offer longer tenors on more affordable lending/pricing terms.

### **Subordinated loans**

Affordable housing providers, developers and construction companies need sufficient equity to raise the required long-term funding or carry out their investment projects. Subordinated loans may bridge this gap to some extent and help the borrower access senior lending from other, commercial financiers, as well as reinforce their balance sheet through this form of quasi-equity, without diluting share capital and ownership.

These loans may either be:

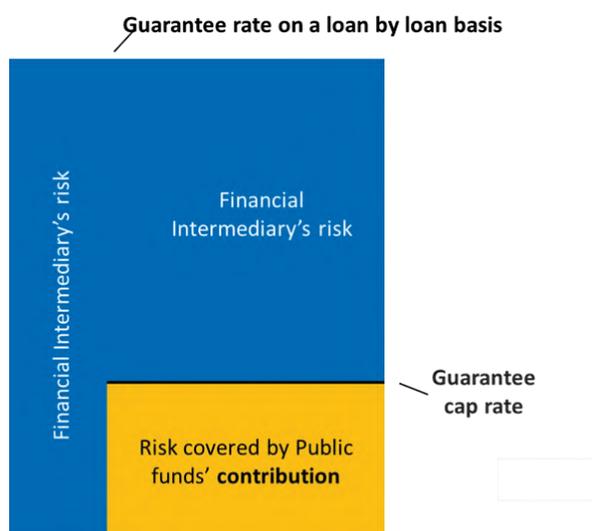
- contractually subordinated, e.g. the financial product ranks junior to other liabilities because of a longer tenor/grace period and may have a sculpted or bullet repayment profile that repays after senior lenders.
- or structurally subordinated by being provided to an operating company lower down in the organisational structure or to a holding company that does not directly generate cash-flows or own the underlying project assets, for example.

### **Guarantees**

Guarantees may be provided to financial intermediaries that are providing loans to affordable housing providers, developers, construction companies or individual homeowners. It would enable financial intermediaries to reduce their collateral requirements and improve their lending conditions, notably in terms of interest rate and tenor (as mentioned above).

The guarantee may be either capped or uncapped depending on the amount of expected losses that they are designed to cover.

### **Capped guarantee**



The guarantee cap rate typically comprises the **portfolio's Expected Loss**

Under this guarantee model the multiplier is calculated as follows:

Multiplier =  $1/\text{Guarantee Rate} * 1/\text{Guarantee cap rate}$

A capped portfolio guarantee is an instrument where the guarantor covers part of the losses of each loan provided by a financial intermediary at an agreed guarantee rate until a pre-agreed threshold at the portfolio level is reached. The lender keeps a share of the risks on each loan to align interests. Once the capped guarantee is fully used, the lender becomes fully exposed to additional losses of new loans going into default.

The guarantee shall cover the unpaid principal and standard interest minus recovered amounts in respect of each defaulted underlying financial transaction originated by the financial intermediary. In the affordable housing sector, these financial transactions may take the form of senior loans, subordinated loans or leasing.

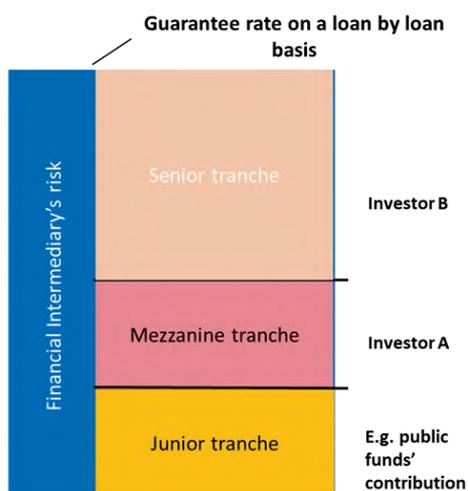
Individual loan guarantee rates will be defined according to the type of borrower and the sub-sector targeted. The guarantee (total covered loss) cap is usually estimated based on the average probability of default or on the loan default rate expected to occur and should be decided with financial intermediaries based on their track record.

The benefits of a capped portfolio guarantee for the financial intermediary are the following:

1. It usually limits the need of covering for the expected loss on the part of the lender (e.g. reduction of the amount of provisions recognised as expenses in the lender's profit and loss statement).
2. It provides a more limited impact in terms of capital relief (except for banks applying the AIRB approach).

This capped guarantee can be provided as a counter-guarantee to an intermediary guarantee provider.

### Uncapped guarantee



*The uncapped guarantee may covers the **portfolio's Expected and (part of the) Unexpected Loss***

*Under this guarantee model the multiplier is calculated as follows:*

$$\text{Multiplier} = 1/\text{Guarantee Rate} * 1/\text{Guarantee cap rate}$$

An uncapped guarantee is a scheme where, contrary to the previous example, no limitation on the losses to be covered at portfolio level is foreseen. Each individual loan's losses are covered up to the guarantee rate without any cap on pari-passu terms. The funds set aside for the guarantee need to be large enough to possibly cover the losses incurred on each and every loan of the portfolio up to the guarantee rate.

As shown above, the uncapped guarantee is usually tranced, enabling various sources of funds and investors to cover distinct risk levels. Like in the capped model, public funds usually cover the junior tranche, which is exposed to the first losses (together with the financial intermediary which keeps a lower portion of the first losses to align interest). The junior tranche covers a sufficient amount of losses to attract additional investors, who are ready to guarantee additional possible losses with a mezzanine and senior guarantee.

The uncapped and untranced guarantee could be used to establish a single and deep capital market for affordable housing loans and to create a new European Safe Asset.

Like the capped model, the uncapped guarantee will also cover losses taking the form of unpaid principal and standard interest minus recovered amounts in respect of each defaulted underlying financial transaction originated by the financial intermediary. The possible underlying financial products, which may be guaranteed, are similar to those of the capped portfolio guarantee.

The uncapped guarantee may be needed for more capital risky portfolios for which the loss severity is more difficult to foresee or less liquid portfolios. This may result from a lack of a track record, a higher volatility of losses or a higher risk concentration within the loan portfolio, for instance linked to a smaller number of higher value loans or from more fragmented capital markets.

In terms of benefits, the coverage of (part) of the unexpected loss of the financial transactions may provide lower capital risks and/or higher liquidity to financial intermediaries and capital markets. Given its wider reach (coverage of the unexpected loss) and the larger volume of resources needed to provide the risk protection, uncapped guarantees typically are charged a higher guarantee premium than capped guarantees. This guarantee premium could be compensated by lower capital costs and a lower liquidity premium. This will be reflected in the lending costs of the financial intermediaries and capital markets to final recipients. Uncapped loans may therefore be used to support sectors, activities or geographical areas where financial intermediaries are not willing or where capital markets have currently too little liquidity to provide financing or where lending conditions need to be significantly improved to achieve policy objectives.

## **Equity and quasi-equity**

### **Equity**

Equity financing is provided by a fund manager selected by the MA or the HF, which identifies final recipients and invests the resources, together or alongside funds committed by other investors. In return for the investment, the equity fund receives a share of the ownership of the company or the SPV created to construct and/or manage new affordable housing units. For the investor, holding shares generally implies voting right regarding the strategy and operations of the investee as well as a potentially receiving a share of the generated profits. Equity financing provides the investee with stable and patient capital facilitating its long-term borrowing. It may also cover other costs such as land or property acquisition. Convertible loans may also be used and be converted into shares of the supported entity at a later financing stage (for instance, when a specific milestone is achieved).

### **Quasi-equity**

Depending on the legal structure of the investee, quasi-equity instruments may take different forms. For instance, in France, they may take the form of 'titre participatifs'. Other forms of quasi-equity could be perpetual bonds subscribed by investors. The latter are used to strengthen the capital basis of entities without a proper (or without affecting the existing) shareholding structure but with other legal forms (associations, cooperatives). Such type of instruments may be applicable to non-profit structures depending on the applicable legal frameworks in Member States.

## **Grants to be combined with financial products/instruments**

The combination of Cohesion grants in the instruments should be identified in the Member State's programme as a possible form of finance for the specific objectives concerned. If not, the programme would first need to be amended. The following types of grants may be combined with financial instruments depending on the market needs and national legal framework. The grant may also be provided to support specific types of investment projects and/or FRs within the overall instrument structure. The grant intensity may therefore be higher to support lower income final recipients or investment projects where the costs of developing new affordable housing are highest or in socially and economically vulnerable areas or for projects in conservation areas or fulfilling specific construction or performance standards. It may also be modulated to pursue political objectives. In particular, Member States can be encouraged to provide higher grant intensities to housing schemes targeting younger households, facing higher difficulties to access housing, with a view to fostering their capacity to achieve their family plans, or targeting territories facing attractiveness challenges.

### **Interest Rate subsidy**

An interest rate subsidy (IRS) may be provided to reduce the cost of borrowing for the final recipient. This subsidy should apply to the private and public co-financing part of the loan (not to the part of the loan funded by the Cohesion policy funds, if any), providing a discount to ensure the interests paid do not exceed a specified ceiling. This subsidy may have a critical impact by making very much needed long term loans affordable and accessible to affordable housing providers.

The IRS may be accounted as part of the interest payable by the FR. The interest rate subsidy may be paid directly to the FR or on behalf of the FR to the financial intermediaries, or upfront in the form of a discounted lump sum.

### **Capital grant**

A capital grant can be defined as a non-repayable provision of financing that aims to finance part of an investment (on specific cost or on a pro-rata basis) or at covering a viability gap in an affordable housing project.

The capital grant may therefore help solve the 'affordability-return dilemma' in affordable housing projects by covering part of the investment costs in order to keep the final rent levels paid by tenants, for example, at an

affordable level commensurate with their income. This would help increase the return on investments that may be too low to attract private investors.

When combined with a FI in one operation, the capital grant will be provided following the FI rules and may not necessarily be provided to finance only a specific expenditure item/component. It may also be paid upfront under FI rules (not as a reimbursement of incurred costs like traditional grants), to or on behalf of the FR, to cover part of the investment.

#### **Capital rebate**

A grant in the form of a capital rebate can be provided in combination with the FI component, based on the fulfilment of conditions/triggers defined in the funding agreements. The capital rebate may take the form of an early repayment or of a write-off of the loan in the financial intermediary's accounts.

The triggers may be linked to the fulfilment of the objectives pursued by the FI. A capital rebate may for instance be provided after the construction period once the necessary verifications have been carried out or when pre agreed performance standards have been reached.

#### **Endowment**

A grant in the form of an endowment for housing associations can be provided to establish housing associations in MS that have not a fully developed housing association system. These housing associations finance part of an investment (on specific cost or on a pro-rata basis) or cover a viability gap in an affordable housing project.

The endowment may therefore help developing housing association system in MS. Through these housing associations the grant helps solve the 'affordability-return dilemma' in affordable housing projects by covering part of the investment costs in order to keep the final rent levels paid by tenants, for example, at an affordable level commensurate with their income. This would help increase the return on investments that may be too low to attract private investors.

#### **Technical support subsidy or technical assistance grant**

A technical support subsidy may be provided as a cash grant to (or for the benefit of) the FR. This subsidy would cover the investment preparation and implementation costs, such as feasibility, economic or market studies as well as technical analysis and advice.

This subsidy may for instance be used to cover costs during the following steps of the investment project: site investigation, planning and design of the housing project, procurement advice and preparation, monitoring and commissioning of the construction works.

## **Eligibilities and scope – ERDF applicable scope**

Housing situations in each Member State are different and the term "affordable housing" can be interpreted in various ways. This model does not attempt to serve one definition or give preference to a single interpretation. The purpose of this model is to be inclusive of existing frameworks and targets all groups affected by market failures associated with housing scarcity. Member States could use their own criteria based on specific market conditions, to capture the funding gap in affordable housing. It is also inclusive of definitions for "Affordable housing", which may be further defined, pursuant to the forthcoming affordable housing plan, regarding notably the possible changes of EU State aid rules, when the model will be implemented by NPBs, IFIs and other financial institutions.

#### **ERDF's applicable scope**

For NPBI and other financial institutions potentially implementing the proposed model for financial instrument, requirements will be governed by the ERDF Regulation, Article 5-7. All supported measures should be in line with the cohesion policy legislative and policy considerations.

In this regard, the scope of support shall consist of capital expenditure for:

- construction of new affordable housing units

- renovation of existing affordable housing units
- conversion of buildings with other uses
- Equity sharing, partial ownership (e.g. referring to ownership by private individuals) approaches (where justified by market failures and public policy)

Potential financial intermediaries are, in line with CPR:

- National and regional promotional banks
- Dedicated financial organisations backed by governments (debt funds, SPVs)
- Commercial banks

For information, the final recipients who are currently eligible under the relevant programmes and funding agreement in the housing sector may be supported by the model. This includes:

- Housing associations
- Cities and municipal companies
- Approved/regulated affordable housing providers
- Construction and property companies, developers
- Individuals (final recipients, facing affordability issues)

## State aid

The presence of State aid shall be verified at the level of the body implementing the FI as well as at the level of the final recipient.

1. At the level of the body implementing FI/fund manager and the HF, the presence of aid can be excluded if all the following conditions are met:
  - The co-investing body implementing SF and the MA or HF carry out the investment on a *pari-passu* basis, i.e. under the same terms and conditions, at the same time (via the same transaction), they bear at any time the losses and benefits in proportion to their contributions (pro-rata), hold the same level of subordination in relation to the same risk class and there is an economically significant participation of the independent and private co-investors, e.g. body implementing FI in the risk sharing loan. However, this cannot occur when a grant is provided in combination with the loan, e.g. for capital rebate and capital grant which would vitiate the *pari-passu* principle.
  - the remuneration (i.e. management costs and/or fees) of the body implementing the SF and the HF as well as the loan pricing structure of the body implementing SF reflects the current market remuneration in comparable situations, which is the case when the latter have been selected through an open, transparent, non-discriminatory, and objective selection procedure; or

the financial advantage of the programme public contribution is quantified and then fully passed on to the final recipients in the form of an interest rate reduction and/or a decrease in collateral requirements compared to the market rate. The market rate can be either the appropriate market benchmarks for the specific risk and the sector, or the market proxies set out in the Reference Rate communication.

2. At the level of the final recipient, for the combined financial instrument (loan/guarantee and grant components), an assessment should be made whether or not the support constitutes State aid. In some situations, the support may not constitute State aid when it is fully passed on to natural persons benefiting from housing without exercising an economic activity therein.  
In case State aid is present, it should be assessed whether the aid can be considered compatible or exempted from notification under an exemption Regulation. In case the support constitutes State aid and does not fall

under an exemption Regulation, it is necessary to notify it to the Commission, which may approve such aid. There is the possibility to notify it as part of an aid scheme.

The Commission is currently in the process of considering a possible adaptation of the State aid rules to better enable housing support measures in line with the Political Guidelines for 2024-2029. The Commission will consult the public on the possible design of the specific rules for affordable housing, in addition to social housing.

## **Eligibilities and scope – EIBG’s contemplated eligibility scope**

### **EIBG’s contemplated eligibility scope and conditions**

The EIB may have own eligibility rules which will apply to operations where the EIB participates in the implementation of the financial product through direct or indirect lending to final recipients or through loans to MA programmes.

According to the EIB, affordable housing may encompass the following types of residential accommodation:

- Social and affordable housing for persons, which is variously referred to as “social housing”, “affordable housing”, “municipal housing”, and “public housing” in different member states.
- Student accommodation (off campus)
- Key worker or seasonal worker housing
- Care homes and elderly housing<sup>10</sup>.

The EIBG is planning to define its own set of eligibility criteria for governing its support to affordable housing, based on the following conditions:

- A minimum regulatory framework should be in place to confirm the above conditions – this may be a national policy or regulatory framework; a Strategic Local Plan for Affordable and Sustainable Housing or equivalent Sustainable Urban Development (SUD) Strategy; or a suitable governance framework (eg. via a service contract, housing company governance or through the investment criteria of the FI itself).
- The housing may be for rental or for ownership – in case of housing provided for partial or full ownership, specific conditions will be introduced, depending on the financial instrument and local market context, to avoid the risks of funds being used for property speculation.
- A transparent fair and inclusive allocation mechanism shall be in place for the allocation of affordable housing units to households. This would typically take account of income levels, disability, migration status, key workers etc. depending on locally established needs and priorities.
- Housing should be suitably located to avoid urban sprawl and provide proximity to local services, as part of a suitable approved comprehensive urban plan.
- The housing should meet EU regulatory requirements for energy efficiency as transposed into national laws.

EIB Advisory support may be provided at national or local level to support the development of suitable public policy frameworks, or their equivalent, needed to allow for the deployment of the financial instrument, and potentially be a precursor for wider set of reforms related to the housing policies in the country.

Regarding **final recipients**, EIB is considering a set of criteria, which are not mutually exclusive: belonging to a specific eligible target group, being disadvantaged persons, due to income or social constraints, are unable to secure housing at market condition, – or housing providers which provide housing to this group of persons..

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<sup>10</sup> Care homes and elderly housing can be supported with cohesion policy funding under the conditions compatible with the United Nations Convention on the Rights of the People with Disabilities.

The specific characteristics of the final recipients shall be defined at the level of the specific financial instrument and take account of local market context. (For example, income thresholds may take into account the Eurostat definition of housing cost over-burden (housing costs should not exceed 40% of the net disposable income of the occupants), or thresholds established by reference to the income levels of key workers and may vary both by country and within the country by city or region).

In the absence of a national or local regulatory framework, the target groups need to be identified in the investment proposal, with evidence that the target groups are based on solvency (i.e. income level) or on social constraints (that can be, depending on the context, single parent family, elderly, disability, homeless, etc.), depending on the specific socio-economic context.

## **Invest EU Member State compartment**

Member States have the option of providing financial products through a Member State compartment of the InvestEU Programme where the EIBG, NPBI and IFIs would receive a budgetary guarantee from InvestEU to support their investments. Member States have the option to provide all of the forms of financing (*loans, guarantees, equity*) mentioned in the section “Financial products”, through InvestEU. In doing so, implementation would benefit from a single system of rules and practices as well as established contracts already in place. The presence of state aid can be excluded if an IFI implements such support under InvestEU via already existing InvestEU financial products<sup>11</sup>.

Furthermore, depending on the financial product deployed (see below) and the availability of additional guarantees from the central government, such a construction could leverage the available funds.

Member States may benefit from the advisory support available under the InvestEU Advisory Hub, that may specifically support design of national investment programmes.

For the purposes of investments supported by the InvestEU Fund, affordable social housing is understood as support aimed at disadvantaged persons or socially less advantaged groups<sup>12</sup>, who, due to income or social constraints live in severe housing deprivation or are unable to obtain housing at market conditions. When targeting specifically people falling under the ETHOS definition of homelessness and housing exclusion<sup>13</sup>, social housing provision is, as much as possible, to follow a housing led approach. The infrastructure and services are to respect the applicable quality standards and UN conventions and shall not lead to segregation or isolation of specific groups.

Affordable social housing projects may consist in operations such as:

- (a) provision of new, non-segregated and accessible rental social housing stock through one or several of these actions:
  - construction of new buildings;
  - refurbishment or transformation of existing buildings;
  - sourcing of individual housing units from the private housing market (through purchase or mediation).
- (b) set-up of a social rental agency;
- (c) provision of housing-led solutions, combining the provision of rental housing units with enabling support services of proximity (i.e. delivered on-site or made easily accessible);
- (d) adapting existing social housing stock to fit the needs of persons with disabilities, including owner-occupied housing.

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<sup>11</sup> Where necessary, any modifications of such product (e.g. in terms of eligibility) must be rooted in European requirements, i.e. outside of the Member State’s/Managing Authority’s control.

<sup>12</sup> As defined at the national, regional or local level, as applicable, and/or by economic and social contexts

<sup>13</sup> [ETHOS Typology on Homelessness and Housing Exclusion](#)

- (e) targeted support for marginalised communities that experience severe deprivation in their current housing conditions, including owner-occupied housing.