EUROPEAN INVESTMENT FUND

European Progress Microfinance Facility

European microfinance facility for employment and social inclusion

Microcredit Guarantee

INTRODUCTION

The purpose of this document is to provide some general information about guarantees issued by the European Investment Fund ("EIF") in the framework of the European microfinance facility for employment and social inclusion of the European Community, called European Progress Microfinance Facility ("EPMF"). The first part of this document contains background information on EPMF and the purpose of the guarantees issued by EIF under EPMF ("Guarantees"). The second part provides information on the key terms and conditions of such Guarantees.

I. European Progress Microfinance Facility and Microcredit Guarantees

EPMF was established by the European Parliament and the Council[1] in 2010 in order to

- increase access to, and availability of, microfinance especially for certain at-risk groups, such as unemployed persons, persons at risk of unemployment or social exclusion and vulnerable persons in a disadvantaged position regarding access to the conventional credit market,

- support the development of entrepreneurship activities and micro-enterprises, especially in the social economy and micro-enterprises which employ persons belonging to at-risk groups listed above, and

- promote equal opportunities for women and men.

The EPMF aims at achieving this through an appropriate range of actions including guarantees, risk-sharing, equity and debt instruments.

In July 2010, the European Commission mandated EIF to implement the EPMF on behalf of the European Community through guarantee instruments. Pursuant to this, EIF will issue guarantees and counter-guarantees to public and private bodies (i.e. financial, microfinance or guarantee institutions) established on national, regional, or local levels ("Intermediaries") providing microcredit loans or guarantees on microcredit loans to persons and micro-enterprises established in the EU Member States.

II. THE GUARANTEE

Set out below is a description of the key provisions of the contract under which a Guarantee is issued (the "Guarantee Agreement") under the EPMF.

The following outline of the Guarantee Agreement's key terms does not purport to be complete, and is qualified in its entirety by the detailed terms and conditions of the Guarantee Agreement. Furthermore, Guarantees may contain certain specific terms for different intermediaries. This document does not constitute an offer of any nature

[1] Decision No. 283/2010/EU of the European Parliament and the Council of 25 March 2010 establishing a European Progress Microfinance Facility for employment and social inclusion.

whatsoever and does not create any binding obligations on EIF to enter into a contract with any third party on the terms set out in this document or otherwise.

1. DIRECT GUARANTEES AND COUNTER-GUARANTEES

A Guarantee may be either:

- a **direct guarantee**, where the Guarantee covers new portfolios of micro-financing transactions entered into between the Intermediary and eligible beneficiaries ("Final Beneficiaries"), or

- a **counter-guarantee**, where the Guarantee covers new portfolios of guarantee instruments issued by the Intermediary in favour of an institution (a "Sub-Intermediary") to cover (either directly or via one or more sub-intermediaries) micro-financing transactions entered into with Final Beneficiaries.

2. PURPOSE OF THE GUARANTEE

The purpose of the Guarantees is to provide European Union resources to increase access to, and availability of, microfinance for Final Beneficiaries by having regard to the following criteria:

- the overall effect on the volume of financing provided to the eligible Final Beneficiaries,

- the effect on the volume of financing provided to each of the different types of Final Beneficiaries, and

- the effect on the volume of financing by the Intermediary in terms of geographical reach.

In no circumstances may Guarantees replace similar guarantees received by Intermediaries for the same purpose under existing European, national and regional financial instruments.

To stimulate access to and availability of microfinance, the Guarantee Agreement contains a mechanism whereby the extent of guarantee cover is dependent upon the amount of principal of the transactions which benefit from the Guarantee and are included in the relevant EPMF portfolio.

The aggregate amount of principal made available under such transactions is referred to as the "Actual Portfolio Volume". If the Guarantee is a direct guarantee, the Actual Portfolio Volume is the full principal amount made available under the micro credit loans entered into with Final Beneficiaries ("Final Beneficiary Transactions") covered by the Guarantee. If the Guarantee is a counter-guarantee, the Actual Portfolio Volume is that portion of the principal amount that is covered by the guarantees issued by an Intermediary, which are covered by the Guarantee.

The Guarantee Agreement contains a mechanism whereby the Actual Portfolio Volume is adjusted at the end of a Final Beneficiary Transaction's disbursement period (or, if earlier, at the end of the period in which transactions may be included for cover by the Guarantee (the "Availability Period")). This adjustment is made to ensure that the Actual Portfolio Volume is in line with the amounts ultimately drawn down under Final Beneficiary Transactions.

The Guarantee Agreement sets a target volume of transactions to be reached by the Intermediary (the "Agreed Volume"). Intermediaries must use their best efforts to ensure that the Actual Portfolio Volume reaches the Agreed Volume.

3. ELIGIBILITY CRITERIA

In order to benefit from the Guarantee, Final Beneficiary Transactions and Final Beneficiaries must comply with certain eligibility criteria (the "Eligibility Criteria").

3.1 Eligibility Criteria – Final Beneficiaries

Final Beneficiaries must be either:

- persons who have lost or are at risk of losing their job, or who have difficulties entering or re-entering the labour market, as well as persons who are facing the threat of social exclusion or vulnerable persons who are in a disadvantaged position with regard to access to the conventional credit market and who want to start or further develop their own micro-enterprise, including self-employment, or

- Micro-enterprises, especially in the social economy, as well as Micro-enterprises, which employ persons referred to in the paragraph above.

"Micro-Enterprise" means a micro-enterprise as defined in the Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises (2003/361/EC) (OJ L124, 20.5.2003, p.36), as amended (the "Recommendation"). In accordance with the Recommendation, a micro-enterprise is, inter alia, defined as an enterprise which employs fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 2 million.

"Micro-enterprise in the Social Economy" means a Micro-enterprise, which produces goods and services with a clear social mission and/or which provides services to members of the community with a non-profit purpose.

The micro-enterprise, including self-employed people, and persons that wish to start or develop a micro-enterprise, shall be established or to be established in the Member States of the European Union.

In addition, in order to be eligible, Final Beneficiaries must not be delinquent, defaulting under any other loan with the relevant Intermediary or Sub-Intermediary nor be insolvent or subject to bankruptcy proceedings. Furthermore they shall not have a substantial focus on gambling, tobacco, human cloning or arms production and trading sectors.

3.2 Eligibility Criteria - Final Beneficiary Transactions

a. Eligible types of finance

Guarantees cover portfolios of micro-loans below EUR 25,000 for each Final Beneficiary Transaction and Final Beneficiary, or portfolios of guarantees covering such micro-loans. The micro-loans must have a fixed bullet or amortising repayment schedule (excluding any credit lines) and shall not be revolving loans, restructuring of existing loans, non-performing loans, nor refinancing loans (unless at legal maturity).

b. Purpose of finance

Final Beneficiary Transactions shall cover the set up and/or development of a Micro-enterprise, such as investment financing, working capital, including the acquisition of licences, and other start-up costs for Micro-enterprises (established or to be established).

c. Maturity

The term of Final Beneficiary Transactions must be at least 3 months.

The Guarantee Agreement may contain additional eligibility criteria, which are agreed on a case-by-case basis with Intermediaries.

4. THE GUARANTEE CAP

The amount payable by EIF under the Guarantee is subject to a cap (the "Guarantee Cap").

In order to stimulate access to and availability of microfinance, the Guarantee Cap is dependent, inter alia, upon the Actual Portfolio Volume and is calculated, throughout the life of the Guarantee Agreement, in accordance with the following formula:

Guarantee Cap = Actual Portfolio Volume x Guarantee Rate x Guarantee Cap Rate

For the purpose of such calculation, the Actual Portfolio Volume means at any given time the Actual Portfolio Volume most recently reported to EIF (details of the Intermediary reporting requirements are set out below).

In order to achieve a risk-sharing arrangement with Intermediaries, the Intermediary losses covered by the Guarantee (as further described in section 6 below) are limited to a percentage rate specified in the Guarantee Agreement (the "Guarantee Rate"), which cannot exceed 75%.

In addition to this, the "Guarantee Cap Rate" contained in each Guarantee Agreement is applied. Such Guarantee Cap Rate is based on an estimate of the Intermediary's expected cumulative net[2] losses on the portfolio covered by the Guarantee.

Intermediaries shall retain at all times on their books a minimum of 20% of the credit risk under each transaction covered by the Guarantee for which they shall not benefit from another guarantee (any collateral provided by the Final Beneficiaries shall not constitute such guarantee).

5. INCLUSION AND EXCLUSION PROCESS

The transactions entered into by Intermediaries that may be covered by the Guarantee are termed "Intermediary Transactions".

All Intermediary Transactions that comply with the Eligibility Criteria and that have been entered into or, subject to certain conditions, approved during the Availability Period must be included in the Guarantee's portfolio (the "Portfolio"). However, once the Actual Portfolio Volume has reached the Agreed Volume, no further Intermediary Transactions may be included in the Portfolio.

To include Intermediary Transactions in the Portfolio, Intermediaries must submit to EIF an inclusion notice within the deadlines specified in the Guarantee Agreement. Upon EIF's receipt of such notice, the Intermediary Transactions referred to therein shall be automatically included in the Portfolio. Intermediary Transactions so included in the Portfolio are however covered by the Guarantee as from the date on which the relevant Intermediary Transaction is concluded.

If an Intermediary Transaction is cancelled or does not comply with the Eligibility Criteria or any other provision of the Guarantee Agreement, then it may be excluded from the Portfolio. Exclusion of an Intermediary Transaction from the Portfolio will result in a reduction of the Actual Portfolio Volume and, therefore, in the Guarantee Cap (as the Guarantee Cap is dependent, inter alia, on the Actual Portfolio Volume).

As explained above, the Guarantee Agreement contains a mechanism whereby the Actual Portfolio Volume will be adjusted at the end of a Final Beneficiary Transaction's disbursement period (or, if earlier, the end of the Availability Period) to be in line with the amounts drawn down under Final Beneficiary Transactions.

6. EXTENT OF GUARANTEE COVER – LOSS

The Guarantee covers, at the Guarantee Rate, certain losses incurred by an Intermediary in connection with Intermediary Transactions included in the Portfolio ("Loss"), subject to the Guarantee Cap and the other provisions of the Guarantee Agreement.

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[2] Net of recoveries.

If the Guarantee is a direct guarantee, the loss typically covered is any amount of principal or interest due (excluding default or capitalised interest or other costs or expenses), payable and outstanding under the relevant Final Beneficiary Transaction following acceleration by the Intermediary.

If the Guarantee is a counter-guarantee, the loss typically covered is any amount due and paid by the Intermediary under the terms of a guarantee issued to a Sub-Intermediary.

The Guarantee only covers losses if the default that triggered acceleration of the relevant Final Beneficiary Transaction or payment as the case maybe from the Intermediary (in case of counter-guarantee) occurred no later than six years after the date of entering into such Final Beneficiary Transaction (but not beyond its term or maturity).

7. GUARANTEE CALLS

Intermediaries may claim payment under the Guarantee by sending a guarantee call to EIF in the form set out in the Guarantee Agreement. Guarantee calls are however limited to a maximum of one per "Calling Period", which is a period of three calendar months (the first Calling Period of each year starting on 1st January) during which the guarantee call may be sent at any time. Subject to the Guarantee Cap, EIF shall pay amounts claimed in a guarantee call within two months after the end of the Calling Period during which the relevant guarantee call is received.

If payment of all amounts claimed under the Guarantee in any calendar semester would result in the Guarantee Cap being exceeded, then EIF shall only make payment up to the Guarantee Cap amount. Any amounts claimed above the Guarantee Cap will be paid following an increase (if any) of the Actual Portfolio Volume which results in an increased Guarantee Cap.

8. RECOVERIES

For each Guarantee an estimated recovery rate will be fixed reflecting the percentage expected to be recovered by an Intermediary in respect of Losses (the "Recovery Rate"). The amount to be paid by EIF under the Guarantee following each Loss shall be reduced by such Recovery Rate.

9. CLAWBACK

Intermediaries shall be required to repay amounts paid by EIF under the Guarantee under certain circumstances such as:

- if an amount has been paid to an Intermediary above the Guarantee Cap, any such excess amount must be repaid;

- if an Intermediary Transaction does not comply with the Eligibility Criteria or any other provision of the Guarantee Agreement, any amount paid by EIF related to such Intermediary Transaction must be repaid together with interest;

- if an Intermediary, a Sub-Intermediary or a Final Beneficiary is found guilty of fraud in relation to the EPMF, then all amounts paid to such Intermediary, Sub-Intermediary or Final Beneficiary (as applicable) must be repaid or requested to be repaid (as applicable) together with interest; and

- if any amount paid by EIF under the Guarantee relates to an illegal activity of a Final Beneficiary, any amount paid by EIF related to such Final Beneficiary must be repaid, together with interest.

10. COMMITMENT FEE

A commitment fee may be payable by Intermediaries following the end of the Availability Period. Such commitment fee is a one-off fee calculated after the end of the Availability Period on the difference between the Agreed Volume and the Actual Portfolio Volume. The calculation is progressive, i.e. the lower the Actual Portfolio Volume, the higher the commitment fee payable with thresholds at 30%, 70% and 90% of the Agreed Volume. No fee will be payable by the Intermediary if the Actual Portfolio Value reaches 90% of the Agreed Volume or if the Guarantee Agreement is terminated before the end of the Availability Period.

11. REPORTING

Intermediaries shall be required to send to EIF:

- every 6 months until the expiry or termination of the Guarantee Agreement, a report containing information about Intermediary Transactions included in the Portfolio, and

- every 30 April and 31 October until the last day on which Intermediary Transactions may be included in the Portfolio, a notice reporting the number of eligible Intermediary Transactions entered into during the preceding calendar quarter (i.e. 31 March and 30 September, respectively).

12. VISIBILITY AND PROMOTION OF THE EPMF

It is important that the EPMF is promoted and that Final Beneficiaries are made aware of the EU support. Therefore, Intermediaries are required to promote the EPMF and to cooperate with organisations which represent the interests of the Final Beneficiaries or which provide mentoring and training programmes to the Final Beneficiaries.

Intermediaries must also ensure that Final Beneficiary Transaction documentation states: "This financing benefits from a guarantee issued under the 'European Progress Microfinance Facility' established by the European Union." The exact wording needs to be used and translations will be provided by the EIF as applicable.

13. MAINTENANCE OF RECORDS, MONITORING AND AUDIT

Monitoring and audit of Intermediaries

Intermediaries are required to maintain and provide upon request information necessary to enable EIF, the Commission (including the European Anti-Fraud Office – OLAF), and the European Court of Auditors to verify the correct use of the European Community's funds and compliance with the terms of the Guarantee Agreement. Intermediaries are required to maintain such records throughout the life of the Guarantee Agreement and for five years following its termination or expiry.

Intermediaries must also allow EIF, the Commission, and the European Court of Auditors to carry out controls and inspections at Intermediaries' premises.

Monitoring and audit of Sub-Intermediaries and Final Beneficiaries

Intermediaries are also required to ensure that EIF, the Commission (including the European Anti-Fraud Office – OLAF), and the European Court of Auditors have the same monitoring and audit rights in respect of Sub-Intermediaries and Final Beneficiaries benefiting from the Guarantee. To this end, Intermediaries are required to ensure that each Sub-Intermediary (if applicable) and each Final Beneficiary undertakes to maintain relevant records for a period of five years from the date when the EIF's liability in respect of the relevant Intermediary Transaction expires.

Intermediaries are further required to insert in their agreements with Sub-Intermediaries (where applicable) and Final Beneficiaries the following standard text:

"The counter party acknowledges that the European Investment Fund ("EIF"), the agents of EIF, the European Court of Auditors (the "ECA"), the Commission and the agents of the Commission including OLAF (the "Agents") shall have the right to carry out controls and to request information in respect of this agreement and its execution. The counter party shall permit inspections by EIF, the agents of EIF, the ECA, the Commission and the Agents of its business operations, books and records. As these controls may include on the spot controls of the counter party, the counter party shall permit access to its premises to EIF, the agents of EIF, the ECA, the Commission and the Agents during normal business hours."

Again, the exact wording needs to be used and translations will be provided by EIF.

14. STATE AID

Intermediaries, in the context of the implementation of the Guarantee Agreement, are required to comply with all applicable State aid rules. Because of the public nature of the EPMF budget, the Guarantee is to be taken into account by its direct and/or indirect beneficiaries when considering State aid rules.

15. CURRENCY

Typically, the target volumes and payments made under the Guarantee Agreement by and to EIF shall be in Euro. In such cases, if an Intermediary Transaction is denominated in a currency other than Euro, or a Loss occurs in a currency other than Euro, the Guarantee Agreement will set out the exchange rate mechanism to be applied.

However, in some cases and subject to certain conditions, currencies other than Euro of relevant EU member states may be used under the Guarantee Agreement.

16. GOVERNING LAW

The Guarantee Agreement shall be governed by, and construed in accordance with, the laws of the Grand Duchy of Luxembourg.