Regional Sovereign Wealth Funds

Case Studies

CLDP

COMMERCIAL LAW DEVELOPMENT PROGRAM

September 2022

Contents

About CLDP 6

Background 7

Introduction into Sovereign Wealth Funds 7

Case study selection 9

Key Lessons from Case Studies 10

- Fund Objectives 10
  - Primary fund objective: Realizing investments in local economies 10
  - Secondary fund objectives 11
- Investment Mandate 11
- Regulatory Basis 12
- Management & Governance Structure 13
  - Involvement of private sector investors or alternative sources of capital 14
  - Management capacity 14
- Capitalization & Ownership 15

Key Insights from Stakeholder Consultations 16

- RSWFs need to unlock allocation for existing financial resources 16
- RSWFs also need to attract alternative sources of capital 17
- RSWFs should contribute to accelerating procurement process 17
- RSWFs need to find balance between retaining government control and independent expert management 18
- Regional governments have varying levels of readiness for implementing RSWFs 18

Recommendations on next steps 19

Annexure A – Law concerning financial relations between central and local governments 20

Annexure B – Case Studies 23

About CLDP

The Commercial Law Development Program (CLDP) is a division of the U.S. Department of Commerce that helps achieve U.S. foreign policy goals in developing and post-conflict countries through commercial legal reforms. CLDP's unique, government-to-government technical assistance draws upon highly experienced regulators, judges, policymakers, business leaders and attorneys from both the public and private sectors to deliver results that make meaningful and lasting changes to the legal and business environments of our host countries.

About Rebel Group

The regional sovereign wealth fund case studies and this report was developed with the support of Rebel Group. Rebel is an independent, employee-owned advisory group operating internationally from its home base in the Benelux and intercontinental offices in Washington DC, San Francisco, Dusseldorf, Nairobi, and Johannesburg. Rebel specializes in economics, feasibility, financing, and transaction advisory for projects in all infrastructure sectors, including energy and renewables, transportation, water and waste management, ports, and airports, as well as social infrastructure and housing. Besides its advisory practice, Rebel is active as equity investor and in public investment fund structuring or sovereign wealth funds, specifically in infrastructure financing.

Background

Founded by the Indonesian Government in 2021, the Indonesia Investment Authority (INA), a sovereign wealth fund (SWF), is intended to strengthen the country's economy by diversifying into new asset classes to finance the country's economic development. Following the INA's example, several subnational governments are interested in creating their own Regional Sovereign Wealth Funds (RSWFs). Subnational governments intend to invest their budget surpluses in RSWFs to fund subnational infrastructure projects. Indonesia's Coordinating Ministry of Economic Affairs (KEMENKO EKON) has requested CDLP's assistance to develop case studies to guide Indonesian subnational governments as they determine the best RSWF mechanism for stimulating infrastructure development.

Introduction into Sovereign Wealth Funds

A sovereign wealth fund (SWF) is a government-owned investment vehicle that is established with the purpose of making investments in various financial assets. SWFs are typically capitalized through a government's budgetary surplus. In case a government has excess money available, SWFs are used to allocate the money to investments rather than keeping it on the accounts of the central bank or creating excess expenditure on the budget. The purpose of establishing a SWF differ from government to government and drives much of the design elements of a SWF. The most well-known and largest SWFs are those from the Middle East and Norway. Middle Eastern countries generate a large portion of their revenue and budget surplus from exporting oil and gas and have established SWFs for purposes of economic stability and preserving future wealth.

Sovereign wealth funds fall into four broad categories that differ based on their purpose of establishment and their respective investment strategies with various levels of risk acceptance and liquidity of investment.

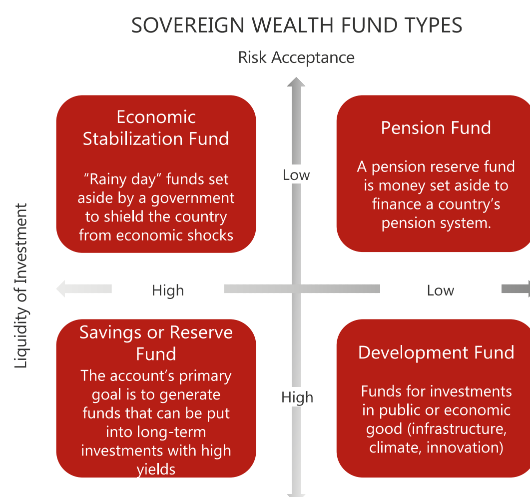


Figure 1: Types of Sovereign Wealth Funds

1. *Economic Stabilization Fund* – established to stabilize the economy in cases of economic shocks. Capital from the fund may be utilized to supplement shortages in the government budget or to fund economic incentive programs.
2. *Pension Fund* – established for the purposes of funding expected future pensions benefits of the population, initially capitalized with budget allocation (i.e., not with budget surpluses) and

supplemented with pension contributions, from which it is expected to generate a stable long-term and cash generating investment return.

3. *Savings, Reserve or Endowment Fund* – established with the purpose of investing budget surpluses which are accumulated in the fund to generate returns. The returns can be used for government expenditures, the principal amount is to remain in the fund.
4. *Development Fund* – established with the purpose of funding investments in public infrastructure or services or for economic good. Investments are usually focused on fixing "market failures", (i.e., investments which financial markets fail to supply). Investments can be of long-term nature, innovative, high capital costs, or in some cases, only partially financially viable.

Subnational governments in Indonesia intend to invest their budget surpluses to fund subnational infrastructure projects, which aligns most closely with the Development Fund typology described above. The case studies will thus focus on development funds that match the objectives of Indonesia's subnational governments in terms of purpose and nature.

Sovereign development funds or regional development funds can be further categorized based on their objectives and level of strategic or commercial investments.

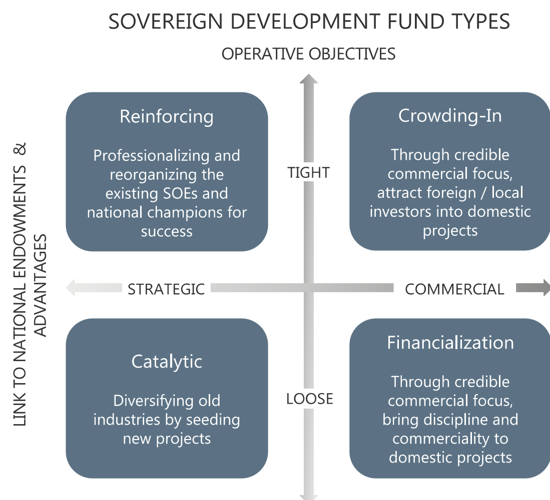


Figure 2: Types of Sovereign Development Funds

This categorization results in development funds with four distinct purposes:

1. *Reinforcing* – these development funds are tasked with the responsibility to reorganize, professionalize and innovate state holdings so as to drive commercialization and higher returns.
2. *Crowding-in* – these development funds are tasked with making investment that attract private sector investors to participate in emerging domestic industries that offer high financial and developmental returns.
3. *Catalytic* – these development funds invest in new industries to diversify the economy away from existing industries that are no longer profitable or sustainable over the long term. Investments can also be made in nascent industries that are expected to gain significant traction in the long run.

[1] Source: Clark and Monk, 2015

4. *Financialization* – these development funds can deepen the local financial industry by bringing commercial focus, investment discipline and long-term patient capital, which will result in growth of capital markets, development of new financial intermediaries and new investors.

Case study selection

This report describes case studies of a variety of regional sovereign wealth funds or regional development funds. The purpose of the case studies is to provide KEMENKO and subnational governments with insights on how RSWFs can be structured and can be catalytic for investment in regional development. As agreed with KEMENKO, the following criteria were used for the selection of case studies:

1. Funds that solve bottlenecks in public / infrastructure project investment
2. Funds that have (at minimum, partial) public ownership
3. Funds that have (at minimum, partial) public governance
4. Funds that are established as part of (sub) national policy decisions
5. Fund from a country with a similar economic and/or legal context
6. Funds from developed and developing capital markets
7. Also included national & international level fund examples (i.e., national government supporting local government) as alternative mechanisms

The selection criteria resulted in the following, diverse set of case studies:

- *Odisha Urban Infrastructure Development Fund* – India – a regional development fund with focus on water and sanitation, making public investments only.
    - Product offering: Grants for viability gap funding and project preparation and long-term local currency finance
    - Capitalization: Capitalized through a (national) sovereign loan from KfW Germany with small contribution of local government
- *Ho Chi Minh City Urban Development Fund* – Vietnam – municipal development fund with focus on public infrastructure and services, making private investments only (including PPPs).
    - Product offering: long-term debt & equity
    - Capitalization: Local government budget, local revenue bonds and Official Development Assistance (ODA) through sovereign loans from the World Bank
- *Florida State Infrastructure Bank* – USA – regional or state infrastructure fund with focus on transport infrastructure making both public and private investments.
    - Product offering: loans and credit enhancement products, such as guarantees
    - Capitalization: Federal grants and contributions from state budget
- *Regional Development Agencies* – Netherlands – regional development fund with focus on strengthening the local economy through innovation making private sector investment only.
    - Product offering: equity, junior and senior debt
    - Capitalization: National and local government budgets
- *Philippines "Green Green Green" Fund* – local government support fund focusing on "green" urban infrastructure making public investments only.
    - Product offering: public grants
    - Capitalization: National government budget
- *Kenya Innovative Financing Facility for Water or KIFFWA* – project development facility, supporting local governments in developing bankable water projects.

- Product offering: Convertible grants and equity
- Capitalization: funding from the Government of the Netherlands through Netherlands Water Partnership.

Detailed case studies can be found in Annexure B.

Key Lessons from Case Studies

The following section will describe the main lessons that were drawn from the case studies. Lessons drawn from the case studies are organized according to the following fund characteristics and features:

- *Fund objectives* – Why was the fund established? What is its mission?
- *Investment mandate and strategy* – How does the fund realize its mission?
- *Legal basis* – On what basis was the fund created or established?
- *Governance structure & ownership* – Who owns the fund? How are decisions made? How are operations and oversight organized?
- *Capitalization* – What is the source of funding and what kind of capital does the fund use?

Fund Objectives

RSWFs are established to serve various purposes. Notably, RSWF objectives highly depend on the level of local economic development that already exists in the jurisdictions they serve.

The following common themes around RSWF objectives were drawn from the case studies:

Primary fund objective: Realizing investments in local economies

1. *Developing market RSWFs*
    - *Catalyze infrastructure development* - One common denominator among all developing market case studies is the increasing need for urban infrastructure due to high rates of urbanization. As such, in the context of developing markets, one of the main purposes of RSWFs is to develop local economies through investments in regional infrastructure and services.
    - *Close investment gap* - A widening infrastructure investment gap[2] between available resources and infrastructure needs creates the increasing need for alternative capital resources, which local governments seek to develop and leverage through the development of RSWFs.
    - *Crowd-in capital* - RSWFs in developing markets can be classified as the crowding-in type of development funds, as they focus on attracting private sources of capital for infrastructure development by structuring risk profiles of projects and by developing local financial markets.
    - *Provide long-term risk capital* - The effectiveness of crowding-in type of RSWFs is dependent on an initial source of financing that offers longer term tenors that match the horizon of its investments (i.e., commonly infrastructure projects), or risk acceptance which is not available in the market.
    - *Provide financial flexibility* - In addition to long-term tenors, RSWFs can provide additional flexibility through subordination, equity capital, grace periods, or tenor extensions. Greater risk acceptance is provided through concessional capital in terms of (partial) grants and sub-market pricing.

[2] Defined as an increasing gap between the need/demand and supply of investments in infrastructure.

2. *Developed market RSWFs*
    - *Solve market failures* - RSWFs in developed economies are created to solve market failures by making investments in industries or segments where there is underinvestment by the private sector.
    - *Strengthen economies* - As such, in the context of developed markets, the purpose of RSWFs is more focused on strengthening local economies through optimizing infrastructure or spurring innovation by supporting new industries.
    - *Provide catalytic funding* - RSWFs in developed markets can be classified as the catalytic type of development funds, as they seek to diversify away from old industries.
    - *Avoid crowding out market players* - Catalytic RSWFs need to ensure they do not crowd-out existing market players to remain effective and provide, on net, incremental value to the market.

Secondary fund objectives

Other than realizing investments in the local economy, RSWFs may also serve the following secondary objectives:

- *Develop local financial markets* - RSWFs contribute to the development of local financial markets by enhancing the capacity of the financial system in funding investment and diversifying risk. By increasing the number of market players, deep and liquid markets are created that result in more transparent and efficient pricing, attract investors and transfer risk to parties able to bear them. In case of RSWFs, this refers to the bearing of long-term risk of financing infrastructure projects that the existing market is unable to absorb.
- *Develop investment capacity* - the case studies showed that (local) governments of developing countries lack the capacity and experience to manage investments. With RSWFs, governments can build investment experience, either by establishing a specialized government agency or by learning through a private investment manager.
- *Solve bottlenecks in project development* - RSWFs are also established to solve for bottlenecks in project development by extending technical assistance and grants for project development of bankable projects.

Investment Mandate

The investment mandate of an RSWF is determined by its objectives. As such, differences between the investment mandate of RSWFs in developed and developing markets can likewise be observed.

	Developing markets	**Developed markets**
Investment focus	Support rapid urbanization through developing basic infrastructure	Strengthen local economies through strategic infrastructure investments or new innovations to diversify local economy
Beneficiaries	Private and public sector players	For infrastructure, both public and private players. For innovative investments, solely private sector beneficiaries
Sectors	Mostly focused on infrastructure to accommodate urbanization, such as transport, water & sanitation	Transport infrastructure or innovative sectors, such as plant-based proteins, electric vehicles, etc.
Products & pricing	**Loans** and equity with flexible but market-based pricing. In case of long-	**Loans & equity**, with flexible but market-based pricing, focused on

term public projects, can also provide **equity**. Otherwise, due to a lack of exit possibilities, equity is not commonly used. **Grants** are provided in the form of viability gap funding. **Technical assistance** is also provided for capacity development or early project development phases.

providing enabling investments for private investors.

Some commonalities in the way RSWFs are established in both developing and developed markets have also been observed:

- *Government policy-led* - RSWFs are established to realize investments defined by government policies, whether in infrastructure or strengthening local economies through innovation.
- *Illiquid investments in nascent markets* - RSWFs operate where private markets are underdeveloped. As such, they are often exposed to illiquid investments particularly when investing in infrastructure. The lack of liquidity demands a rigorous investment and risk management process.
- *Long term sustainability* - Most RSWFs aim to be revolving to create a permanent and relatively stable additional revenue/financing source for investments in the local economy. A revolving fund is achieved when the proceeds from the investment activities can cover the operational cost and any investment write-offs.
- *Flexible financing terms* - As a result of the capital base, RSWFs can offer more flexible financing terms (such as, grace periods, tenor extension). RSWFs, however are unable to assume (much) more risk than the market, as this would in theory result in a net loss of the fund. As a result, the fund would be depleting, assuming no replenishments.
- *Professional management & procedures* - A revolving fund requires the implementation of qualitative and market-based investment practices, strong investment acumen and risk management policies. These capacities are often lacking within public institutions but can either be developed or outsourced.

Regulatory Basis

RSWFs are typically set up under a government decree, regulation, law, which provides the RSWF framework. Within the boundaries of the regulatory framework, (subnational) governments can set up an RSWF. A clear regulatory framework is required to offer governments sufficient guidance on the RSWF set up and operations. The regulatory framework may be set up through an act of parliament or through an issuance by the relevant executive agency, as long as the agency is given the institutional mandate by law to promulgate such issuances. Given the long-term nature of investment activities of an RSWF, it is necessary for RSWFs to have a robust regulatory basis and framework that are de-linked from political cycles.

The regulatory framework of the case studies provided a comprehensive description of the RSWF's organization and operations. A regulatory framework should provide a broad indication of the following aspects:

- *Investment scope, activities, and restrictions* – description of the fund objectives and its investment mandate.
- *Financial product offering and pricing* – description of the types of financial products that can be offered and the pricing mechanisms.

- *High level investment criteria & eligible beneficiaries* – what quantity (e.g., monetary value) and quality standards projects and/or its beneficiaries need to meet in order to be eligible for funding.
- *Establishment & legal status* – what will be the legal form(s) of the RSWF including the conditions for establishing an RSWF.
- *Management & governance structure* – structuring options for management and governance bodies.
- *Source of capital & ownership* – description of the sources of capital and eligible owners and its shareholding of the RSWF.
- *Administration including: accounting, auditing and reporting* – description of administrative requirements.

Management & Governance Structure

The governance structure is a key element for the success of an RSWF. The governance structure is a system of checks and balances, specifying the work performed by the respective governing bodies (management, investment, and supervisory committee) of a fund to ensure that it is operated not only in accordance with the relevant regulation or law and its mandate, but also in the best interests of the fund and its investors.

The objective of fund governance is to uphold the regulatory principles, which are typically part of the investment fund regulations. Generally, these principles aim to ensure that:

- The fund will be managed in accordance with its objectives
- Assets are kept safe and decision-making follows standardized proceedings
- Investors hold rights to and receive their pro-rata share of the fund's assets
- The fund is managed for the benefit of the fund's shareholders and not its service providers.

Concluding from the case studies, a governance structure ensures accountability and transparency through various governance bodies, which generally and at a minimum can look as follows:

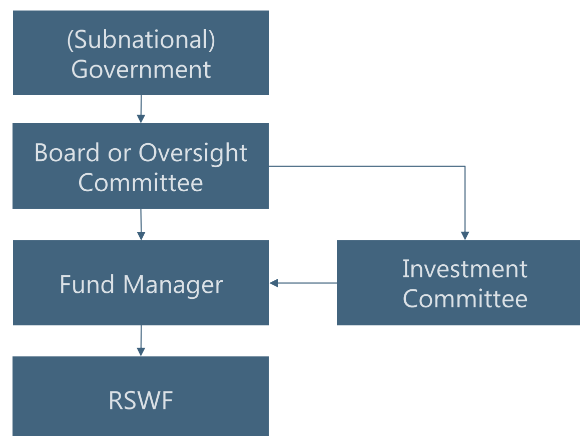


Figure 3: Typical governance structure

- *Investor or owner* – in the illustration above, this is the (subnational) government. Ownership can, however be shared between multiple public and/or private shareholders.

- *Board or oversight committee* – oversees the fund and ensures it is operated and managed according to its objectives, that performance meets expectations, and strategy is aligned with the objectives of the fund owner(s). The board is typically formed by representatives of the fund owner.
- *Fund manager* – manages the day-to-day operations of the fund, which include investment and risk management, administration, and reporting. The fund manager reports to the board.
- *Investment committee* – checks quality of decision making by scrutinizing and approving or advising on investment decisions made by the fund manager.
- *RSWF* – Legal entity that holds the assets.

The design of the governance structure should also take in consideration how the fund can be most effective and efficient. The addition of more governance bodies may result in slow and bureaucratic decision making, thereby making the fund uncompetitive and ineffective. Furthermore, strict criteria should be set for the selection of the members of the respective governance bodies to ensure qualitative and unbiased decision making. Criteria may include:

- *Members* – members must represent the interest of the fund owner (government). Members must also make unbiased decision making, which can be achieved through the addition of independent board members.
- *Experience* – members must have relevant experience and successful track record in fund relevant industries and investment management.

In addition to the main governance principles, the governance structure may also take into consideration the following:

Involvement of private sector investors or alternative sources of capital

An RSWF may seek to attract other sources of capital by sharing ownership over the fund or by leveraging its capital through the issuance of debt instruments, such as bonds. On this, the following learnings have been drawn from the case studies:

- *Adopt market practices* - To develop the trust of others, RSWFs need to adopt market accepted investment procedures, such as standardized investment process, risk management, reporting and accounting. Furthermore, the fund manager should be reporting to an independent board and the co-investment community.
- *Institutionalize accountability & reliability* - If a fund is to attract private capital or originate deals locally and bring in co-investors (e.g., syndication), it must be accountable and reliable. Putting in place systems of checks and balances (such as adhering to gold standard reporting and auditing procedures) provides these.
- *Avoid political bias* - The risk surrounding RSWFs is, that of political bias, as they are owned by the government. Political bias can undermine the credit and investment process and threaten the financial sustainability of a fund. When attempting to crowd in private capital, political bias should be avoided, through the unbiased ownership and/or governance structure and preferably also management.

Management capacity

With regard to the management of the RSWF the following lessons are drawn from the case studies:

- *Commerciality* - The purpose of setting up an investment vehicle outside of traditional government agencies, such as central banks or ministries of finance, is to create a credible third-party investor. The idea is to bring market discipline to sectors that may have never had it and to develop local financial markets. The new vehicle should thus be commercial orientation, which in turn will guide management and decision-making.
- *Outsourcing* – given the commercial orientated, management is best to be delegated to an experienced fund manager, (local) financial institution or a government specialized management agency. In case of a newly established government agency, it will take time to build organization, processes, and investment acumen.
- *Lack of investment capacity* – Also, local government institutions often lack the capacity to effectively manage RSWFs, are not commercially orientated and decision making may become politically influenced.
- *Maintaining control* - When outsourcing the management, the board or supervisory committee provide the government with the tools to keep control over the RSWF.
- *Private sector preference* – In case an RSWF seeks to involve private sector investors, these will have preference for a privately managed investment fund or specialized government agency.

Capitalization & Ownership

RSWFs are established by government institutions and are fully or partially capitalized by government. Different modalities in government ownership exist as well as in public-private ownership models. Furthermore, capital of RSWFs can be leveraged with external sources of capital.

Ownership

- *Establishment* – RSWFs are established and capitalized by government institutions and therefore always are in whole or in part owned by governments.
- *Ownership* – Ownership by subnational government (sometimes with oversight from national government), as well as shared ownership between national and subnational government institutions were found (e.g., the RDAs in the Netherlands).
- *Public-private ownership* – In cases of a shared public-private ownership model, it must be ensured that most of the public ownership is held by subnational government(s) over national government to ensure that investment strategy and decision making are aligned with local interests. Private investors would likely require majority ownership to ensure investment decision-making is free of political bias. Although in theory, shared public-private ownership is possible, none of the case studies had such ownership structure.

Capitalization & size

- *Sources of equity capital* - RSWFs are generally capitalized with local government budget surpluses, from within the local government budget and/or with budget from national government. The government's investment in the RSWF is in the form of equity, thereby gaining ownership over the RSWF.
- *Tenor* – Generally, the invested capital is of a permanent nature, e.g., invested capital is not being re-distributed but is revolving.
- *Enabling flexible financing terms* – By keeping a long-term perspective, RSWFs can provide more flexible financing terms compared to what is available in the market.

- *Minimum fund size* - RSWFs require a minimum size to remain self-sustainable over the long term. Investment returns are required to cover fund costs, management costs and potential investment losses.

Leveraging public capital
RSWFs can leverage public resources for the development of local projects, by attracting alternative sources of capital, whether domestic or international, and private or development finance. Some considerations include:

- *Leverage* - Equity investment can be leveraged with debt through the issuance of bonds or (in)direct loans, which can be as follows:
    - *Local lending* – the fund lends directly from local banks or financial institutions
    - *International lending* – the fund indirectly lends through sovereign loans from MDBs or DFI, such as World Bank or KfW.
    - *Municipal or Tax revenue bonds* – the local government institution issues tax revenue bonds of which the proceeds are on-lend or invested in the RSWF.
- *Creditworthiness* - Before an RSWF has the capacity to issue bonds on its own merit, it will need to have proven its creditworthiness as a reliable and stable financial sector player. Furthermore, an RSWF will need to have gained sufficient size in terms of assets under management, financial, operational and organization track record and a credit rating.
- *Underwriting* - As such, RSWFs bonds are often underwritten or guaranteed by public revenues. This form of financing can lead to developments in the local capital market: the market is deepened as government can lend at multiple levels and widened as investors have more investment options, which will lead to a more shock resistant / diversified capital market.
- *Use of tax revenue bonds* - Require a developed and deep local financial market to ensure liquidity over the bonds. Furthermore, tax revenue bonds require fiscal discipline of (local) government institution(s) and an effective tax collection system. The issuance of bonds on the local market requires a sufficiently developed and liquid local financial market. In the developing market RSWFs reviewed, financial sector development is typically in its nascent phase. In developed markets, this is a more common practice, as these markets are wider and deeper.
- *Alternative sources* - Alternatively, debt can be raised from international sources, such as multilateral and bilateral development institutions or MDBs & DFIs.
- *Investment rationale* – An incentive for MDBs and DFIs to finance regional development goals is that is provides them with a diversified portfolio of infrastructure projects.

Key Insights from Stakeholder Consultations

The following section describes the key motivators for potentially establishing RSWFs in Indonesia, based on stakeholder consultations in Jakarta, Indonesia with KEMENKO and Indonesian subnational government representatives. Based on the lessons learned from the case studies as well as additional relevant resources, recommendations will be made based on how these identified needs can be addressed.

RSWFs need to unlock allocation for existing financial resources

RSWFs can enable subnational governments unlock restricted financial resources which may be difficult to allocate for infrastructure investment. It was indicated during the stakeholder meetings that some Indonesian subnational governments generate excess income through budget surpluses because of economic growth, income or sale of state-owned enterprises, concessions, licenses, permits etc.

This excess income is accumulated on a (subnational) government account; however, it is unclear to governments how they can unlock these financial resources to make investments in regional infrastructure.

The current law on the establishment of Regional Endowment Funds[3], is unclear about how excess budget can be utilized for investment in regional infrastructure. An analysis of the law is included in Annexure A. Compared to the Indonesian law, the legal framework of the RSWFs reviewed in the case studies tend to provide more detail on the objectives, mandate, restrictions, governance structure and sources of capital of the RSWFs. The decree on the establishment of local development funds in Vietnam is particularly clear in the definition of the legal framework.

Finding: Based on the above findings, the RSWF model should be tailored according to the existing law and/or to new policies of KEMENKO, MoF, MHA, and/or other ministries to potentially unlock existing financial resources.

RSWFs also need to attract alternative sources of capital

Subnational governments in Indonesia seek to attract alternative sources of capital, for example those from the private sector, development finance, green and/or climate funds, to accelerate investment in local infrastructure. As such, subnational governments seek to "crowd-in" capital, which circles back to the type of sovereign development fund that seeks to attract alternative sources of capital (i.e., Crowd-in) by making investments that attract private sector investors to participate in emerging domestic industries that can attain high financial and developmental returns. Several of the case study funds seek to crowd-in capital. Approaches used in the case studies include:

- *Official Development Assistance* – the Ho Chi Minh City Urban Development Fund and Odisha Infrastructure Fund attracted ODA from respectively World Bank and KfW, through sovereign on-lending.
- *Local financial market* – The Ho Chi Minh Urban Development Fund managed to leverage its fund resources by issuing bonds that were underwritten by municipal revenues, on the local capital market. The Florida State Infrastructure raised debt through issuing bonds on its own cash flows.
- *Viability Gap Funding (VGF)* – VGF can enable the realization of projects by funding financial viability gaps and thereby mobilizing private capital resources for infrastructure development. The challenge with VGF, however, is that it depletes the fund's resources unless it can be structured successfully as a revolving fund. The Odisha Infrastructure Funds is an example of a fund that provides VGF.
- *Cross-subsidization* – although not found as part of the case studies. RSWFs can realize high-impact through cross-subsidization. In this structure, projects that yield a return, support the funding of financially non-viable but high-impact projects.

Finding: There is a lack of clarity on mechanism(s) to capitalize RSWF and clearer and appropriate mechanisms for the Indonesian context should be developed.

RSWFs should contribute to accelerating procurement process

Subnational governments are looking for solutions that can accelerate the procurement of infrastructure. The slow procurement of infrastructure particularly public-private partnerships is a

[3] LAW OF THE REPUBLIC OF INDONESIA NUMBER 1 OF 2022 CONCERNING FINANCIAL RELATIONS BETWEEN THE CENTRAL GOVERNMENT AND LOCAL GOVERNMENTS – Articles 164 - 166

multi-faceted and complex issue that is beyond the scope of RSWFs typically solve. However, RSWFs can contribute to the enabling environment for PPPs that could help accelerate infrastructure procurement processes. This is often needed to be able to build a sufficient project pipeline needed for RSWFs to be successful. For example, RSWFs can integrate transaction assistance either through technical assistance grants or technical assistance loans. Such interventions need to be designed based on specific analysis of where the gaps are in the procurement process.

Finding: There are procurement barriers that are likely to make it difficult for RSWFs to successfully invest in a project pipeline. RSWFs in Indonesia likely need to actively be involved in mitigating these procurement barriers to the extent it fits within its investment mandate.

RSWFs need to find balance between retaining government control and independent expert management

It was indicated that governments prefer to keep ownership and maintain control over RSWFs by managing and governing RSWFs themselves. The current law dictates Regional Endowment Funds or REFs are to be managed by the treasury or a government agency. This is in line with international practices, it will need to be clarified in what manner national government would take ownership. However, about the management of funds, subnational governments however lack the capacity to manage the operations.

Case studies have shown that contracting an independent investment manager is an efficient way of operationalization RSWFs. In addition, this also offers benefit to interact with private sector investors. An alternative is to establish a specialized government agency. The challenge with the establishment of a new agency is that it will take considerable amount of time to establish, build and expand the organization and its operations.

Finding: There is a lack of depth of capacity of local government to manage RSWF and will likely need to find an external expert manager

Regional governments have varying levels of readiness for implementing RSWFs

There are varying levels of readiness for implementing RSWFs both from financial readiness as well as implementing capacity. It was indicated that some subnational governments have available financial resources that they seek to unlock as well as higher implementing capacity. More explicitly, the province of West-Java has availability over capital resources and researched the possibility of setting up an RSWF. There is also more readiness from both a project pipeline and internal capacity to be able to

It will need to be investigated in more detail, how these capital resources can be unlocked, what the restrictions exist and the total and yearly amount. Furthermore, to be effective a clear law should be established on RSWFs with possibilities for external fund management, as this would enhance the execution power of fund operations.

Finding: Urgent need of local governments to implement RSWF. Furthermore, there is a lack of a coherent framework, and variety of needs of regional governments

Recommendations on next steps

Findings	Recommended Technical Assistance
An Indonesian RSWF model needs to be tailored to existing and new policies of KEMENKO, MoF, MHA, and/or other ministries	Identify options for RSWF model based on analysis of needs, and existing policies and legislation and deep dive of international best practices
Lack of clarity on mechanism(s) to capitalize RSWF	Analysis of legal options to transfer idling financial resources to set-up RSWF, and identify fund structure and vehicles to mobilize private capital resources
Slow procurement of potential projects	Analysis of procurement barriers on project/sector pipeline and options to mitigate procurement barriers, which are in line with potential mandate of an RSWF
Lack of depth of capacity of local government to manage RSWF	Gap analysis, skills assessment and tailored training to operationalize model and/or procure potential fund manager
Urgent need of local governments to implement RSWF	Pilot establishment framework and operational model in regional government with urgent need with the goal to create model/template framework (e.g. urgent need of West-Java)
Lack of coherent framework, and variety of needs of regional governments	Develop unified financing framework (and strategy) for RSWFs

Annexure A – Law concerning financial relations between central and local governments

The establishment of endowment funds is regulated under the following law:

LAW OF THE REPUBLIC OF INDONESIA NUMBER 1 OF 2022 CONCERNING FINANCIAL RELATIONS BETWEEN THE CENTRAL GOVERNMENT AND LOCAL GOVERNMENTS. Relevant excerpts from the law are as follows:
Definitions - **Regional Endowment Funds (REFs)** - are funds originating from APBD which are eternal and the funds resulting from its management can be used for Regional Expenditures without deducting the principal funds. - **APBD –** The Regional's Budget which outlines the Region's annual financial plan set by regional regulations. - **SILPA -** Excess of Budget Calculation, is the excess difference between the realization of budget receipts and expenditures for 1 (one) budget period. (eg. Budget surplus)
CHAPTER VI - ESTABLISHMENT OF ENDOWMENT FUNDS
Article 164 (1) Regions can establish Regional Endowment Funds which are stipulated by Regional Government Regulations. (2) The establishment of the Regional Endowment Funds as referred to in paragraph (1) considers, among other things, the fiscal capacity of the Regional Government and the fulfilment of the need for mandatory Government Affairs related to basic public services. (3) The results of the management of the Regional Endowment Funds as referred to in paragraph (1) are intended for: a. obtaining economic benefits, social benefits, and/or other benefits previously determined; b. contributing to regional revenues; and c. organizing the public benefit across generations.
Article 165 (1) The Regional Endowment Fund as referred to in Article 164 paragraph (1) is managed by the Regional general treasurer or Regional Government public service agency. (2) The management of the Regional Endowment Funds is carried out in an investment that is free from the risk of impairment. (3) The results of the management of the Regional Endowment Funds as referred to in paragraph (1) shall become Regional Revenue.
Article 166 Further provisions regarding the procedures for the establishment and management of the Regional Endowment Funds are regulated by or based on Government Regulations.

Article 149 (2) – (2)
In the event that the Regional SILPA is high and the service performance is high, the SILPA can be invested and/or used for the establishment of the Regional Endowment Fund by taking into account the needs of the Regional Governments' priority that must be met.

Analysis

Based on consultations during the presentations on Regional Sovereign Wealth Funds in Jakarta, it was found that local governments seek to mobilize (internal or external) resources in RSWFs with the purpose of investments in local development. Based on the understanding of the law on the establishment of regional endowment funds, the law does not seem to entirely meet the needs of the subnational governments, who seek to realize investments in regional infrastructure.

Establishment of Regional Endowment Funds
Subnational governments can establish Regional Endowment Funds (REFs) on their own, following Regional Government Regulations, depending on its fiscal capacity and the subnational government meeting its obligations relating to basic public services.

Conclusion: Regional Government Regulations would need to be reviewed to gain a deeper understanding of the REF establishment criteria.

Investment restrictions
REFs can be capitalized through SILPA (budget surplus). The principal accumulated capital in the REFs are restricted to investments in risk-free assets or investment that is free from impairment *(Article 165 (2))*. However, any proceeds (returns) from the investments may be invested in economic or social benefit or government expenditure *(Article 164(3))*. As such, all paid-in capital (eg. the total amount of accumulated budget surpluses), may only be invested in risk-free assets. However, any proceeds or returns (more than the accumulated principal amount) may be invested in regional infrastructure *(Article 149 2 -2)*. As such before being able to make meaningful investments in regional infrastructure, a REF would first need to accumulate a considerable capital base and generate considerable returns, before it would be able to make any sizeable investments in local infrastructure.

Conclusion: However, the above analysis does not necessarily exclude regional infrastructure investments, as "risk-free" investments can be structured, through for example guarantees from national government. It will have to be investigated how far the definition of risk-free can be stretched. It should be noted that unlike in developed markets, infrastructure investments in emerging markets are substantially riskier investments and are unlikely to fit within the intended investments of REF.

Capitalization restrictions
Based on the above definition, we draw the understanding that REFs can be capitalized through the APBD, depending on the fiscal capacity and the government meeting its obligations. REFs have an eternal character and so does the capital in the REF. Any, capital available (in excess to the paid in capital or principal funds) that are a result of the management of the fund, may be utilized for expenditures of the regional government.

Conclusion: The law is unclear if a REF may be capitalized with other sources of capital and/or may be leveraged through the issuance of debt instruments.

Management
REFs are managed by the Regional general treasurer or Regional Government public service agency *(Article 165 (1))*. Based on the above understanding, REFs can only be publicly managed. It is not allowed to contract an external private investment manager or company. As a result, this may exclude working private investors, which would prefer a privately owned investment manager, which would be more aligned their own interest. The investment expertise and capacity can also be developed in a specially established government agency, however it would take considerable time to build and grow such an organization and processes.

Conclusion: The case studies indicated that mandating the management to a private investment manager is common practice, which can result in a closer cooperation with the private sector.

Annexure B – Case Studies

1. Vietnam: Ho Chi Minh City Urban Development Fund

1.1 Background and Establishment

Country: Vietnam
Sub-national: Provincial & municipalities
Purpose: Financing of municipal infrastructure
Products: Equity & Debt
Capitalization source: Local government budget and local bond issuance

Local Development Investment Funds (LDIFs) in Vietnam originate from the need to develop municipal infrastructure in response to an increase in the demand for municipal services, which was a result of rapid urbanization, decentralization, and high rates of economic growth. Under the first pillar of Vietnam's Partnership Strategy in 2007-2011, the government identified the need to reform the financial system, an essential element of which was the development of a local capital market to support the financing of infrastructure.

A significant investment gap existed in municipal infrastructure. During the development of the partnership strategy, it was assessed that the magnitude of the infrastructure demand was unlikely to be met by public investment and official development assistance (ODA). Furthermore, the need for LDIFs was spurred by the devolvement of the responsibility for municipal infrastructure development to provincial governments, which had limited budgetary resources and suffered from a combination of weak institutional capacity and policy uncertainties. Private financial markets were not adequately deep or broad, in the short to medium term, to meet the growing demand from municipals for infrastructure finance.

In response to these challenges, the government instituted the "2001 Public Administration Reform Master Contract" to enhance private investments in municipal infrastructure, which included the need and design of LDIFs. Given the need for private capital, LDIFs have commercial investment mandates and are allowed to leverage private capital and invest in municipal infrastructure projects that offer cost recovery. LDIFs are also allowed to engage in short-term borrowing from state-owned commercial banks and other state-owned enterprises[4].

The Ho Chi Minh City (HCMC) Fund for Urban Development (HIFU) was the first LDIF that was established in Vietnam and was renamed to the HCMC Finance and Investment State Owned Company (HFIC) in 2011. Up to 2022, HFIC has financed a total of about VND 11,200 billion (~USD480m) investments in over 320 projects across sectors including bridges, roads, wharves, industrial parks, new urban areas, accommodation, resettlements, schools, hospitals, clean water supply networks, wastewater treatment plants, solid waste, and public passenger transport. Transport infrastructure accounts for the largest sector financed by HFIC.

As the HFIC is established as an LDIF and is required to act according to the LDIF regulations, the following case study will focus on LDIFs in Vietnam in general. Where possible, we highlight nuances of HFIC compared to the local LDIF regulations.

1.2 Investment Mandate

The mandate of a LDIF describes its aims, the limits within which it is supposed to invest, and the investment policy. Although this may differ based on the specificities of an LDIF, the general operational scope of LDIFs is to:

- Realize projects in municipal infrastructure as defined in the local the 5-year socio-economic development plan;

[4] https://issuu.com/objectif-developpement/docs/05-va-focales

- Make investments (equity) and loans according to the list of investment and lending sectors as approved by the People's Committee;
- Mobilize medium and long-term capital from (private) domestic and foreign organizations;
- Invest in projects, invest in the establishment of economic organizations, invest in capital contribution, purchase of shares and capital contributions of economic organizations on the list of investment and lending sectors of the Fund;
- Entrustment for lending and investment; receive entrustment management of state financial funds locally, domestic, and foreign organizations and individuals;
- Carry out the operation of issuing local government bonds as authorized by the People's Committee; and
- Operate independently of the provincial or municipal budget.

1.3 Investment Strategy

The investment mandate of an LDIF is developed based on Vietnam's socio-economic development strategy, the 5-year socio-economic development plan, the actual situation of the province or municipality, and the operation scale of the local development investment fund. Annually, the LDIF manager proposes a list of investment and lending sectors to contribute to promoting socio-economic development of the province or municipality and which may include investments in the following sectors:

- Education;
- Health care;
- Industry;
- Agriculture & Fisheries;
- Environmental services;
- (Renewable) Energy;
- Housing;
- Culture & Tourism;
- Transportation;
- Fields to encourage socialization; and
- Other priority areas

Based on the 5-year operation plan approved by the People's Committee, the LDIF shall draw up the operational plan and annual financial plan for the fund management council to submit to the People's Committee for approval. The LDIF will then provide investments and loans according to the approved list[5].

1.4 Financial Products

[5] https://documents.worldbank.org/en/publication/documents-reports/documentdetail/998561468782112468/vietnam-hifu-development-project

LDIFs can provide both risk capital (equity) and loans[6].

1.4.1 *Investments*

LDIFs are able to offer a very wide range of risk capital, however the effective investment strategy is restricted in the fund design to maintain sufficient control over the capital in the fund.

LDIFs can provide risk capital for:

- Equity investments in for profit companies;
- Equity investments in the form of a contract (public-private partnership - PPP investment contract and business cooperation contract - BCC) or implementation of an investment project;
- Other forms of investment allowed by law.

1.4.2 *Loans*

Although LDIFs have the capacity to make investments (risk capital), they are predominantly set up for lending purposes, where LDIFs offer a unique value proposition by offering long-tenor loans which fit the requirements of infrastructure projects.

- **Tenor:** Up to 15 years (>15 years when approved by the People's Committee)
- **Collateral Security:** Land, housing, buildings, structures, and other immovable assets (in accordance with law on loan security) or otherwise in accordance with the loan law.
- **Interest rate:** Market-based interest, taking into account the following:
    - *The minimum lending interest rate determined on the principle of not being lower than the average interest rate of mobilized capital sources, considering the opportunity cost of equity capital, management costs, risk provisions and other costs related to lending activities.*
    - *Risk premiums are determined by the LDIF manager on a transactional basis.*

1.5 Institutional Structure

LDIFs are fully (100%) owned by the respective provincial or municipal government body. It is a public agency with unremunerated equity (i.e., no cash will flow back to the shareholder) provided by its public shareholder(s). LDIFs are established as commercial financial institutions[7].

1.6 Governance Structure

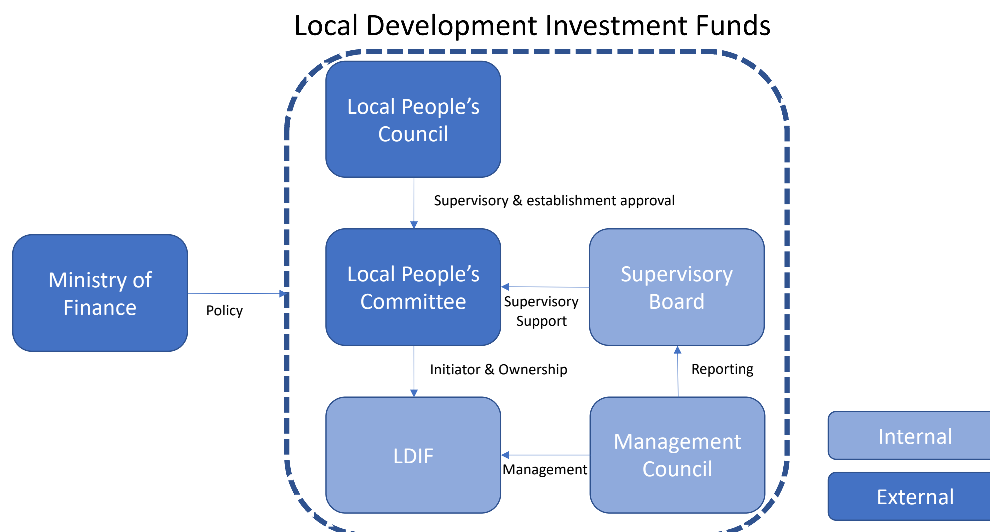
The governance structure of LDIFs is made up of multiple governing bodies, which can be classified as either internal or external bodies. The internal bodies are directly involved in the operations of the LDIF, whereas the external bodies take a role as owner and supervisor. The governing structure of LDIFs is reflected in the below overview and each body is described in subsequent sections.[8]

---

[6] https://documents.worldbank.org/en/publication/documents-reports/documentdetail/998561468782112468/vietnam-hifu-development-project

[7] No: 147/2020/ND-CP - PROVISIONS ON ORGANIZATION AND OPERATION OF LOCAL DEVELOPMENT INVESTMENT FUND

[8] No: 147/2020/ND-CP - PROVISIONS ON ORGANIZATION AND OPERATION OF LOCAL DEVELOPMENT INVESTMENT FUND



1.6.1 Ministry of Finance

The Ministry of Finance (MoF) is not directly involved in the establishment and operations of LDIFs. The MoF however is responsible for developing and submitting to the national government any proposed mechanisms and policies on the organization and operation of local development investment funds and coordinating with the State Bank of Vietnam in managing lending activities of LDIFs. As a national level entity, the MoF is thereby not directly involved in the governance structure, but only at a policy level.

1.6.2 People's Council (Supervisory body)

The People's Councils represent the local authority of the state and are the top supervisory bodies at each level. They do not govern directly but instead elect and oversee People's Committees that act as executive bodies carrying out local administrative duties. The People's Council is, among others, responsible for:

- Approval of establishing a LDIF;
- Deciding on the organization and operation method of the LDIF;
- Approval of the plan on capitalizing the LDIF from the provincial or municipal budget;
- Approval of the list of investment and lending sectors of the LDIF; and
- Supervision of LDIF operations.

1.6.3 People's Committee (Executive body)

The main function of the People's Committee is to represent the state as owner of the LDIF. Furthermore, the People's Committee acts as the initiator of the establishment of a LDIF and submits it to the provincial People's Council for approval and request for budget (e.g., fund capitalization resources). Furthermore, the People's Committee is involved in the approval and supervision of the LDIF strategy, operations, and appointment of the fund Management Council.

1.6.4 Fund Management Council

The fund Management Council is responsible for the day-to-day operations of the LDIF. The People's Committee shall appoint the members of the Management Council and on other matters. LDIF may be organized and operated by either:

- Establishing an independent management and administration company in the respective province or municipality; or

- Entrusting other financial institutions in the province or municipality to manage and administer the LDIF.

People's Councils, advised by the People's Commission, shall decide on the mode of organization and administration.

1.6.5 Supervisory Board

The LDIF Supervisory Board assists the People's Committee and the fund Management Council in controlling the organization and exercise of the rights of ownership and the management and administration at the LDIF.

1.7 Investment decision making

The authority which will take investment decisions is based on the relative total value invested by the LDIF. Thresholds for investments and loans differ and are as follows:

- Decision making for projects where equity is invested in an enterprise or project:
    - Up to 10% of LDIF's equity – Management Council
    - >10% of LDIF's equity - People's Committee
- Decision making for financing by extending loans to projects:
    - Up to 15% of LDIF's equity – Management Council
    - >15% of LDIF's equity - People's Committee

1.8 Legal Basis

LDIFs are established under a government decree. The first decree on the organization and operation of LDIFs dated from 2008 (Decree No. 138 dated August 29, 2007). In 2021, together with Decree 37 dated April 22, 2013, this decree was replaced by Decree No. 147 dated February 5th, 2021. The Decree prescribes the organization and operation of a LDIF established by a province or centrally-run city. Furthermore, the decree describes the activities of capital-raising, lending, investing, entrusting and receiving entrustment to perform the function of LDIFs.

A LDIF is established as an off-budget state financial fund established and operated by the People's Committee of a province or centrally run city.

LDIFs are comparable to any other fund and have a legal status, charter capital, seals, and may open accounts at the State Treasury and commercial banks lawfully operating in Vietnam.[9]

1.9 Capital Structure

People's Councils are responsible for approving capital from the local government budget for the capitalization of LDIFs. LDIFs are thereby 100% government owned. However, they can be leveraged by attracting other sources of domestic (private) and foreign capital. LDIFs can also receive and on-lend capital (among other ODA funds), which will be managed in accordance with the ODA agreement[10].

1.9.1 Bonds

As one of the goals of the LDIFs is to deepen and broaden local capital markets, LDIFs can also leverage its equity base by issuing local government bonds (with local government as the issuer) in the local capital market.

[9] *no: 147/2020/nd-cp - provisions on organization and operation of local development investment fund*
[10] *https://cii.com.vn/en/introduction/founding-shareholders*

The source of bond repayment is guaranteed from the revenue of the local government budget11. Issuance of municipal bonds have been the main source of capital for the HFIC, for example. Bond terms in the municipal bond market range from 3- to 30-year with fixed rate. The majority of sub-national governments issue bonds with five-year tenors, accounting for 50 percent of total issued volumes. So far, only HFIC has successfully issued bonds with 10- to 30-year tenors (21% of volume), which reflects the maturity of HFIC relative to other LIDFs in Vietnam.

1.9.2 Other sources of capital

HFIC was able to attract funding from the World Bank[12]. The objective of the World Bank financing was to develop HFIC as a model LDIF (in terms of internal policy and procedures for financial policy, sub-project appraisal, social and environmental safeguards, and partnership with the private sector) and increase private sector participation in financing municipal infrastructure in general. Total loan was USD 50m with 10-year grace period and 40-year tenor.

1.9.3 Minimum capital requirement

The charter capital at the time of establishment of a LDIF shall not be less than VND 300 billion. Furthermore, LDIFs of which the charter capital drops below this threshold will be dissolved, when not sustaining the minimum fund size for a longer period. Minimum capital requirements to funds are often put to ensure operational efficiency and continuity.

1.10 Project Example

HFIC invested in a project for production of 300 clean-energy buses powered by Compressed Natural Gas (CNG) to gradually replace old fossil-fueled buses as a move to cleaner air in Ho Chi Minh City. The project was implemented by Saigon Transportation Mechanical Corporation (SAMCO) between 2013 and 2015 at a total investment of approximately VND 163 billion (USD 7.8 million). CNG buses bring proven economic benefits: CNG buses bring both economically and environmentally benefits. Emissions from the CNG buses are significantly lower compared to conventional diesel-powered buses and CNG vehicles also operate more quietly, while reducing fuel costs by almost 30%.

1.11 Key Lessons Learned

- LDIFs are set up as commercial financial institutions and act accordingly, however they do not generate cash return for shareholders, and returns are fully recycled for new investments
- LDIFs are capitalized with and based on this can mobilize other sources of capital, for example through issuance of bonds on the local market
- LDIFs are established and approved by local governing bodies (in Vietnam the People's Committee of the province or municipality).
- Ministry of Finance only takes the role of policy implementor and maker.
- LDIFs can mobilize significant alternative sources of capital for public investments. With total lending activities of ~USD480m HFIC is a good example of a successful LDIF.

---

[11] *from july 1, 2018, municipal bond issuances have followed the 2017 public debt management law, decree no.93/2018/nd-cp (june 30, 2018) on sub-national government debt management and other regulatory guidelines on government bond issuances. the bond issued volume must be within the annual sub-national government debt limit approved by the national assembly. issuing municipal bonds is one of the means to raise capital for local governments under provisions of the state budget law and law on public debt management.*

[12] *https://www.worldbank.org/en/news/loans-credits/2007/06/20/vietnam-ho-chi-minh-city-investment-fund-for-urban-hifu-development-project*

- LDIFs are comparable to any other fund and have a legal status, charter capital, seals, and may open accounts at the State Treasury and commercial banks lawfully operating in Vietnam
- A minimum of VND 300bn (~USD 13m) is necessary to establish a LDIF, to ensure operational continuity.
- LDIFs can be managed through a SPV (established by government for management and administration) or a local regulated financial institution.
- LDIF structure is layered with multiple supervisory bodies (3), which may render operations inefficient.
- LDIFs are capitalized through the budget of the respective local government body (province or municipal).
- Leverage is created through issuance of local government bonds, which are subsequently (partially) guaranteed by the national government and services from the revenue from the local government budget.
- When a LDIF is sufficiently mature (such as HFIC), there is appetite in the market to take of long tenor bonds (10 – 30 years).
- In Vietnam, provincial and municipal government have full autonomy over LDIFs. The national government, through Ministry of Finance, is only involved through policy making.
- HFIC seems like a successful example of a sub-sovereign wealth fund, as it was capitalized through the municipals budget, issue bonds, attract ODA from the World Bank and invested in projects with public benefits.
- Most LDIFs are currently at the start-up phase or are just in the process of being set up, sometimes ambitiously, sometimes without the local managers fully grasping or understanding yet the funds' potential. It is often the manager of the local Vietnam Development Bank branch that takes charge of the management.

2. The Netherlands: Regional Development Agencies

2.1 Background and Establishment

Country: The Netherlands
Sub-national: Provincial or Regional
Purpose: Financing of innovative industries
Products: Equity & Debt
Capitalization source: budget of national government or government bonds (AAA)

Initially, Regional Development Agencies (RDAs) were established during the 70's, at the initiative of the MoEA (MoEA), to address economic underdevelopment in specific rural regions. Due to economic development, the focus of RDAs has since shifted to strengthening and advancing regional economies in general. RDAs support entrepreneurs with innovation, investments, and internationalization, so that they can accelerate the growth of their companies. RDAs thereby promote sustainable growth of regional economies, help create jobs and improve (rural) livelihoods in general. RDAs also support entrepreneurs in times of economic uncertainty, such as during the COVID-19 crisis. With the incorporation of Invest-NL in 2020, a nationally focused development agency and governed by MoEA, RDAs under the guidance and in support of Invest-NL. Whereas before 2020, RDAs were able to support any project in their own geographical area and focus themes, they now act in support of Invest-NL. In this respect, Invest-NL will focus on large scale projects with substantial capital needs enabling the development finance environment to focus more on drawing in foreign corporates and FDI. In this structure, RDAs will be focused on supporting local SMEs, that fall within the boundaries of Invest NL and their respective Economic Development Agenda's.

Currently, The Netherlands has nine RDAs that aim to strengthen the (regional) economic structure. The RDAs were established at the initiative of the MoEA. Through a subsidy relationship, MoEA is responsible for policy for the RDAs and promotes shareholding through the private equity firm. The nine RDAs include:

1. **The Brabant Development Agency (BOM)** - active in the province since 1983;
2. **Horizon** - active in the province of Flevoland since 2019;
3. **Impuls** - active in the province of Zeeland since 2007;
4. **InnovationQuarter** - active in the province of South Holland since 2014;
5. **The Limburg Institute for Development Finance (LIOF)** - active in the province of Limburg;
6. **The Northern Development Agency (NOM)** - active in the provinces since 1974 in Drenthe, Friesland and Groningen;
7. **Oost NL** - was created in 2017 from a merger of Gelderland & Overijssel RDA's;
8. **RDA InWest** - active in the province of North Holland since 2021;
9. **RDA Utrecht Region** - has been active in the province of Utrecht since 2020.

In the case study RDA Utrecht will be used as a trailing example. Where RDAs share communalities, reference will be given to RDAs in general. RDA Utrecht is one of the most recent RDAs. It was founded because of the RDA restructuring in 2020, thereby requiring each province to have a (shared) RDA. The investment agenda of RDA Utrecht is mostly driven by population growth. It is projected that the number of inhabitants will grow with approximately 165,000 inhabitants over the next 20 years (~+12%). The province wants to facilitate this growth to utilize the influx of knowledge, ideas and skills for the well-being and prosperity of the province. At the same time, the provincial government wants to ensure the quality of life in the region does not suffer from this growth, given the already high population density.

The RDA Utrecht is a broadly supported RSWF as its an initiative of different local actors including: the province of Utrecht, (6) municipalities, Utrecht University, the University Medical Centre Utrecht and on a

national level the MoEA. Furthermore, support and prioritization was given to RDA Utrecht, given that in other provinces RDAs have proven to play a major role in stimulating the local economy by creating new jobs and wealth.

2.2 Investment Mandate

The main aim of the RDAs in the Netherlands is to promote economic growth (through additional investments), boost employment and innovation in the region, in conjunction with possible solutions for social issues. In this respect, the RDAs mainly focus on young, innovative companies and have four main focus areas:

- Participations in the form of investing in private companies and managing those participations;
- Promoting development and innovation by companies, with focus on SMEs;
- Promoting investment by bringing foreign companies to the Netherlands and prevent companies from moving abroad;
- The restructuring and development of industrial estates.

2.3 Investment Strategy

RDA Utrecht's investment strategy is focussed permanently strengthening the economic structure of the region, thereby guaranteeing jobs, prosperity, and well-being. Now and in the future. Utrecht RDA aims to meet the need for (risk) capital among innovative and growing SMEs within the region. RDAs only provide financial support when there is so-called "market failure". It also supports the business community and projects submitted by the business community aimed at renewing and improving the living environment.

The investment strategy is formed by the principles of the Regional Economic Agenda (set by MoEA together with local government authorities and business environment) and in line with nationally defined top-sectors and innovation policy relevant to the region. Leading themes in this respect for RDA Utrecht are Future-proof living environment, Healthy people, and Digitization.

Avoidance of market competition

With its financing, RDAs aim to meet the needs of the target group, without taking over the role of the commercial financial market. To avoid *market disruption and incompatible government support*, the investment principles of RDAs are structured as follows:

- Never finance or participate alone (without a market party) or act as lead investor. RDAs need to catalyse private sector investments.
- Never take an interest in a company > 50% in the issued share capital. RDAs should never assume most of the risk, thereby creating an agency problem.
- Always offer the market the proposal for financing or participation first to be able to make optimum use of market power. RDAs need to ensure they don't disrupt the market.

2.4 Financial Products

Financing by RDAs is generally provided in the form of venture capital, being share capital, convertible loans or subordinated debt. The amount of a Financing per Applicant is:

- **Ticket sizes:** Minimum EUR 250,000 with max of EUR 1,250,000 (per investment round). More than € 2,500,000 (over two tranches) may never be provided to one costumer or group of companies,

being 2 times the maximum ticket size. Because RDAs always works together with a bank and/or a private equity party, the requested "ticket" up to € 5 million can be filled with equal financing parts.

- **Equity participations:** In all cases where RDAs participate in shares in the capital (or equity-like), the RDA will hold a meaningful shareholding with a minimum of 5% and a maximum of 49% of the issued share capital.
- **Debt financing:** The amount, duration and tranches of the Financing are matched and structured based on the business plan, thereby offering a high level of flexibility[1]. The RDA can define payment milestones on which the financing can be provided. The interest or fee shall be in line with the market or slightly above it.
- **Debt Pricing** The RDA must have a revolving character. Thereby the target return of the RDA, after deduction of costs, tax, inflation and currency depreciation, must retain an equivalent capital. Taking all these factors in consideration, it is estimated the minimum annual return should be 4% at RDA level (eg. After deduction of management fees and currency depreciation).

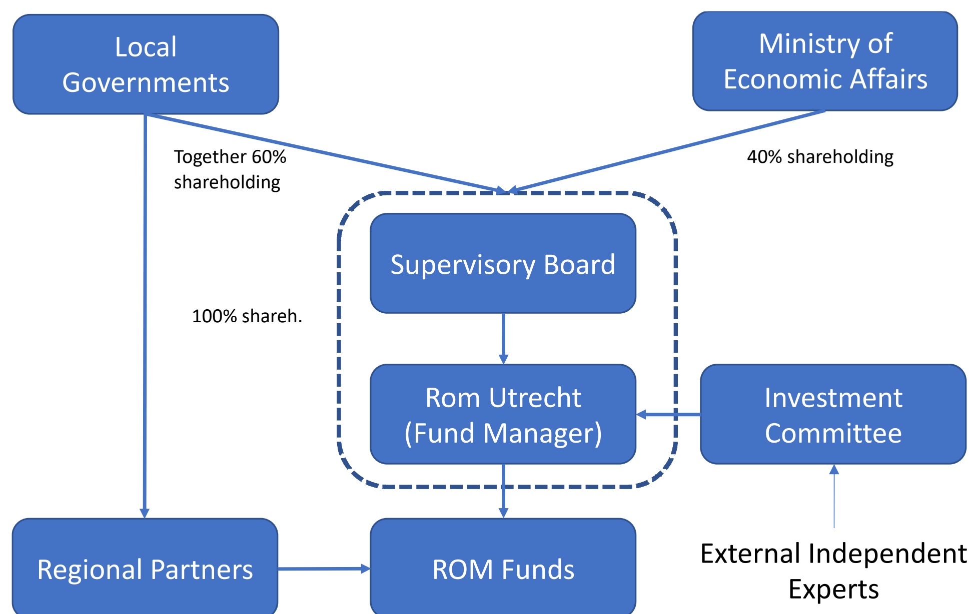
2.5 Institutional Structure

In order to enable the RDA to operate quickly, in a market-oriented manner and to limit the resulting risks, the RDA is structured as a Private Limited Company. When opting for the limited, shares must always be offered to the incumbent shareholders. This reduces the chance that conflicts of interest could arise at shareholder level. The risks for the shareholders are limited to their contribution to the private limited company. The MoEA, the province of Utrecht, the municipalities of Amersfoort, Hilversum, and Utrecht and possibly the UMCU and Utrecht University will become shareholders of the RDA. The regional partners jointly acquire 60% of the shares in the RDA. The remaining 40% is obtained by the MoEA, thereby ensuring the majority of ownership is represented by local stakeholders. The initiating government bodies have committed, on a long-term basis, to contribute to the exploitation budget of the RDA and invest capital in the RDA fund, this according to their respective financial capacity.

2.6 Governance Structure

The day-to-day management of the RDA is carried out by the Fund Manger. The functioning of the RDA, and the functioning of the Fund Manager is monitored on a regular basis by the Supervisory Board and annually by the AGM. The Supervisory Board assesses the functioning and whether the RDA achieves its objectives. The AGM tests the performance against the long-term policy and the RDA's framework. In accordance with the wishes of the shareholders and the MoEA, the functioning and effectiveness of the RDA will be evaluated periodically. The governance structure of RDAs is very much in line with common market practices. The Utrecht RDA governance structure is as follows:

[1] Taking in consideration that RDA are long-term revolving funds.



2.6.1 General Meeting of Shareholders

The shareholders form the General Meeting of Shareholders (AGM). The AGM appoints the members of the Supervisory Board (SB) of the RDA. These in turn appoint the director, after approval by the AGM. The AGM provides the frameworks within which the RDA operates, such as the assignment to operate within the Regional Economic Agenda. The General Meeting of Shareholders (AGM) consists of all shareholders of the RDA. The key powers of the AGM are:

- Approve the strategic plans (long term) of the management
- Adoption of the annual accounts
- Appoint members of the statutory board, after nomination by the Supervisory Board
- Decisions regarding: amendments to the articles of association, amendment of the issued capital and issuance of shares, making distributions from equity and changing the registered office or dissolving the company
- Determining the frameworks within which the RDA operates

Resolutions at the AGM are taken based on shareholding, as long as a qualifying majority of the shares (50%+1) is represented.

2.6.2 Supervisory Board

The Supervisory Board, on behalf of the AGM, supervises the operational management of the RDA. The Supervisory Board has a minimum size of 3 and a maximum of 5 people and will be composed of independent experts. The Supervisory Board has the following duties and powers:

- Testing the activities of the RDA against the policy of the RDA
- Approve the strategic and annual plans of the management
- Approving interim reports (quarterly reports)
- (joint) signing of the annual accounts
- Nominate statutory directors for appointment to the AGM

- Deciding on the remuneration of the members of the Executive Board as appropriate
- within the remuneration frameworks
- Assess the performance of the board
- Management solicited and unsolicited advice

The voting rights of the Supervisory Board are equally distributed among all members. Decisions of the Supervisory Board are taken by a majority of votes. If the votes of the members present at the meeting of the Supervisory Board are tied, the chairman has a casting vote.

2.6.3 Fund Manager

The Fund Manager is instructed to design and implement the policy of the RDA and to be accountable for this to the Supervisory Board. The day-to-day management and responsibility for the functioning of the RDA lies with the statutory Fund Manager. The Fund Manager must have relevant (local) experience and qualities to develop the RDA into a market-oriented and solid institute. From an operational aspect, the Fund Manager evaluates the financing applications and test those against State Aid restrictions (also to ensure market is not disturbed) prior to going into further detailed investment analysis. The Fund Manager submits the investment proposal to the investment committee for review and approval once the proposal is deemed qualitative enough by the fund manager and its investment team. Other roles of the Fund manager include portfolio and risk management, financial and impact reporting and maintaining an active network with local business environment and related instituted such as educational and health care institutions.

2.6.4 Investment Committee

In the investment process the investment committee is the governance body that approves investment proposals based on the project meeting the investment criteria (quality) and eligibility criteria of the RDA or respective sub-fund. The RDA investment committee consists of 3 to 5 independent external industry experts that are experienced in the local economy. If the investment committee approves the financing/participation proposal, the financing can be provided. If the investment committee approves the financing/participation proposal, but the amount or the conditions exceed the competence of the investment committee, the proposal can be submitted to the Supervisory Board. The decision of the investment committee is not without obligations but must be regarded as a binding recommendation for the Fund Manager. Deviation from this advice is only possible by submitting investment proposal to the Supervisory Board to obtain approval. This should however be an exception to the rule.

2.6.5 Regional Partners

Regional partners can act as co-investor in specific RDA Funds. Regional partners are 100% owned by a local government authority and allow local governments to, in addition to their contribution to RDA Utrecht, invest in specific themes, geographies or industries that they deem relevant for their respective economic development agenda.

2.6.6 Participants board & Economic Board

The Participants board and Economic Board do not have a formal position in the governance structure of RDA Utrecht. They play an advisory role to ensure the voice of the local business environment, education and health care sector is being heard.

- **Participants Board** – the participants' council is formed with the parties that contribute to the operational costs (small municipalities), but that are not shareholders in the RDA. This is an advisory body of the RDA. Each year, the participants' council advises the management on the annual plan and the policy intentions of the RDA. The participants' council receives the annual report and other progress reports each year.

- **Economic Board** - The leading companies from the Region are represented in the Economic Board, also form an advisory board for the management of the RDA. They identify and advise on current

economic developments in the region and the possible role of the RDA in this regard. To this end, the RDA management will call on the Economic Board on a regular basis. The frequency of this is variable, but at least twice a year.

2.6.7 Ministry of Economic Affairs

As with all RDAs in the country, the MoEA is an important partner, this also applies to the RDA Region Utrecht. MoEA plays a key role in the establishment of RDAs and as a shareholder. In addition to contributing to annual operation budget and capital contribution. MoEA has an elementarily role in connecting national themes to ensure regional economic policy is coordinated on a national level. Naturally, the RDA conforms to the so-called "shareholder instruction" of the MoEA. Through the connection with the regional economic agenda, the RDA links up with the mission-driven top sectors that are relevant to the region, which are supported by MoEA. As a shareholder however, MoEA will only be a minority shareholder, whereas the local government authorities jointly will hold the majority.

2.7 Legal Basis

RDAs find their origin in 1974, when the first RDAs were setup to invest in regional economic development to fight rural economic decline, which was a result of the economic crisis of the time. RDAs are setup by the MoEA as a result from local economic policy notes. Over the years, due to economic growth, the RDAs have been repurposed and their respective role has changed from economic recovery to investing in economic growth and innovation. RDAs are not established under a specific law, regulation, or decree. They find their origin from regional economic policy decision making, that have been taken by the MoEA in cooperation with relevant local government institutions.

2.8 Capital Structure

The RDA Utrecht has been established by the MoEA, together with local government authorities which include: the province of Utrecht, the municipalities of Amersfoort, Hilversum, and Utrecht. On the long term, potentially also the Academic Hospital of Utrecht and the Utrecht University will become shareholders. In order to ensure RDA Utrecht serves the regional economic agenda, the local government authorities jointly have 60% of the shares in the RDA. The remaining 40% is held by the MoEA. The founding government authorities have initially capitalized the RDA as following and have formulated long term investment goal:

	Target investment	**Start Investment**
Province of Utrecht	EUR 15m	EUR 8m
Municipality of Utrecht City		EUR 3m
Municipality of Amersfoort		EUR 1.5m
Municipality of Hilversum	EUR 15m	EUR 1m
University of Utrecht	Once sufficient size & Track Record	
Academic Hospital of Utrecht	Once sufficient size & Track Record	
MoEA	EUR 20m	EUR 8m
Total	EUR 50m	EUR 21.5m

The capital amount is expected to be sufficient to finance the developments of the regional business community over the next 5 years. This means that approximately € 10 million from the fund is available annually for investments in companies.

2.8.1 RDA Capitalization

RDAs must have sufficient capital at its disposal to properly carry out the task assigned to it: strengthening the economic structure. Intentionally, RDAs are not supposed to go beyond that as it may lead to market distortions. As a result, the RDA capitalization is a result of an analysis of the amount of capital needed (proportionally the amount the RDA wishes to contribute) to solve market failures in the financing of innovative SMEs. Furthermore, the RDA capitalization must be large enough to be revolving. In this respect the size must be large enough to carry the fund management costs and the RDA must be able to develop a broad and diversified portfolio. Based on experience, the MoEA maintains a minimum RDA starting size of EUR 20m with target capital of EUR 50m within 5 years after start of operations to remain economically viable over the long term.

2.8.2 Alternative sources of capital

RDAs are solely capitalized with public resources, which are unleveraged. In a sub-fund level, RDAs however can cooperate with co-investors / co-owners. RDAs don't issue bonds to leverage public resources, this as RDAs aim be non-market distortive.

2.9 Project Example

In 2022, RDA Utrecht co-financed Glowfarms, new innovative indoor farming concept. Thanks to the unique cultivation technique, a conveyor belt that moves up and down, the new indoor farm of Glowfarms will become the most advanced vertical farm in Europe. Glowfarm's innovative indoor farming technique results in 95 percent less water use, no use of pesticides, no impact on scarce agricultural land and lower CO2 emissions compared to conventional agriculture. With the added advantage of being independent of the weather or the seasons, resulting in a stable price and quality all year round. Glowfarms scaled up from a modest 110 square meter pilot farm in Hoorn to 2700 square meters in Leerdam (~25x). Where there was one conveyor belt in the pilot farm, the new indoor farm has room for eight much larger conveyor belts, which together can produce 1000 kilos of lettuce and herbs per day. With twenty employees, the young company is working towards a fully automated process in which seeds grow into plants. Glowfarms is a clear project example of how RDAs invest in scaling of innovative SMEs[2].

2.10 Key Lessons Learned

- RDAs explicitly take the position of avoiding disturbance of competitive markets, as such RDAs are never a lead investor, but it will co-finance with banks and other investors. Furthermore, the investment offering is targeted towards underserved segments
- The investment strategy of the RDA's is supposed to be broadly supported as it is developed between the MoEA and local governments authorities, with consultative input from the local business environment and education institutions.
- RDAs are not established under a specific law, they are a result of economic policy decisions, which can be fluid or adjusted, given that the role of RDAs over the years has changed from fighting economic decline to economic growth and innovation.

---

[2] https://www.romutrechtregion.nl/

- RDAs invest in innovation to strengthen and diversify the national and local economies, as per example of Glowfarms.
- RDAs put emphasis on including independent experts in the governance bodies to ensure inclusion of industry expertise in decision making and avoidance of political influenced decision making.
- Majority shareholding is held by local governments to ensure the RDA serves local interest.
- RDAs are revolving funds, which are required to carry their own budget. In this respect, RDAs can provide financing to innovative companies, but need to ensure commercial viability.
- The governance structure of RDAs is comparable to common market practices and each governance body carries the right amount and kind of responsibilities, thereby ensuring the interest of the shareholders is served.

3. USA: Florida State Infrastructure Bank

3.1 Background and Establishment

Country: United States
Sub-national: State-level
Purpose: Financing of local transportation infrastructure
Products: Loans and credit enhancements
Capitalization source:

- Federal account: Federal funds
- State account: State funds and bond proceeds

State Infrastructure Banks (SIBs) in the United States constitute revolving infrastructure investment funds established and administered by states to finance a wide range of transportation projects.[1] SIBs are designed to complement traditional Federal grants by giving States greater flexibility in financing infrastructure investments.[2]

SIBs were first authorized in 1995 under the "National Highway Designation Act (NHS)" to support the acceleration of mobility and transportation improvements by offering a variety of financial assistance options to local private and public entities (i.e., local transportation authorities, economic development agencies, transit agencies, local transportation departments, etc.) through state transportation departments (DOTs).[3] Initially, the NHS authorized the U.S. Department of Transportation (USDOT) to establish a pilot program and select 10 states to participate and enter into cooperative agreements with the Federal Transit Administration (FTA) or the Federal Highways Administration (FHWA). Under these cooperative agreements, participating states could use a portion of their Federal-aid funds (provided in fiscal years 1996 and 1997) as seed money for the establishment of their SIBs.[4] The selected states were Arizona, California, Florida, Missouri, Ohio, Oklahoma, Oregon, South Carolina, Texas, and Virginia. In 1997, Congress passed the USDOT Appropriations Act, which expanded the program by enabling additional qualified states to participate and provided USD 150 million general fund appropriation to support SIB capitalization.[5]

Subsequently, the Transportation Equity Act for the 21st Century (TEA-21) of 1998 expanded the pilot program for four States (Florida, Rhode Island, Missouri, and California), enabling them to further capitalize their SIBs with Federal-aid funds provided through fiscal year 2003.[6] [7] In 2005, Congress authorized a permanent SIB program (codified in Title 23 of the United States Code) and expanded eligibility to include all States and U.S. territories.[8] Approximately USD 661 million in Federal-aid funds were provided to capitalize SIBs between fiscal years 1996 and 2003.[9] To date, no additional Federal funds have been made available to capitalize SIB pilot programs.

[1]BATIC Institute: An AAshto Center for Excellence, 2022.
[2]U.S. Department of Transportation Federal Highway Administration, 2002.
[3]Texas Department of Transportation , n.d.
[4]United States Environmental Protection Agency, 2013.
[5]AASHTO Center for Excellence, n.d.
[6]AASHTO Center for Excellence, n.d.
[7]The remaining SIBs could continue to operate with the Federal funding authorized in fiscal years 1996 and 1997, as well as any additional State or local funds.
[8]Federal Transit Administration , 2015.
[9]U.S. Department of Transportation Federal Highway Administration, 2002.

Text Box 1. Summary of SIB Legislative History

SIB Legislative History

- **1995:** NHS Act established the pilot SIB program in 10 states.
- **1997:** U.S. DOT Appropriations Act expanded the program to include 39 states and provided USD 150 million to support SIB capitalization.
- **1998:** TEA-21 provided additional funding to four States to capitalize their SIBs.
- **2005:** Congress authorized a permanent SIB program (codified in 23 U.S.C. 610.).

In total, 33 States have established SIBs and provided some type of financial assistance to transportation projects.[24] The FHWA reports that, as of 2016, participating States have entered into 834 loan agreements totaling USD 5.9 billion.[25] It should be noted that States are at varying stages of SIB program implementation, from limited or moderately active programs to more robust and mature ones.[26] Additionally, the size of SIBs – based on total size of loan agreements - also varies significantly from less than USD 1 million (Arkansas) to more than USD 350 million (Arizona).[27]

The Florida SIB, housed in the Florida DOT's Project Finance Office, was established in 1997 (Section 339.55 of the Florida Statutes), and constitutes the second most active SIB in the country (measured by value of agreements). As an early adopter, Florida received multiple rounds of federal capitalization (see Text Box 1).

The Florida SIB includes Federal and State capitalized accounts, both of which operate under the same SIB institution (a common feature among SIBs). The Federally funded SIB account is capitalized with Federal money and the requisite state match funds. The State-funded SIB account is capitalized with State money only. Although the State-capitalized account is not technically a SIB as the State is not required to report to the USDOT, the same individuals run the institution and select which projects are financed.

The Florida SIB has "become an important financial tool to accelerate the delivery of critical transportation projects, generate economic benefits, and encourage increased local and private participation in transportation projects."[28] For each USD 1 loaned by the combined Federal and State-funded accounts, the projects have mobilized USD 6.08 of private capital.[29] As of 2020, the Florida SIB had funded 106 loans, amounting to USD 1.9 billion.[30]

As described, a SIB must operate within the purview of Federal and State regulations. Due to the latter, States have been able to exercise a considerable degree of latitude in the structuring and implementation of their programs. The following case study will focus on the Florida SIB, while also showcasing key elements of US SIBs in general.

3.2 Investment Mandate

Florida Department of Transportation (FDOT) operates two separate accounts within its SIB: a Federally funded account and a State-funded account. The operating guidelines of each SIB specify the requirements and procedures for the administration of the Bank's Federally funded and State-funded accounts, in alignment with Federal and State law. While Federal legislation defines the general operating framework for a SIB (i.e., basic

[24]FHWA, 2014.
[25]Center for Innovative Finance Support , n.d.
[26]U.S. Department of Transportation Federal Highway Administration, 2002.
[27]U.S. Department of Transportation Federal Highway Administration , 2002.
[28]Puentes & Thompson, 2012.
[29]FHWA Center for Innovative Finance Suppoirt , n.d.
[30]FHWA Center for Innovative Finance Suppoirt , n.d.

requirements), State law has shaped its strategic direction and tailored the program to meet State-specific needs and priorities, as described in the subsections below.[31]

3.2.1 SIB Federally funded account

The operational scope of the Federally funded account of the Florida SIB is defined under TEA-21, and includes the following key provisions[32] [33]:

- **Forms of assistance and minimum/maximum amounts:** Funds deposited into the accounts of the SIB may be used to make loans or provide other forms of credit assistance to a public or private entity in an amount equal to all or part of the cost of carrying out the project. The minimum loan amount for each project is USD 1 million.[34]
- **Qualifying projects:** Funds may only be used to provide assistance to eligible projects under title 23 of the United States Code (USC), or capital projects as defined in section 5302 of title 49 of the USC.[35]
- **Non-Federal match:** States are required to contribute, at minimum, to the bank from non-Federal resources an amount equal to at least 25% of the amount of each capitalization grant made to the State.
- **Other requirements:** States are also required to ensure the SIB maintain an investment grade rating on its debt and/or has a sufficient level of bond or debt financing instrument insurance to maintain its viability.
- **Cooperative Agreements:** USDOT is required to enter into cooperative agreements with the States for the establishment of SIBs to make loans and assist public and private entities in carrying (or proposing to carry) out eligible projects.

The Cooperative Agreements are a critical part of the SIBs structure. As States participating in the SIB program must execute cooperative agreements with the Secretary of Transportation, which establishes the basic requirements and structure of the SIB. In the case of Florida, the Cooperative Agreement was entered into by the FHWA, the FTA, the Federal Railroad Administration (FRA) - all agencies of the USDOT – and the FDOT. Under the Agreement, FDOT is designated as the administrator of the SIB, with legal, managerial, technical, and operational capabilities (FDOT , n.d.). FHWA, FTA, and FRA oversee compliance, distribution of funds, and corrective action, as needed)(see Section 1.5.2 for further details on SIB Supervising Bodies). FDOT is required to submit annual audits and Biennial Reports to FHWA, FTA, and FRA. The components included in the cooperative agreement are outlined in Text Box 2 (FHWA , 2014). Note that the cooperative agreement is only applicable to the Federally capitalized account of the Florida SIB.

---

[31] Center for Innovative Finance Support , n.d.

[32] FHWA , n.d.

[33] Cornell Law School , n.d.

[34] FDOT , n.d.

[35] Section 5302 of title 49 of the USC defines capital projects as a project for acquiring, constructing, supervising, or inspecting equipment or a facility for use in public transportation, expenses incidental to the acquisition or construction (including designing, engineering, location surveying, mapping, and acquiring rights-of-way), payments for the capital portions of rail trackage rights agreements, transit-related intelligent transportation systems, relocation assistance, acquiring replacement housing sites, and acquiring, constructing, relocating, and rehabilitating replacement housing; rehabilitating a bus; remanufacturing a bus; overhauling rail rolling stock; preventive maintenance; leasing equipment or a facility for use in public transportation; a public transportation improvement that enhances economic development or incorporates private investment; the introduction of new technology into public transportation; the provision of nonfixed route paratransit transportation services in accordance with section 223 of the Americans with Disabilities Act of 1990 (42 U.S.C. 12143); crime prevention and security; establishing a debt service reserve; and mobility management. For additional information, see: 49 U.S.C. Title 49 Transportation, Sec. 5302 "Definitions".

Text Box 2. Key Components in a Cooperative Agreement[36]

Cooperative agreements define and designate:

- The parties to the agreement and their respective authorities;
- The entities responsible for administering the SIB;
- The accounts to be created in the SIB;
- Agreement by FHWA or FTA to make payments to the State for deposit in the SIB's Federally-capitalized account;
- The state's matching requirement;
- Financial assistance terms, including timely and appropriate use of SIB funds, allowable leveraging (i.e., use of Federal funds and State match as a source of security for bonds issues by FDOT to finance loans made through the SIB), compliance with federal laws and regulations, and use of repayment proceeds, fees, compensation, or other collateral;
- Accounting and auditing procedures, including establishment of fiscal controls and accounting procedures, annual performance audit, submission of an annual report, and records retention;
- Terms and sanctions for noncompliance with cooperative agreement; and
- Terms for amendments.

3.2.2 SIB State-funded account

The operating guidelines for the Florida SIB State-funded account are enshrined in Section 339.55 of the Florida Statutes.[37] In addition to outlining the terms of the financing and the evaluation criteria for loan and credit applicants (which will be described in Section 1.3), Florida Statutes limit the SIB participation from the State-funded account to the following projects:

- Transportation facility projects that are on the State Highway System, provide increased mobility on the state's transportation system, or provide intermodal connectivity;
- Projects of the Transportation Regional Incentive Program (TRIP)[38]; and
- Construction and enhancement of natural gas fuel production or distribution facilities.

The State-funded SIB may also lend capital costs and/or provide credit enhancements for emergency loans for damages incurred to public-use commercial deepwater seaports, public-use airports, and other public-use transit and intermodal facilities (Official Internet Site of the Florida Legislature , n.d.).

Note that, per Florida Statues, to be eligible for consideration, a project must be consistent (to the extent feasible) with local metropolitan planning organization (MPO) plans and local government comprehensive plans.[39]

---

[36]U.S. Department of Transportation Federal Transit Administration, 2005.

[37]Official Internet Site of the Florida Legislature, n.d.

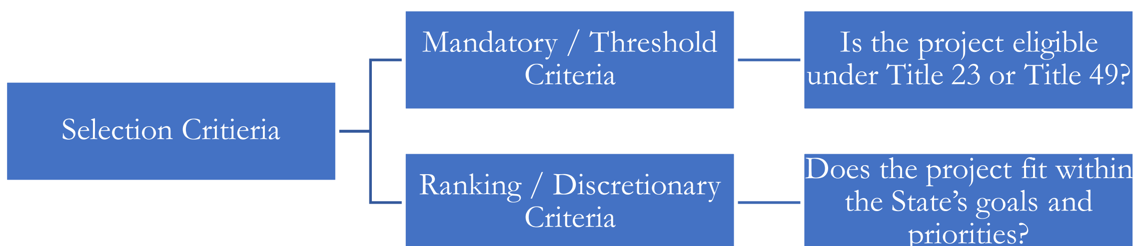
[38]Florida's TRIP is a matching program created in 2005 to promote regional planning and leverage investments in regionally significant transportation projects. TRIP monies are to be used to match local or regional funds for these transportation projects. TRIP projects are eligible under Florida's State-funded SIB account as long as they are matched by a minimum 25% from funds other than SIB.

[39]Official Internet Site of the Florida Legislature, n.d.

3.3 Investment Strategy

Each SIB sets evaluation criteria for the selection and prioritization of projects. This selection process can include some form of risk assessment. However, this varies from SIB-to-SIB, ranging from modest to thorough due diligence reviews. As shown in Figure 1 below, criteria for the selection of recipients may be categorized as (i) mandatory or threshold criteria and (ii) ranking or discretionary criteria.[40] All States apply the first category, as this refers to the requirements of Federal legislation. The second category refers to additional selection criteria, which are typically tailored to the State's needs and priorities.

Figure 4. Selection and Evaluation Criteria



Florida has been identified by the FHWA as one of the best practice examples of project selection criteria, which include:

- Higher present value of repayments
- Security of repayment stream
- High level of financial feasibility
- Creation and enhancement of economic benefits
- Acceleration of project completion (i.e., likelihood that assistance would enable the project to proceed at an earlier date than would otherwise be possible)
- Promotion of innovative public-private partnerships and ability to attract private debt or equity investment
- Use of new technologies that increase efficiency in project operation (i.e., intelligent transportation systems)
- Protection of the environment
- Demonstrated benefits for intermodalism, cargo and freight movement, and safety
- Projects using the SIB loan as a smaller percent of the overall project costs, with a focus on local and private participation
- Safety improvements.

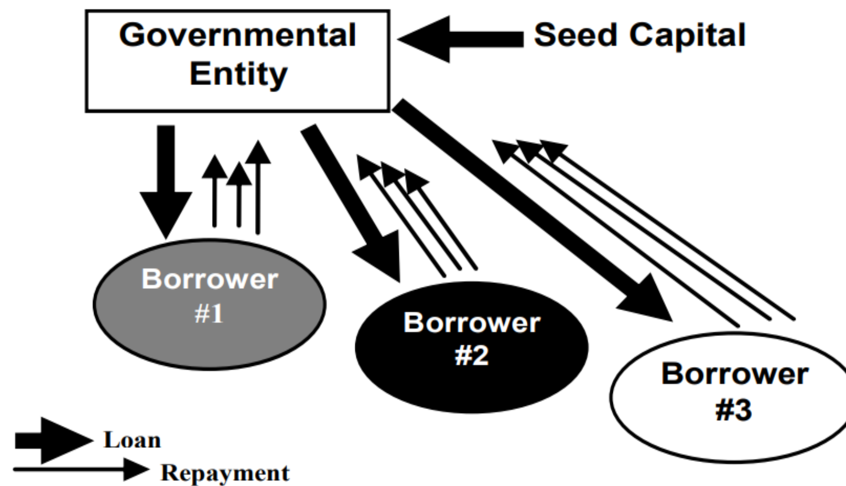
3.4 Financial Products

Similar to private banks, SIBs can provide public and private sponsors with a wide variety of loans and credit assistance enhancement products. As illustrated in Figure 2, one of the major advantages of providing loans or other forms of credit assistance to project is that their repayments are recycled for subsequent projects,

[40] U.S. Department of Transportation Federal Highway Administration, 2002.

advancing the development of infrastructure projects. Because of this, SIBs serve as a flexible and useful tool in meeting a state's transportation project financing needs, maximizing Federal and state dollars.[41]

Figure 5. State Infrastructure Bank Capital Flow (Source: USDOT)



The Florida SIB can provide loans and credit enhancements (described in section 1.4.1. below). The Bank's assistance may be used for refinancing. However, to date, it has not participated in any refinancing.[42] State legislation was approved in 2003 allowing FDOT to issue revenue bonds in order to leverage the State SIB loan portfolio repayment stream.[43]

3.4.1 Loans and credit enhancements

According to the FHWA, loans are the most typical form of assistance provided by SIBs.[44] Five states, including Florida, account for about 90% of the total dollar amount of all SIB loans.[45] Loan terms specific to the Florida SIB are outlined below[46]:

- **Pricing / Interest rate:** At or below market interest rates, "based on market conditions, the financial strength of borrower, term, loan, and other systemic risks".[47]
- **Loan terms:** The loan may use a grace period, allowing repayments to be deferred up to 5 years following project completion or the opening of the road to traffic, in the case of highway projects (whichever is later). The maximum loan maturity allowed, including deferrals, is 35 years (for Federally funded SIB projects) or 30 years (for state-funded SIB projects).
- **Minimum loan size:** The minimum loan amount is $1 million, with FDOT occasionally making exemptions for small or one-of-a-kind projects.[48]
- **Loan seniority:** The SIB loan amount may be subordinated to senior project debt with at minimum an investment grade rating (BBB or higher).[49]

---

[41] AASHTO Center for Excellence, n.d.
[42] U.S. Department of Transportation Federal Transit Administration, 2005.
[43] U.S. Department of Transportation Federal Transit Administration, 2005.
[44] U.S. Department of Transportation Federal Highway Administration, 2002.
[45] AASHTO Center for Excellence, n.d.
[46] FHWA Center for Innovative Finance Support , n.d.
[47] FHWA Center for Innovative Finance Suppoirt , n.d.
[48] U.S. Department of Transportation Federal Transit Administration, 2005.
[49] U.S. Department of Transportation Federal Transit Administration, 2005.

The majority of Florida's SIB-assisted projects were "production-ready" – meaning the planning and engineering was advanced to the point that, with enough funding, construction could begin within a short period of time. The SIB assistance allowed these projects to accelerate their timelines between one to 15 years.[50] The Florida SIB's flexible financing terms have contributed to the early delivery of transportation projects and/or delivery of projects that may otherwise not have been developed. As previously mentioned, Florida's State-funded account provides additional flexibilities to project sponsors.[51] Most of Florida's SIB activity comes from this account.

3.5 Institutional Framework and Governance Structure

SIBs are established and fully owned by the respective State. While some States have enacted comprehensive legislation creating the institutional framework (i.e., oversight bodies) for the SIB, others were generic and brief in nature.[52]

In the case of Florida, the legislation is relatively general. In terms of governance structure, the main bodies involved can be broadly classified in two groups: administrative and supervising bodies. The former is directly involved in the establishment and operations of the SIB, while the latter takes a role as supervisor.

Administrative bodies

The most common approach is to house the SIB within the State DOT, as is the case of the Florida SIB. However, other approaches include (but are not limited to) the establishment of a special purpose (non-profit) corporation (i.e., Missouri) or the placement of the SIB within another government agency (i.e., Vermont). Additionally, the degree of "formality" under which each SIB operates varies significantly. Some SIBs report having full-time staff members responsible for administrating the SIB, while others assign responsibilities within the existing state DOT staff.

Per the Florida SIB's cooperative agreement, FDOT is the designated agency of the State for the administration of the SIB, with legal, managerial, operational, and technical capabilities.[53]

For the Federally funded SIB account, FDOT is responsible for:

- Providing the non-Federal match equal to at least 25% of the Federal funds provided;
- Entering into written agreements with project recipients and disbursing the funds agreed upon;
- Maintaining fiscal controls and accounting procedures related to payments received and disbursements made through the SIB. This includes providing SIB balances during each accounting period and conducting an annual independent financial and compliance audit of the SIB, which is to be submitted to the FHWA and the FTA; and
- Submitting a biennial report to FHWA and FTA at the end of each Federal fiscal year.

For both SIB accounts, FDOT's role as administrator includes selecting project recipients, maintaining loan underwriting guidelines and monitoring procedures, as well as reviewing borrowers' semi-annual progress reports on the project's financial activities. These activities are conducted by FDOT's SIB manager. For the Federally funded SIB account, the prioritization of projects considers whether these are included in the adopted comprehensive transportation plan of the relevant Metropolitan Planning Organization (MPO) and the Florida Transportation Plan (FTP).[54]

[50] U.S. Department of Transportation Federal Transit Administration, 2005.
[51] U.S. Department of Transportation Federal Transit Administration, 2005.
[52] U.S. Department of Transportation Federal Highway Administration, 2002.
[53] FDOT , n.d.
[54] FDOT, n.d.

FDOT's Office of the Comptroller is the SIB's trustee and is responsible for safeguarding advances from fiscal irresponsibility and enforcing the repayment of advances.[55] Overall, according to Fitch Ratings, FDOT SIB management policies have proved to be robust and "reflected by the fact that the program has not suffered a default to date."[56] FDOT has also been recognized for developing a support and outreach program for the Florida SIB, including state-wide workshops to promote a better understanding of the SIB as a financing mechanism.

Investment Authority

Per the cooperative agreement, the Florida Division of Treasury under the Department of Insurance is designated as the SIB's custodian.[57] As the Florida SIB is established as an escrow account in the Treasury, all proceeds are invested by the Treasury in alignment with the established state investment guidelines.[58] Under the Florida Comprehensive Investment Policy, the Florida Division of Treasury is the designated investment authority. Within the Division of Treasury, investment and operational decisions are made by the Investment Work Group, which includes the Director of the Division. Section 17.575 of the Florida Statutes creates a Treasury Investment Council that reviews the investments and provides recommendations to the Work Group regarding the investment policy and strategy.[59]

Some States have an appointed board or advisory committee (which typically include members external to the DOT) responsible for overseeing the SIB program and approving projects. However, there is no evidence indicating that this is the case for Florida's SIB.[60]

Supervising bodies

FTA and FHWA serve as supervising bodies to the Federally capitalized account and signatories to the cooperative agreement with FDOT. Among their key responsibilities, FTA and FHWA[61] [62]:

- Ensure SIB programs are effectively administered and, when relevant, provide technical assistance to States.
- Make payments to FDOT for deposit in the federally funded SIB account.
- Ensure FDOT compliance with the terms of the cooperative agreement (and defined in TEA-21) and, if necessary, request corrective action.

3.6 Capital Structure

Federally funded SIB account

As previously mentioned, the Federally funded account of the Florida SIB is capitalized with Federal funds and State matching funds (75%/25%), both of which are a critical initial infusion to the start-up of the SIB. To date, the Federally funded account has been capitalized with USD 126 million in Federal dollars, of which approximately USD 11 million are Federal transit funds and USD116 million are Federal highway funds.[63] The Federally-funded account has not been recapitalized since 2004.[64]

State-funded SIB account

The Florida SIB State-funded account is capitalized solely by State funds and net bond proceeds. Historically, the Florida SIB has received strong State support reflected in appropriations. In 2000, the Florida legislature

---

[55] FDOT, n.d.
[56] FitchRatings, 2018.
[57] FDOT, n.d.
[58] FDOT, n.d.
[59] Department of Financial Services, 2021.
[60] U.S. Department of Transportation Federal Highway Administration, 2002.
[61] U.S. Department of Transportation Federal Highway Administration, 2002.
[62] FDOT, n.d.
[63] FHWA Center for Innovative Finance Support , n.d.
[64] Puentes & Thompson, 2012.

approved a transportation funding package that provided USD 150 million to the Florida SIB phased out over a three-year period to satisfy the State's growing transportation demands.[65] Additionally, according to Brookings Institution, as of 2012, state gasoline and excise taxed contributed USD 10 million per year to the State-funded account.[66] As of 2020, the State-funded account has been capitalized with approximately USD 500 million.[67]

Bonds

As mentioned, the Florida DOT is allowed to issue revenue bonds to leverage the State SIB's loan portfolio repayment stream as a consistent source of loan funding.[68] According to State law, revenue bonds can be issued for the purpose of "financing or refinancing the construction, reconstruction, and improvement of projects that are eligible to receive assistance from the State-funded infrastructure bank."[69] The duration of each series of bonds may not exceed 30 annual maturities. To date, two series of SIB bonds have been issued: the first in 2005 for USD 62.3 million and the second in 2007 for USD 61.3 million.[70]

The Florida SIB program bonds have a hybrid structure (cash flow and reserve fund), secured by pledged loan repayments, interest earnings, and reserves.[71] These bonds are issued at a state level and are not General Obligation (GO) bonds; as such they do not represent indebtedness of the State of Florida, nor do they impact the State's credit rating. Bonds are also secured by a debt service reserve account in "an amount equal to the least maximum annual debt service, 125% of average annual debt service, 10% of the par amount of the bonds, or the maximum amount permitted under federal tax laws." The reserve account is funded with cash.[72] According to Fitch Ratings, as of 2018, Florida's SIB recorded a high portfolio concentration, with 10 of its 16 borrowers accounting for almost 90% of the portfolio. Osceola County, the largest borrower, accounts for 16% of the loan portfolio.[73]

3.7 Project Example

The Florida SIB has demonstrated to be a useful mechanism to promote local and private investment in transportation projects. The SIB invested nearly USD 14 million in the construction of the USD 17 million Orchard Pond Parkway – the State's first private toll facility – through a loan to the private developer.[74] The project, located in Tallahassee, encompasses a 5.2-mile toll road connected with a paved bicycle and pedestrian trail. The remaining project costs were covered by the developer, who also "donated scenic easements for the nature trail and bike path."[75] The toll road will be owned by Leon County and operated by the developer (under a lease). Tolls revenues will be used for loan repayment and road maintenance.[76]

3.8 Key Lessons Learned

The following section provides an overview of key lessons learned from structure of the Florida SIB, as well as from SIBs in the United States, in general:

- The concept of revolving funds behind SIBs creates a permanent and relatively stable additional revenue/financing source for local transportation projects.

[65] FHWA Center for Innovative Finance Support, n.d.
[66] Puentes & Thompson, 2012.
[67] FHWA Center for Innovative Finance Support, n.d.
[68] U.S. Department of Transportation Federal Transit Administration, 2005.
[69] Official Internet Site of the Florida Legislature, n.d.
[70] FHWA Center for Innovative Finance Support, n.d.
[71] FitchRatings, 2018.
[72] State of Florida Division of Bond Finance, n.d.
[73] FitchRatings, 2018.
[74] FHWA Center for Innovative Finance Support, n.d.
[75] FHWA Center for Innovative Finance Support, n.d.
[76] FHWA Center for Innovative Finance Support, n.d.

- SIBs can provide flexible project financing terms (i.e., interest rates, repayment schedules, and maturity), which contribute to satisfying the State's transportation needs through early delivery of transportation projects and/or delivery of projects that may otherwise not have been developed.
- In addition to providing attractive loan terms, States have the flexibility to pass legislation enabling their SIBs to issue revenue bonds in order to leverage the State SIB loan portfolio repayment stream, as it the case for Florida.
- Each SIB sets evaluation criteria for the selection of projects, which can be tailored to meet State-specific priorities. In the case of Florida, State legislature outlines a comprehensive set of criteria, ranging from the security of the repayment stream and level of financial feasibility to the protection of the environment and use of innovative technologies.
- SIBs have proven to be a useful mechanism to promote local and private investment in infrastructure projects. In the case of Florida's SIB, the Federally funded and State-funded accounts have leveraged USD 6 in projects for every USD 1 loaned.
- SIBs are established and fully owned by the respective State. Therefore, the robustness of their institutional framework (beyond Federal requirements) varies from State-to-State. SIBs are typically house within the State DOT, which serves as the Bank's administrator. FTA and FHWA serve as oversight and supervisory bodies.[77] [78]
- SIBs operated under the purview of Federal and State legislation. The latter can provide States with the flexibility to tailor the structure of the SIB to meet state-specific needs, as well as to expand their State capitalization programs. For instance, Florida legislature approved a transportation funding package that provided USD 150 million to State-funded SIB account.
- However, the need for State-specific legislation for the implementation of SIBs has resulted in some States (excluding Florida) experiencing protracted legal processes associated with enacting legislation. In some cases, this has severely impacted or fully interrupted the SIB implementation timeline.
- The creation of State-funded account (to complement Federally funded SIB account) is critical in unlocking more flexible loan terms, as these are not required to abide by Federal regulations and restrictions. This is particularly relevant as many States indicated Federal requirements are complex and can impact program effectiveness, particularly by delaying smaller projects (and, in some cases, increasing costs).

[77] U.S. Department of Transportation Federal Highway Administration, 2002.
[78] FDOT, n.d.

4. Kenya: Kenya Innovative Finance Facility for Water (KIFFWA)

4.1 Background and Establishment

Country: Kenya
National: National and sub-national projects
Purpose: Co-developing water infrastructure
Products: Early-stage capital (equity or debt) and technical assistance
Capitalization source: Donor seed funding of USD 11.5M (Netherlands government)

The Kenya Innovative Finance Facility for Water (KIFFWA) is not like any ordinary project preparation facility. KIFFWA takes the position of co-developer of commercial water initiatives in Kenya with potential follow-up financing. KIFFWA supports commercial water initiatives by bringing in early-stage capital and offering expertise that is lacking in early-stage project development: the riskiest stage even for water initiatives with the potential for commercial viability.

The key objectives of KIFFWA are to create more bankable water projects and to draw in more private finance in the water sector. In addition, KIFFWA seeks to enhance the bankability of initiatives of lead developers and support them in mobilizing financing to reach financial close. The KIFFWA investment policy was revised in recent years to enable KIFFWA to also invest in projects at a late development or commercial stage (after financial close), but at this moment in time KIFFWA has not yet implemented this capacity.

KIFFWA was designed by the Netherlands Water Partnership[1] (NWP) and the Embassy of the Kingdom of the Netherlands (EKN) in Kenya in 2016[2]. The EKN aimed to establish and fund an innovative financing facility that does not invest, but funds or finances preparatory work on project engineering and financial engineering and generates investments by third parties. A growth in water sector investments contributes to the attainment of SDGs 6, 9, 12, 13, 14 and to the development aspirations of Kenya inter alia through employment, sustainable agriculture, industrial production, and access to water and sanitation.

KIFFWA's current investment pipeline consists of 14 qualified water and climate impact initiatives across different stages of development, representing a CAPEX value of circa EUR 200 million (from a development budget of EUR 14.2M). In 2021, KIFFWA was selected by the Partnership for Green Growth and the Global Goals (P4G) as global sector winner for SDG 6[3].

4.2 Investment Mandate

The main area of focus for KIFFWA is the development stage that entails identification, feasibility, permits, finance guarantee/ grants and financial close (see Figure 1). Under its current operational model (which not includes actively investing in/financing potential projects), the role of KIFFWA stops at financial close.

[1] The Netherlands Water Partnership (NWP) is a network of around 180 internationally-oriented Dutch organizations working in the water sector. It is also often used as a platform for the roll-out of Dutch-led international development projects in this field.
[2] https://www.netherlandswaterpartnership.com/expertise/finance-water/kiffwa
[3] https://p4gpartnerships.org/netherlands-water-partnership-nwp-kenya-innovative-finance-facility-water-kiffwa

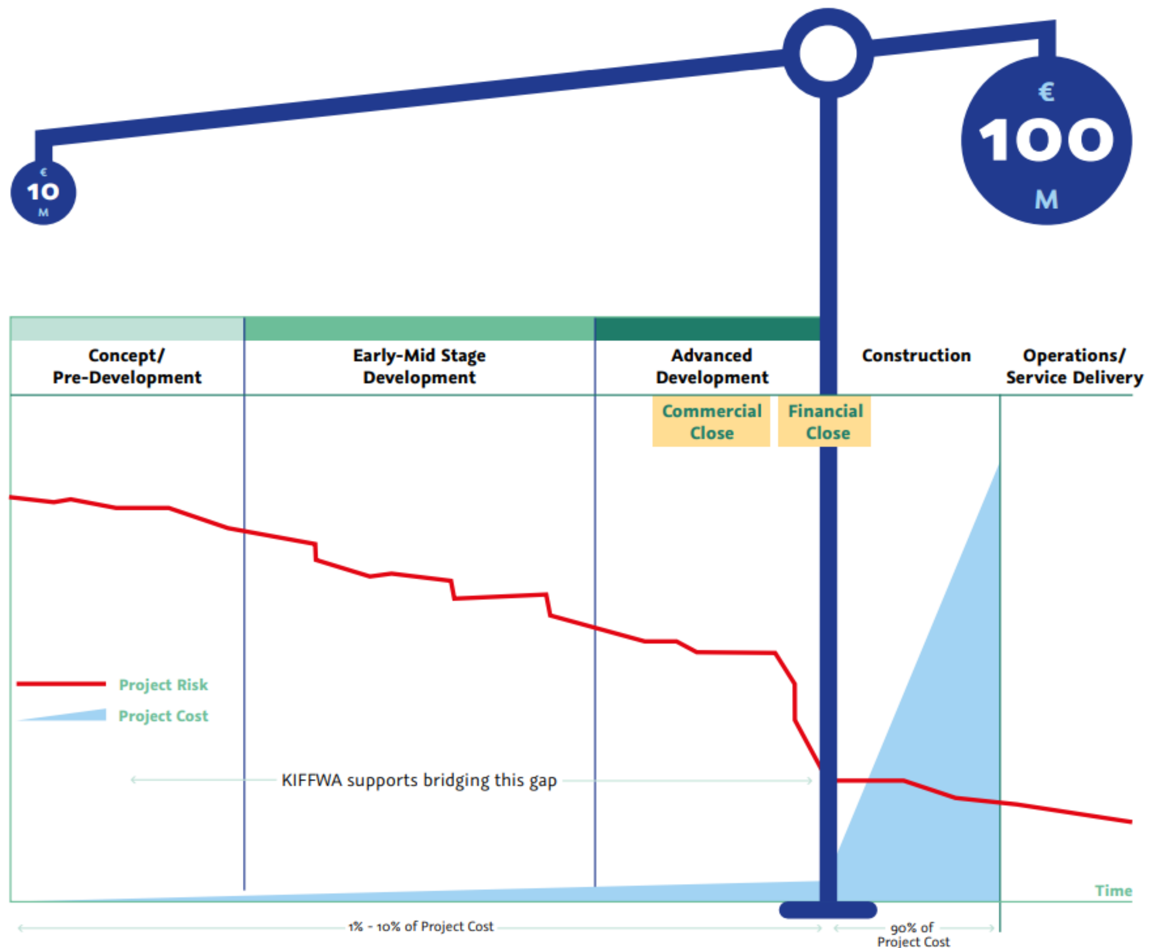
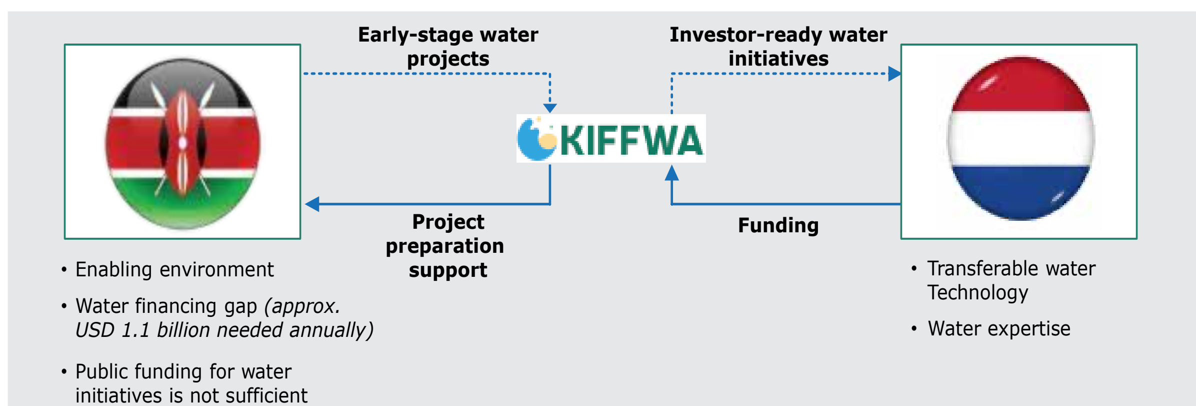


Figure 1. Stages of project development (KIFFWA Public Annual Report 2020)

The graph below provides an overview of the KIFFWA model and the role of the Dutch government in the design of the facility. KIFFWA can provide project preparation support to early-stage water project and get them to the level of being ready for investors. By providing this kind of support KIFFWA seeks to realize benefits on both sides. From the perspective of the Netherlands, KIFFWA seeks to realize benefits by transferring the Netherlands's global expertise in water technologies and knowledge. From the Kenyan perspective, benefits will be realized in closing of investment gap by attracting private institutional capital in the water sector, creation of an enabling environment catalyzing water investment and of course the realization of water related projects.

KIFFWA seeks to become (at least partially) revolving and self-sufficient – in the initial setup by seeking refunding at financial close. Refunding can take the form of a success fee, a loan, mezzanine finance, or an equity stake in the initiative.



4.3 Investment Strategy

KIFFWA takes the role of co-developer role to a lead developer of potentially bankable water projects in Kenya. In its investment structure, KIFFWA provides early-stage capital and financial expertise to support the creation of viable water investment opportunities and attract (private) providers of finance. KIFFWA funds a maximum of 50 percent of the development budget in return for a minority stake in the development SPV. Activities that will be supported or funded by KIFFWA include:

- Capital Expenditure identification and planning;
- Legal Advisory Services;
- Project Management Costs;
- Securing of Easements / Wayleaves;
- Execution of Commercial Agreements;
- Procurement of EPC and O&M Contractors;
- Obtention of permits, licenses, and other approvals;
- Completion and Update of Technical Studies;
- Financial Advisory Services including Transaction Advisory and Fund Raising.

Eligible project types include all kinds of water related projects:

- Ports Irrigation;
- Desalination plants;
- Hydro Power Stations (dams and/or run of river);
- Water Reuse;
- Drinking Water;
- Industrial Water;
- Flood Protection;
- Sanitation & Hygiene;

- Wastewater Treatment;
- Integrated Water Resources Management.

4.4 Financial Products

KIFFWA makes use of convertible grants as their instrument to support developers. If an initiative is a success, KIFFWA will at financial close convert the invested grant amount plus a premium (to be agreed with the lead developer of a project in a Joint Development Agreement).

Applying this framework of convertible grants, the following financial instruments can be used as a recoup mechanism for KIFFWA:

- **An one-off fee:** entitling KIFFWA to be paid the invested amount plus a premium by the developer and/or incoming investors at financial close directly.
- **An equity stake:** providing KIFFWA with a share in the company (SPC) profits of the project which could be sold to other investors to recoup KIFFWA's investments. As KIFFWA will typically have a minority stake the rights and options of KIFFWA would have to be clearly written down in advance (this instrument may not work in case of a public owned initiative).
- **A loan:** entitling KIFWA to be repaid according to the agreed terms and conditions (regarding bullet, annual, interest rate, tenor, subordinate, convertibility etc.). The challenge with this instrument is to acquire collateral as security for the payment of debt service.

4.5 Investment Criteria

Potential projects should typically meet the following requirements:

- All water sub sectors including drinking, irrigation, sanitation and hygiene, hydropower, port, desalination, Integrated Water Resource Management (IWRM) are eligible for support;
- The focus is on early-stage projects that are financially viable and have positive social, economic and environmental impacts;
- The minimum project investment size (CAPEX) should be EUR 2M;
- The contribution of KIFFWA to project development budget is 50 percent (remainder for lead developer) and typically capped at EUR 500K;
- KIFFWA supports activities such as technical studies, legal advisory and structuring support, financial modelling, fundraising;
- Projects must be able to repay KIFFWA at financial close:
    - One off payment with premium;
    - Equity into the project;
    - Loan into the project.

In 2018, the KIFFWA investment mandate was revised to enable KIFFWA to also invest in projects at a late development or commercial stage. Given that project development is a time-consuming activity (can easily take three to four years), this was considered a faster way of creating success stories to further raise the profile of KIFFWA in support of KIFFWA branding activities. Within this revised investment policy, KIFFWA can now

act as an investor in the water sector (supporting development, construction and potentially operations), although the emphasis will for now remain to be on (co)-development of water initiatives. Although the investment mandate was amended, no late development or commercial stage investment activities have materialized.

As described in the revised investment mandate, late development and/or commercial stage projects will be limited to a maximum of 20 percent of the portfolio value, with investments capped at EUR 1 million. As part of implementing this revised investment mandate, KIFFWA is exploring the possibility of establishing a Blended Finance Facility to be able to actively invest in projects also after the financial close phase.

4.6 Institutional Structure & Legal Basis

KIFFWA is set up as a typical PE Investment Fund with an offshore fund (Netherlands) and an onshore manager (Kenya), as well as a Board, IC, KYC Procedures, MEL, & Back Office Services:

- **An off-shore fund:** the KIFFWA Foundation (based in the Netherlands). The Foundation executes the investments and owns the assets represented in those investments.
- **An onshore fund manager:** KIFFWA Limited (company limited by shares based in Kenya). KIFFWA Limited is responsible for investment origination, screening and manages all aspects of the KIFFWA organization.

This structure is legally feasible and ensures tax optimization. It also allows KIFFWA do attract both soft and hard investors - accommodating strategic (capitalization) partners that can only invest in 'for profit' organizations[4].

4.7 Governance Structure

4.7.1 Overview

KIFFWA also has a dual governance structure: the fund and fund manager have separate Boards of Directors. The KIFFWA Stichting Board (fund) and KIFFWA Limited Board (fund manager) are established on distinct foundational levels, with KIFFWA Stichting being a program led board and KIFFWA Limited being a commercially led board.

[4] KIFFWA Annual Report 2017

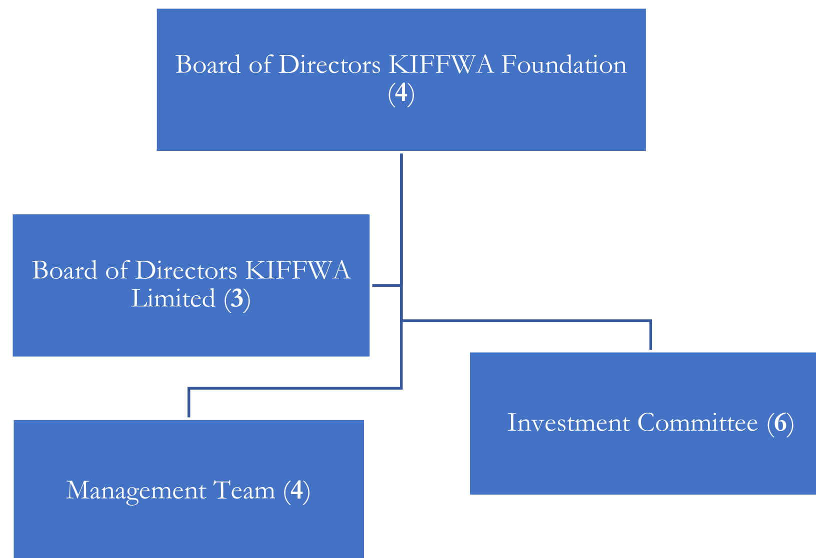


Figure 2. KIFFWA organizational structure (brackets indicate the number of members)

4.7.2 Investment decision making

The fund manager originates and presents propositions (investments or TA advisory) to the Investment Committee (IC). The IC has the mandate to propose projects to the Board of Directors of the fund (Stichting KIFFWA Foundation). In the end, the Board of Directors of the fund approves projects and invest (as the fund ''owns" the actual investments).

4.7.3 Role of government

KIFFWA consciously operates at a certain distance from the government in Kenya. The rationale underlying this decision is the desire to take its own initiative, and work with developers at their own discretion. This also gives KIFFWA the flexibility to move quickly and adapt its structure or policies when and if needed.

Working without explicit government involvement in the operations of KIFFWA has however also proven to be a challenge, as the successful development of many projects in the water sector is dependent on some form of central or local government support and/or approval.

4.8 Capital Structure

KIFFWA is capitalized through donor funding, which it seeks to leverage with other sources of capital.

4.8.1 Donor seed funding

KIFFWA is capitalized with donor seed funding of EUR 10M (USD 11.5M at the time) provided by the Dutch government through their Embassy in Nairobi, Kenya. Of this initial budget of EUR 10M, a 50/50 split was introduced between:

1) spending on operating expenses for the fund and fund manager;
2) project development.

4.8.2 Other sources of capital

KIFFWA seeks to be (partly) revolving by recouping their investments in projects plus a margin to compensate for write-offs at financial close. So far, only one project has reached financial close however and KIFFWA has not yet been able to recoup any of their investments in projects in its portfolio.

The current funding round for the KIFFWA program ends in 2023. KIFFWA together with the Netherlands Embassy in Nairobi is therefore requesting other donors and interested parties to support KIFFWA to ensure its sustainability beyond the current funding period. Initially, there were two options in terms of the scope of fundraising:

1. Creating a Blended Finance Facility of 350M EUR: to (partially) fund project development, operations, and initial CAPEX requirements of the present KIFFWA portfolio and allow for multi-country expansion. This would give KIFFWA the option to work with a fully funded solution and bring the capacity to also lead the financing through to operation or growth of an initiative.
2. Attracting EUR 10-20M additional donor/grant funding: this would simply entail a continuation of the current model with additional resources from different donors than the Netherlands government.

The priority of KIFFWA in terms of fundraising currently lies with the second option – additional resources from donors. Partnerships are also being explored with financiers such as the African Development Bank or Afrixembank.

4.8.3 Minimum capital requirement

The project development process in Africa generally takes long – and the water sector is perhaps even more complex, meaning that it is reasonable to consider a longer period to bring projects successfully to financial close. The experience of KIFFWA so far is that its operations have resulted in very limited returns on its investments in the first 5 years. In terms of minimum capital requirements, this implies that the originally agreed EUR 10M (USD 11.5M) capitalization of the fund is not sufficient to cover both operational expenditures and investments. It is important to note that KIFFWA only targets an infrastructure sub-sector.

The set-up and capitalization of KIFFWA has been inspired by facilities such as InfraCo Africa - a publicly financed and privately managed developer of greenfield infrastructure projects. The box below provides information on this facility.

InfraCo Africa provides funding and expertise to infrastructure projects on the African continent, enabling them to grow from an initial concept to a bankable investment opportunity. InfraCo Africa works with projects at their earliest stage, either directly where they already have an experienced lead developer, or in providing on-the-ground project development expertise through their own teams. It can also provide equity to fund the construction of pioneering projects or for innovative infrastructure businesses that need to scale-up or demonstrate commercial viability to attract further investment.

InfraCo Africa is part of the Private Infrastructure Development Group (PIDG): it is managed as a private

Box 1. InfraCo Africa.

4.9 Project Example

Purefresh is a Kenyan start-up supplying vending points for the sale of safe and clean water. The company closed its funding round (relatively small - raising USD 1M from European impact investors) for a first phase of expansion, enabling it to grow from a pilot area to sites across four counties. The project concept involves the use of a commercial borehole to purify water, using advanced (reverse osmosis) technology and then distribution of the water via bowsers to water kiosks where it is sold at an affordable price. KIFFWA has

supported the business since 2019 and has been instrumental in Purefresh being able to close this round through funding support, technical expertise, and support on governance (financing a feasibility study for expansion and supporting in business planning and fundraising for example).

KIFFWA is currently exploring the possibility of supporting the next phase of Pure Fresh's expansion strategy[5]. This would include expanding operations to five more counties and launching a mobile application so customers can order and pay for water from kiosk operators online.

Four other initiatives have also been prioritized by KIFFWA for financial close in the next 12 months.

4.10 Key Lessons Learned

- KIFFWA was designed and funded by the Netherlands Water Partnership (NWP) and the Embassy of the Kingdom of the Netherlands (EKN) in Kenya in 2016. Other donors and financiers have been invited to co-invest in KIFFWA, but none have committed thus far.
- KIFFWA as a facility aims to enhance the bankability of initiatives of lead developers and support them in mobilizing financing to reach financial close.
- KIFFWA does not (yet) actively invest itself in potential projects, but funds or finances preparatory work on project engineering and financial engineering and generates investments by third parties.
- KIFFWA seeks to become (at least partially) revolving and self-sufficient – in the initial setup by seeking refunding at financial close. Refunding can take the form of a success fee, a loan, mezzanine finance, or an equity stake in the initiative.
- KIFFWA has a minimum project investment size (CAPEX) of EUR 2M and the contribution to project development budget is maximum 50 percent (remainder for lead developer) and typically capped at EUR 500K.
- KIFFWA's investment policy was revised in later years to enable KIFFWA to also invest in projects at a late development or commercial stage – this allows KIFFWA to stay in during construction and operating phases and to exit at an opportune moment.
- Late development and/or commercial stage projects will be limited to a maximum of 20 percent of the portfolio value, however investments are capped at EUR 1M, which provides KIFFWA with limited gunpowder to make any meaningful investments at that stage.
- To carry out its activities, KIFFWA has the typical structure of an investment fund, consisting of two institutions: an off-shore Fund: Stichting KIFFWA Foundation (in the Netherlands) and an onshore Fund Manager: KIFFWA Company Limited by Shares (based in Kenya). It has a dual governance structure. The fund and the fund manager/advisor have separate Boards.
- Due to structural deficiencies in the water sector in Kenya such as over-reliance on the government to provide water services and donor funding related market distortion, it has been difficult to attract private investment and participation in the water sector compared with other sectors such as telecommunication or energy.
- KIFFWA addresses this weakness in the water market in Kenya: there is a lack of support in the project development phase and there is potential added value in financial structuring and attracting (private) finance. KIFFWA has however not (yet) demonstrated that the current model is the best model to resolve this problem.

---

[5] https://impactalpha.com/how-pre-development-financing-is-building-a-pipeline-of-water-projects-in-kenya/

- KIFFWA only reached its first financial close on a project in 2020 – and the size of the project was relatively small.
- In 2020, the 17 projects under development represented approximately EUR 19M of project development (inclusive of the KIFFWA contribution) and if all were to reach financial close would be expected to attract EUR 267M in capital investment. This means KIFFWA would have a potential leverage of 1:14 on private finance.

5. India: Odisha Urban Infrastructure Development Fund (OUIDF)

5.1 Background and Establishment

Country: India
Sub-national: State of Odisha
Purpose: Financing of state urban infrastructure projects.
Products: Loans, grants, technical assistance.
Capitalization source: Primarily loans from KfW (German development bank) with some local government budget.

The State of Odisha is one of the least urbanized states in India but in 2001-2011, it outpaced the national average of the country in terms of urban population growth. At the same time, municipal financing in the state was considered weak, with the state Government of Odisha primarily funding infrastructure projects through its budget and through grants. Whereas the local infrastructure planning and development functions were devolved to over a hundred Urban Local Bodies (ULBs)[1] in the state, funding of projects was historically heavily reliant on the state government.

It is against this backdrop that the Odisha Urban Infrastructure Development Fund (OUIDF) was established. The idea to create the OUIDF was borne out of a financial cooperation agreement between the Government of Germany and the Government of India for the "financing of urban infrastructure projects with positive effects on the environment." In 2013, the OUIDF was formed as a Trust under the Housing and Urban Development Department of the state Government of Odisha. The purpose of the OUIDF is to provide financial and technical assistance to aid in the development of ULB projects, by "progressively increasing the external financing of ULB-level capital projects in a sustainable manner and in a non-guarantee mode." The OUIDF will enable this through:

1) Catalyzing the development of well-structured and bankable projects;
2) Capacity building for project conceptualization, development and implementation; and
3) Facilitating state and ULB-level reforms that can be precursors for further investments.

The funding of OUIDF, since its establishment, has come primarily from loans from the German Development Bank KfW.

5.2 Investment Mandate

To ensure planned and inclusive infrastructure development of urban Local Bodies / Cities / Towns in to livable, economically vibrant and productive, sustainable an efficient entities with provision of adequate and durable public infrastructure and amenities, including affordable housing and livelihood opportunities for all sections of the society and bringing out efficiency in the service delivery mechanisms, community participation and accountability of urban local bodies and parastatal agencies towards citizens, in convergent manner.

The objectives of the OUIDF are:

- **Financial assistance** to ULBs, Statutory Boards, Public Sector Undertakings and Private Investors, for implementing urban infrastructure projects with positive environmental impact in the State of Odisha;
- **Financing** of infrastructure projects sponsored by private investors on a commercial basis when the infrastructure projects are considered strategically important;

[1] Local bodies that administer a city, town, or a specified locality.

- **Invest in infrastructure** projects that have a positive environmental impact, positive impact on climate change and no negative social impact;
- **Mobilize financial resources** (including private and capital market) to finance urban infrastructure development;
- **Institutional building** by strengthening the financial responsibility, project planning, financing, implementing capacities of the participating ULBs/ Statutory Bodies/Planning/ Development Authorities and to become financially self-sustainable.

5.3 Investment Strategy

The OUIDF primarily supports projects that are included in the city development plan or master plan of ULBs, however, exceptions can be made for projects for which a detailed project report[2] is prepared to the satisfaction of the OUIDF.

Primary investment focus: The OUIDF supports investments in the following core sectors:

- **Water** supply and water supply improvement schemes
- **Sanitation** underground sewerage schemes
- **Solid waste management** (including landfill sites, waste-to-energy, segregation, recycling and reuse, larger compost yards/dump areas)
- **Climate adaptation** measures (e.g. storm water and flood drains)
- **Basic urban infrastructure services** in slums
- **Rehabilitation and resettlement of slums**

Secondary investment focus: It may also provide support to the following sectors (although these are at a lower priority compared to the core sectors, based on the loan agreement with KfW):

- **Energy efficiency** projects including energy efficient street lighting
- **Effluent treatment plants**
- **Bio medical waste management**
- **Infrastructure** Roads, bridges, roads over bridges, underpasses
- **Traffic improvement schemes** including junction improvements, traffic control systems
- **Urban transportation** projects including bus terminals, multi-level parking lots, bus shelters, improvement of urban transportation facilities such as Bus Rapid Transit System, Mass Rapid Transit System etc.
- **Reclamation/ preservation of water bodies**, river front development
- **Food processing**, slaughter house/ modern fish market
- **Electric crematorium**

[2] Specific criteria for a satisfactory detailed project report are identified by the OUIDF.

- **Market complexes** to regularize unauthorized hawking

5.4 Financial Products

The OUIDF has three financial products (sub-funds) for investing in projects:

1. **Urban Loan Fund** for debt financing of infrastructure projects;
2. **Grant Support Fund (Viability Gap Fund)** for economically viable but financially unviable projects;
3. **Project Development Fund** (separately financed by a TA budget) to aid in the early stages of the project development process.

A particular focus is given to this "upstream" investment approach by the OUIDF through project development assistance and capacity building initiatives to ULBs. While this is not a financial product that is invested directly into financing the project, the OUIDF makes this a priority, setting aside resources and utilizing their Project Development Agency to focus on this area.

The aim is to catalyze the development of well-prepared and bankable projects that have a high likelihood of attracting sufficient investment to come into fruition.

5.4.1 Urban Loan Fund (Loans)

OUIDF is predominantly set up for lending purposes. It offers a unique value proposition by offering long-tenor, concessional loans which fit the requirements of infrastructure projects. Loans are available to both public as well as private sector entities.

- **Tenor:** Up to 20 years, but repayment period should not exceed 85% of the life of the asset. OUIDF may cash sweep 75% of borrower's net cash balance after operating expenses and debt servicing.
- **Interest rate:** Fixed simple interest rate linked to average yield of 10-year government security on the primary market within the last 6 months + 100 bps. If principal and interest on loan are repaid timely, a rebate of 100 bps will be provided.
- **Collateral/security:** All machinery and equipment and mortgage of property acquired for purposes of implementing the project. In addition, the Housing and Urban Development Department of Odisha (HUDD) shall provide OUIDF with a Letter of Comfort which states that if the borrower defaults, HUDD will cover what it owes to OUIDF and adjust this amount against any other grant or budget/devolution fund due to from the state government to the borrower.

5.4.2 Viability Grant Support Fund (Grants)

Together with loans and depending on the project's specific requirements, the OUIDF may also provide grant funding to make eligible projects financially viable.

5.4.3 Project Development Fund (Technical Assistance / Capacity Building)

The OUIDF provides support for the following activities through the Project Development Fund:

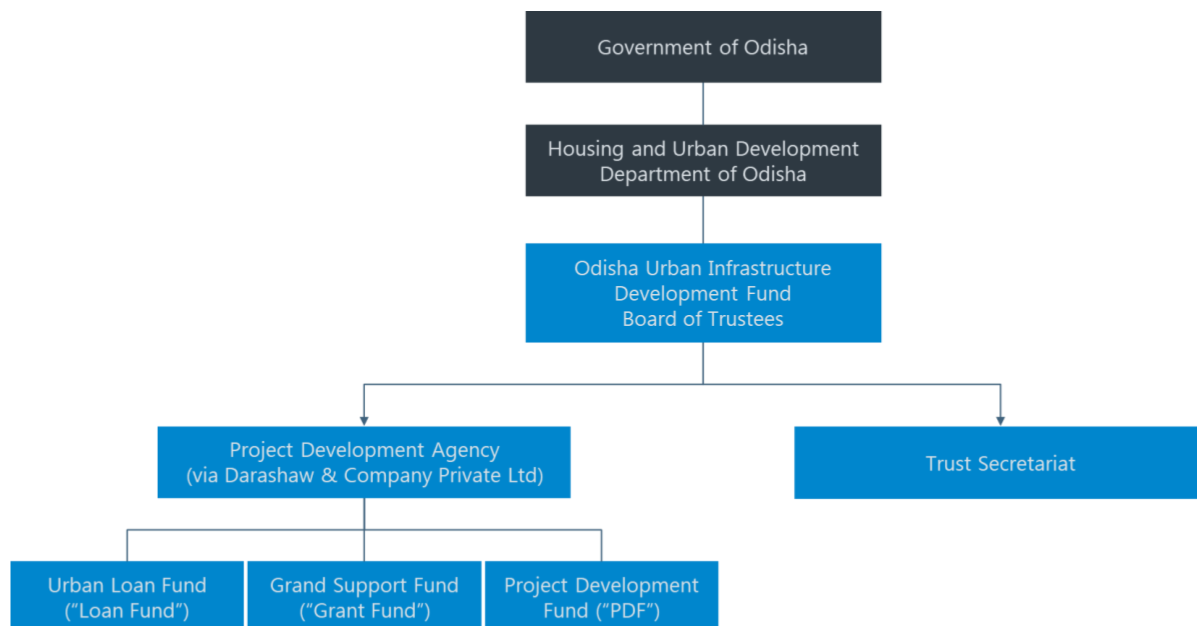
- Preparation of City Development Plans/ Master Plans
- Feasibility studies
- Detailed Project Report/ Bankable project report
- Preparation of tender documents with technical specifications and working drawings
- Proof checking of designs/ drawings
- Procurement services/ Transaction Advisory services

- Construction supervision/ project management
- Project monitoring/ Audit services
- Capacity Building of OUIDF/ Asset Management Company
- Development of Environmental, Social and Climate Change Framework
- Development of innovative financial products
- Capacity building of ULBs, statutory boards, development authorities, regional improvement trusts, special planning authorities involving training, establishing systems and processes, IT enabled solutions, GIS etc.

5.5 Institutional Structure

The OUIDF is 100% government-owned but with financing primarily through long-tenor loans of the Government of India from the KfW and with some unremunerated equity (i.e., no cash will flow back to the shareholder) from the Government of Odisha.

5.6 Governance Structure



5.6.1 Housing and Urban Development Department

The OUIDF was created as a trust under the Housing and Urban Development Department (HUDD) of Odisha, the government agency of the state Government of Odisha tasked to ensure the organized, planned and sustainable growth of cities and towns in Odisha. The HUDD manages over 100 Urban Local ULBs in the state of Odisha. The ULBs are categorized into multiple types of public entities, including municipalities, development authorities, planning authorities, among others, all of which are responsible for the urban development and infrastructure planning of the state. The ULBs under the jurisdiction of the HUDD are effectively the clients of the OUIDF.

5.6.2 OUIDF Board of Trustees

The Board of Trustees of OUIDF report to the HUDD, although the Board defines the charter and disbursement guidelines of the funds under the trust. The Board is comprised of members who have been nominated by the Government of Odisha. Five out of seven Board Members are government officials in the state of Odisha.

- Chief Secretary of Odisha – Chairperson
- Development Commissioner & Additional Chief Secretary – Trustee
- Principal Secretary to Government, Finance Department – Trustee
- Principal Secretary to Government, HUDD – Trustee
- Chairman/Managing Director Industrial Infrastructure Development Corporation – Trustee
- 2 Independent Trustees

The Board of Trustees is responsible for formulating guidelines that define how financial assistance (i.e., credit approvals) will be made, entering into a fund management agreement with a fund manager and delegating fund management powers to such, monitoring the operations of such manager, and monitoring the performance of the Trust.

5.6.3 Trust Secretariat

The Trust Secretariat is led by the Board of Trustees Secretary and CEO of OUIDF and is responsible for providing strategic direction and monitoring the day-to-day operations of the Trust.

5.6.4 Project Development Agency

The Project Development Agency is responsible for project identification, development, appraisal, disbursement, follow-up, and monitoring of the projects of OUIDF. It assists the Board of Trustees in managing the three funds under the OUIDF Trust. The role of fund manager was awarded through a competitive bidding to Darashaw & Company Private Limited, a private consultancy and fund manager. Darashaw thus manages all three funds and executes the funds' investment policies. It oversees project development, loan and grant appraisal and disbursements, project monitoring, collection of loan and interest repayments, fundraising and treasury management, and supports the Government of Odisha in its capacity building efforts for the OUIDF's clients.

5.7 Investment Process / Investment Decision Making

The OUIDF maintains a two-step screening process for loan and grant applications and assesses both the borrower's financial standing as well as the project itself. The principles for screening are summarized below:

	Project	**Borrower**
Initial Appraisal	• Sector eligibility given lending policy • Satisfactory project rationale • Key financial metrics met (including DSCR, debt/equity ratio, FIRR, EIRR) • Environmental, Social and Climate Change Impact • Adherence to credit policy of OUIDF	• Creditworthiness of borrower including: DSCR, debt/equity ratio, collection efficiency or revenue/expenditure ratio, FIRR/EIRR, net worth
Detailed Appraisal	All detailed project material to be assessed: including technical appraisal (e.g., demand projections, project design, costing, site acquisition), work schedule, approvals and clearances, ESG framework, land acquisition, financial and economic analysis, implementation plan, etc.	Detailed creditworthiness check of the last three years financial data of the borrower

The OUIDF maintains the following investment requirements:

- Maximum 50% of the cost of one project may be financed out of Viability Grant Support Fund. In exceptional cases this may go up to 70% depending on the viability of the project.
- Not more than 20% of the Urban Loan Fund of OUIDF will be lent to a single project.
- Minimum 10% of the project cost of each project should be borne by the implementing agency in government sector;
- In case of private sector project, promoter's contribution for a project excluding grant shall not be less than 25% of the project cost
- OUIDF shall also provide short term bridge financing for projects implemented by Government sector
- The floor level for availing ULF is INR 10 lakhs

Investment requirements can be regarded as in-line to common market practices.

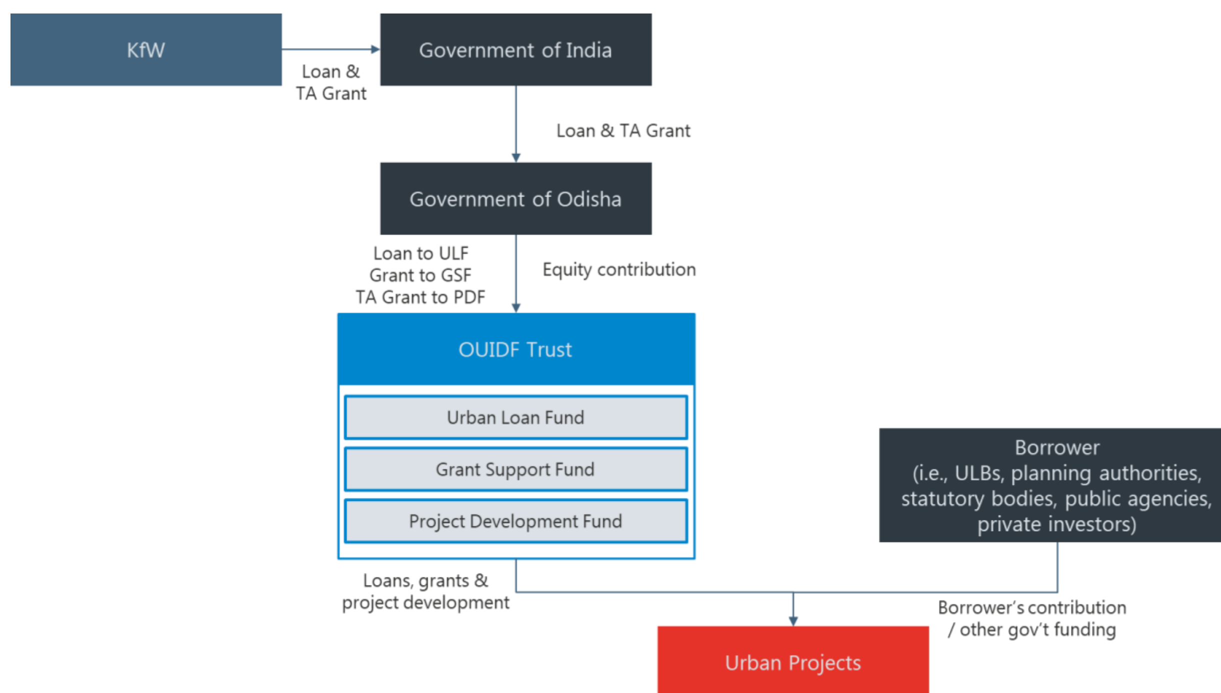
5.8 Legal Basis

The legal framework for the urban sector is provided by the Odisha Municipal Corporations Act, 2003 which applies to Municipal Corporations and the Odisha Municipal Act, 1950 for the Municipalities and the NACs. Following these acts, ULBs need to play a major role in mobilizing resources for infrastructure development in cities, which led to the decision for the incorporation of the OUIDF, with support of KfW. More specifically, the Government of Odisha defined the objectives of the OUIDF to be as follows:

1. **Financial Assistance to local government bodies:** To give financial and other assistance to Urban Local Bodies, Statutory Boards and Departments, Public Sector Undertakings and Private Investors or setting up infrastructure projects in the State of Odisha as per the guidelines issued by the Trust. The ultimate goal of the trust is to become financially self-sustainable and facilitate debt financing of Urban Infrastructure Projects in Odisha in a Non-guaranteed mode;
2. **Mobilize capital resources:** To borrow or raise moneys or loans or receive grants or accept contributions for the above purpose in such manner and on such terms, conditions and securities as the Board of Trustees in their discretion deem fit from time to time;
3. **Payment guarantees:** To guarantee the performance of any contract or obligations and the payment or money or dividends and interest on any stocks, shares or securities of any company, corporation, firms or person in any case in which such guarantee may be considered directly or indirectly to further the main objects of the Trust;
4. **Provide investment:** To subscribe for, underwrite, acquire, hold and dispose of shares, stocks, debentures, debenture stocks, bonds, mortgages, obligations and securities of whatever nature and industry, Government, Trust, Municipal, Local Authority or Body.

5.9 Capital Structure

The OUIDF is 100% owned by the Government of Odisha. However, its financing thus far has been sourced largely through (sovereign) loans and grants from the KfW to the (national) Government of India, which are assigned to the Government of Odisha and then contributed into the OUIDF Trust. In addition to the KfW loans and grants, the Government of Odisha has also put in equity into the OUIDF Trust.



Summary of Capital Infusion Into OUIDF

Loan Date	KfW Loan (mn Euro)	Gov't of Odisha Equity	KfW TA / Grant	Gov't of Odisha Equity	Total	Fixed interest rate[3]	Repayment period
2012	50	5	2.5	0.5	**58**	1.79%	21 years with 5-year moratorium
2017	55	5	2	0.5	**62.5**	1.40%	10 years with 5-year moratorium

While the current sources of financing of the OUIDF are limited to the loans from KfW and unremunerated equity from the Government of Odisha, the OUIDF has the mandate to explore other avenues of external financing (e.g., bonds, loans from other investors, and private investments).

More specifically, the support of multi / bilateral financing is found to have provided the following benefits:

- Access to fixed, low interest long-term funds and technical assistance providing budget and time to build expertise in implementing "Bankable Projects".
- Leveraging Government interventions and available subsidies under various Programmes thereby contributing to highest economy of scale in operations of feasible Projects. a Introducing ULBs to the rigour of Debt Servicing discipline leading to gradual reduction of dependence on budgetary support. a Procurement adopting International Guidelines of Multilateral Agencies. a Greater scope for private

[3] Excludes exchange rate risk

sector participation in asset creation and service delivery. a Capacity Building of ULBs through professional support out of various Technical Assistance Grant.

5.10 Project Examples

Between 2018 and 2020, some projects that received financing from the OUIDF include: the reclamation and development of 34 water bodies in 8 ULBs, energy efficient LED street lighting in new roads across 113 ULBs (30 geographic districts), and the development of an inter-state bus terminal at one of the major tourist destinations within the State of Odisha. Other projects which have received loans from OUIDF include several sewerage systems in various geographic districts, bulk water supply projects, and a municipal solid waste management project.

5.11 Key Lessons Learned

- OUIDF is capitalized primarily through KfW loans and secondarily through equity from the State Government of Odisha, but has the mandate to mobilize other sources of capital, for example through issuance of bonds or through private investments
- OUIDF was created and established by the State Government of Odisha and placed under the purview of the Housing and Urban Development Department of the state government. While the creation of the OUIDF was an outcome of a financial cooperation agreement between the (national) Government of India and the Government of Germany, the national government does not play any supervisory or policy role in the operation of OUIDF
- OUIDF is managed by a private fund manager, while its policy direction and supervision are provided by the (public) Board of Trustees and Trust Secretariat. This allows the OUIDF to utilize private fund management expertise while keeping the overall direction of the Trust within public sector control
- The Project Development Fund allows OUIDF to invest "upstream" (i.e., in activities which help create more bankable projects in the long-term). Emphasis is given to capacity building and ensuring that the clients of OUIDF (i.e., ULBs and other agencies involved in infrastructure delivery) receive sufficient knowledge transfer, thereby improving the overall ability of these state actors to develop and finance infrastructure projects
- Given the range of projects across sectors and geographic locations that OUIDF has been able to finance since its establishment, OUIDF can be considered a successful case for supporting the devolution of infrastructure development to local units

6. Philippines: Green Green Green Fund

6.1 Background and Establishment

The Local Government Support Fund - Assistances to Cities or better known as the "Green Green Green" Fund is a program with US$50 million in annual allocation for green and public open spaces. The fund was launched in 2018 which was initially available to any of the 145 Philippines' towns with city status. [1]

The fund ran from 2018 to 2021 managed by a special unit under the Department of Budget Management, which is a Philippine ministry at the national level tasked to efficiently manage government resources.

Country: Philippines
Sub-national: Cities (Local Government Units)
Purpose: Financing of green infrastructure at the local government level
Products: Grants
Capitalization source: National budget

The fund was launched to provide a parallel program at the sub-national level to the "Build Build Build" program at the national level. [2] This was intended to promote green infrastructure at the municipal-level and addressed two critical issues:

- The lack of green public spaces in cities, particularly urban areas in the Philippines, which are typically car-centric
- Limited prioritization of local funding for green infrastructure

The "Green Green Green" Fund was a mixed success and there are important lessons for practitioners setting up similar facilities. While it has some notable early successes such as providing funding to Pasig City, one of the component cities of Metro Manila, to transform its public infrastructure to support active transport, it also struggled to institutionalize and by 2021, fund utilization had significantly declined from an initial 95% utilization rate in its first year of availability. [3]

6.2 Investment Mandate and Strategy

Policy goals and objectives

The fund's investments were expected to contribute to policy goals and objectives [4]:

- National Greening Program, which is the Philippines' flagship reforestation program;
- Promotion of adequate networks of public open spaces according to the National Urban Development and Housing Framework, the Philippines unified framework for urban development and housing;
- United Nations Sustainable Development Goals (UN SDG) 11 on sustainable cities and communities).

Eligible Projects

The Green Green Green Fund was intend to fund projects that conformed to the following principles [4]:

- Designing for the environment including respecting and harnessing attributes of the existing development; preserving; improving, and adding green and/or blue infrastructure to increase climate resilience, and minimize, and
- Designing for people including ensuring inclusive mobility and usability of public open space.

In practice, these could include green spaces, public parks and gardens, streetscape transformation such as eco-friendly furniture and fixtures, construction of bike lanes and walkways, and green infrastructure enhancements such as *bioswales*.

The Green Green Green Fund could only be used for capital expenditures, and there were specific carve-outs on costs that were not eligible for funding:

- *Payment of personnel services and operational expenditures.* Municipalities were expected to provide co-funding for projects through operational expenditures and personnel.
- *Consulting fees for project development.* To obtain Green Green Green Fund grants, the city was required to provide concept plans and cost estimates as well as input from landscape architects from its own budget. Funding for consultants to help in this process was not eligible for reimbursement.
- *Acquisition, reclamation, or lease of land.* Projects had to be within sites already owned or controlled by the city.

6.3 Products and Offerings

6.3.1 Capital grants

Assistance from the "Green Green Green Fund" were capital grants to the local governments that were structured as trusts. When structured as trusts, funding has to be used for the specific purpose set out for the Green Green Green Fund any portion that was unutilized for its intended purpose would be returned back to the national treasury. It is important to note that these capital grants were not awarded on a competitive basis but rather based on a set allocation to the 145 cities. All the cities had an allocated amount which was set every year – and all the cities had to do was to submit a proposal that was compliant with requirements. Despite this, uptake was not consistent and sharply declined. From an initial utilization of 95% when the program started in 2018, utilization slowly dropped from 60-70% in 2019 and 40-50% in 2020 [3] despite roughly the same budget of roughly US$ 50 million equivalent being available. This demonstrates that capital availability was not actually the primary bottleneck for the deployment of green infrastructure.

6.3.2 Capacity-building

Capacity-building was also initially provided to beneficiary cities. Technical workshops were launched where urban planners were invited to speak about the benefits of green infrastructure and tours for city officials were organized to see local best practices in green spaces. However, resources for capacity-building were reduced after the initial year – which also coincided with reduced uptake in capital grants. This was cited as a possible factor for reduced uptake in the capital grants. [3] This was especially a factor given the lack of priority and familiarity with green infrastructure and public open spaces in the Philippines.

6.4 Institutional and Governance Structure

The Green Green Green Fund was housed as special program directly under the Secretary of the Department of Budget and Management. The program was led by with DBM Assistance to Cities Program Manager, Julia Nebrija.87 This was supported by a small technical review unit, composed of landscape architects and urban planners/designers. Aside from reviewing for compliance, the technical review unit also provided suggestions on design on how they could better align with the objectives of the Green Green Green Fund. This includes

[87] https://dbm.gov.ph/index.php/secretary-s-corner/press-releases/list-of-press-releases/766-dbm-launches-green-green-green-city-public-open-spaces-assistance-program

for example ensuring improved accessibility in cycling infrastructure. A monitoring and evaluation team was planned but also never materialized. [3]

As key officials who supported the Green Green Green program in the Department of Budget and Management moved to other roles and government programs, the Green Green Green Fund was never institutionalized and ended in 2021 with the technical review unit eventually dissolved.

6.5 Legal Basis

The legal basis for the Green Green Green fund was a special provision for a Local Government Support Fund under the General Appropriations Act to provide special assistance to local governments to fund and construct open spaces. This had to be renewed every year in line with congressional approval. To implement the fund, the Department of Budget and Management issued a series of circulars originally in 2018, and subsequently in 2019 and 2020. The circulars covered the following aspects:

- General guidelines on the purpose of the fund
- Prohibitions on the use of funds
- Project implementation to ensure that any disbursement was aligned with the government procurement regulations
- Posting and reporting requirements
- Responsibility and accountability to ensure that they ultimately rested with local governments

6.6 Capital Structure

The funding for the Green Green Green fund was taken from annual appropriations from the national budget which had to be approved and renewed every year. However, at the project-level, there were restrictions on the use of funds to ensure that local governments also provided financial contribution either in terms of land or operational cost. [5] This ensures that local governments have skin-in-the-game for any project funding requested.

6.7 Project Example

As a capital grant facility, the Green Green Green fund can provide catalytic early stage funding to programs of local governments looking to create green spaces. This was the role of the Green Green Green fund in the transformation of Pasig City, one of the component cities of Metro Manila, into the friendliest city for cyclists in Metro Manila. Funding from the program was used during the early stages of a transformational infrastructure investment plan to create cycling infrastructure to spur the adoption of active transport in the city.

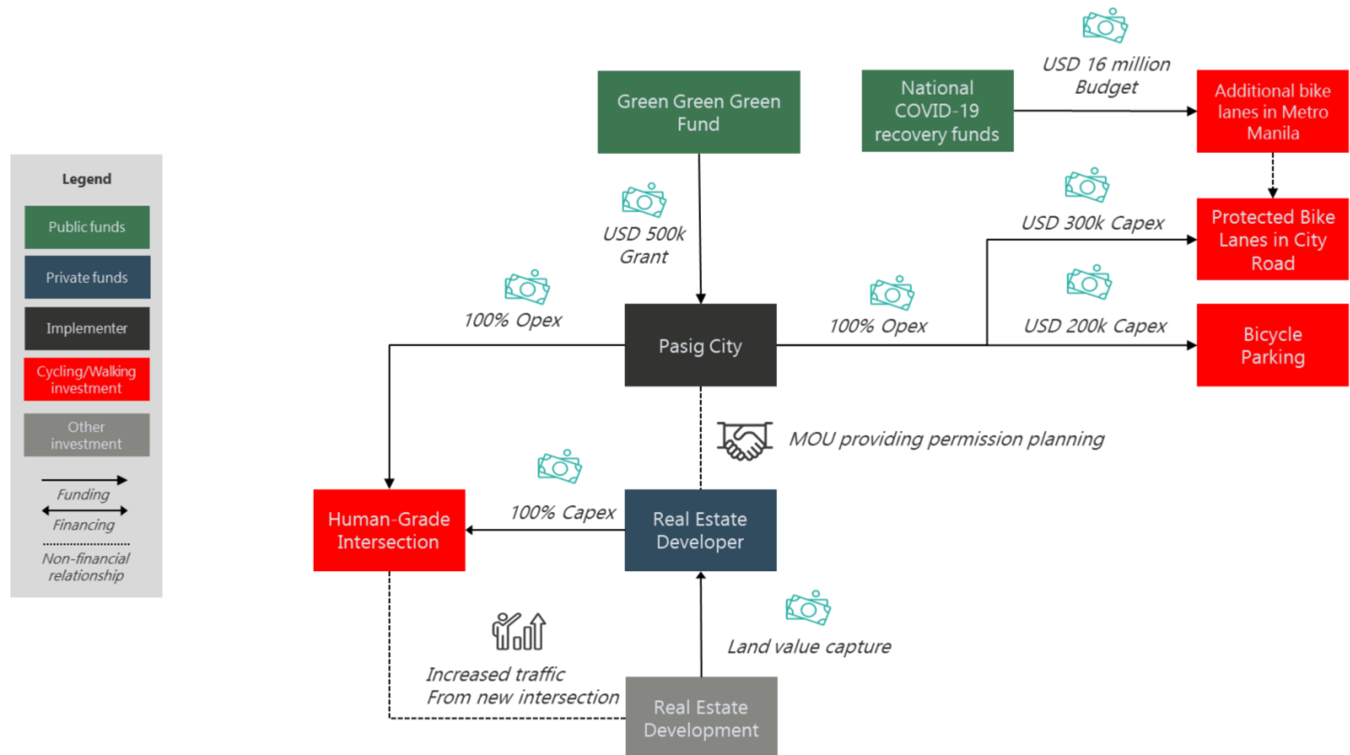


Figure 6 Catalytic funding from Grene Green Green fund to enable cycling infrastructure program (Source: Author's analysis)

Pasig City was able to use USD 500k allocation from the Green Green Green fund to procure and implement 22 kilometres of protected bicycle lanes throughout Pasig City, covering all the major thoroughfares of the central business district in Pasig City. In addition, bicycle parking for 300 bicycles was also procured and initially implemented in government buildings. [6] This was crucial at a time when there was no proven demand for cyclists that would make it difficult to justify any private (or public) investment decision.

The Green Green Green fund actually had a pivotal role in improving project design. While initially the project concept consisted of non-protected bike lanes, to ensure better access, the technical review unit suggested the introduction of protected bike lanes given the observed level of vehicle traffic. Suggestions such as widening of pavements for pedestrians and lighting were also suggested. [3]

After this funding and the initial success of the bicycle lanes where cycling traffic exceeded motorized traffic during peak periods, the successful funding of these project served as a catalyst for further walking & cycling infrastructure. A real estate developer through a PPP with Pasig City developed a cycling and pedestrian-friendly intersection in a major real estate redevelopment in Pasig City. Further, the demonstration project also influenced national government to see the benefits of implementing protected cycling lanes particularly with reduced transport capacity from the impacts of COVID-19 restrictions. The national government invested USD 16 million in cycling, part of which connected Pasig's protected lanes to other areas in the city.

6.8 Key Lessons Learned

The case highlighted several lessons when providing capital funding to local governments:

- Capacity in local government is an important constraint in accessing funding. As the case demonstrated, despite capital availability (even as a non-reimbursable grant), local governments may not always invest in projects despite available funding for capital projects. While extensive capacity-building was budgeted at the launch of the programme including workshops with local governments and efforts government officials to promote green infrastructure, uptake of the programme dropped from 95% in 2018 to less than 50% in 2020 as funding for capacity-building also dropped.

- Support for project development is also crucial in unlocking access to finance. Unfortunately, project development was not eligible for funding under the Green Green Green fund. While certain cities like Pasig City had already a high-levels of capacity for project development, many local governments lack basic project development to develop project concepts to even access grant funding which likely contributed to low utilization of funds for capital projects.

- Ultimately, the largest problem was the lack of institutionalization of the Green Green Green Fund as this was reliant on DBM annually renewing funding through inclusion in the budget and for approval. Initially, there was strong support from leadership from DBM which including funding for the necessary capacity-building and awareness initiatives among the 145 eligible cities. The placement of the 'Green Green Green' fund as a project promoter was arguably not a natural fit with the Department of Budget and When the advocates for the Green Green Green were no longer present at DBM, support was also reduced. Any investment funds or programs should be placed under institutions or agencies where there is mandate alignment.