1998 discharge: ECSC budget

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PURPOSE: Court of Auditors Annual Report on the ECSC for the 1998 financial year. CONTENT: The Report comprises two chapters and a series of tables. The first chapter deals with ECSC solvency and developments concerning main ECSC activities. It concerns the ECSC's solvency at 31/12/1997 and the changes in its main budgetary and financial activities during the year. The ECSC's solvency is of particular interest for the following reasons: 1) apart from some marginal lending from the ECSC's own funds, ECSC loans are financed from bank borrowings and bond issues. It is therefore important for ECSC securities to have the best possible financial market ratings. That, in turn, requires an excellent solvency level; 2) since most ECSC loans are back-to-back with the corresponding borrowings (in terms of rates, currency and maturity), the main remaining banking risk is the risk of non-recovery. Other risks may arise if the balance between loans and borrowings is disturbed by a debtor's defaulting; 3) the Treaty of Paris expires in 2002 and in consequence any changes in the own funds needed to safeguard the ECSC's solvency must be monitored carefully, right up to the expiry of the Treaty, and beyond that date, to ensure that the remaining borrowings can be serviced. - Solvency ratio: at 31/12/1998, the ECSC's solvency ratio was 32.8% compared with 28.3% at 31/12/1997. The change was due partly to the increase in the Guarantee Fund (+6%) but mainly to a substantial decrease in the volume of outstanding loans, owing to the Commission's decision to achieve a level of reserves equal to 100% of loans outstanding after 2002 which are not covered by a State guarantee. Consequently, the solvency ratio will gradually approach 100%. - Provision for large exposures: The expiry of the Treaty of Paris in 2002 is already having a significant effect on the level of ECSC activity. The loan portfolio is shrinking steadily and becoming concentrated on an increasingly small number of debtors. The risk generated by such a concentration of liabilities vis-à-vis third parties was the subject of a Council Directive on the monitoring and control of large exposures of credit institutions which provided for two limits. The Commission established a provision for large exposures in 1995 in order to offset the risk associated with this concentration. The amount of the provision is calculated as a function of the amounts by which the two limits have been exceeded, as specified in Annex VI to Council Direective 93/6/EEC. Although the Directive is not directly applicable to the ECSC situation, it does result in a policy which is sufficiently prudent as regards the exposures resulting from past transactions. The provision decreased from ECU 27 Mio at 31/12/1997 to ECU 23 Mio at 31/12/1998. The change is due to the fall in the assets in question following repayments in 1998. Specific value adjustments: Under the Council Directives concerning annual accounts, the asset items in the balance sheet must be valued individually and must be the subject of specific value adjustments if necessary. The amount shown inthe balance sheet for specific value adjustments for loans, including interest, fell from ECU 170 Mio to ECU 130 Mio at 31/12/1998 (i.e. 24%). This reduction is due, in particular, to the removal from the balance sheet item 'current assets' of a loan, including the related value adjustment, to a defaulting debtor, which, within the framework of the restructuring of its debt, issued new paper in 1998 to replace a part of its borrowings. The value adjustment in respect of this reduction would otherwise have been ECU 185.2 Mio. The Commission also reviewed the financial position of the other high risk debtors, namely those whose debts to the ECSC were not covered by first-class guarantees and made the necessary value adjustments. - Changes in applications of ECSC funds and resources: The commitments for the ECSC operating budget continued to fall in 1998 (by 14.9%). This trend is due, for the most part, to a decrease in the aid given for retraining (ECU -25.1 Mio) and, to a lesser extent, to the absence of new interest subsidies since no subsidised loan was granted in 1998. In addition, commitments were ECU 60 Mio below the budgetary estimates because of the decrease in retraining aid (ECU - 30 Mio) and reconversion aid (ECU -30 Mio). Resources continued to decline after an isolated increase in 1997. This was mainly the result of 2 opposing factors: (a) the reduction to zero of the levy, for the first time, and (b) a particularly large amount in decommitments for the second consecutive year. In contrast with the estimates, the budget was in surplus for the third consecutive year, which allowed the Guarantee Fund (ECU +30 Mio) and the provisions for the financing of the ECSC operating budget (ECU +26 Mio) to be bolstered even further. - Changes in the balance sheet: The ECSC's

balance sheet total declined by ECU 903 Mio (15.2%) between 31/12/1997 and 31/12/1998 mainly owing to the lower level of loans outstanding from borrowed funds: during the 1998 financial year, the ECSC received ECU 690.6 Mio in loan reimbursements whereas it disbursed only ECU 19.7 Mio of new loans. The amount of outstanding loans from borrowed funds was ECU 2 898 Mio on 31/12/1998. This item will continue declining, falling to around ECU 730 Mio by 23/07/2002 (before value adjustments), almost 90% of which will not be covered by first-class guarantees. The last of these loans will mature in 2019. These figures were calculated on the basis of the loans disbursed before 31/12/1998. Following a Commission decision, there must be no more new loans that would tie up reserves and mature after the expiry of the ECSC Treaty. At 31/12/1997, the liquid asset accounts made up 39% of the ECSC's assets and constituted the second largest item, after loans. The second chapter relates to the statement of assurance concerning the ECSC: The Court has examined the ECSC's accounts so as to provide the European Parliament and the Council with a statement of assurance concerning the reliability of the accounts and the legality and regularity of the underlying transactions. The Court concluded that the financial statements 'gave an accurate picture of the assets and of the financial situation of the ECSC at 31/12/1998, and of the result of its operations for the financial year endingon the same date'. In the Court's view, the legality and regularity of the transactions are, on the wholre, adequately guaranteed.