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Court of Auditors

Special report of the Court of Auditors on loans and borrowings 1

I

*(Information)***COURT OF AUDITORS**

SPECIAL REPORT OF THE COURT OF AUDITORS
on loans and borrowings
(Observations, Articles 206a EEC and 180a EAEC of the Treaty)

This report was adopted by the Court of Auditors in its meeting of 19 July 1982, in application of Articles 206a EEC and 180a EAEC of the Treaty. On 16 April 1982 it was sent for comment to the Commission of the European Communities whose replies are attached.

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CHAPTER I

INTRODUCTION

Background

1.1. Historically, the implementation of the Community's policies has been financed by the Community budget, itself wholly financed by budgetary revenue⁽¹⁾. However, a significant change may be discerned in the period 1975-1981 with the increasing recourse by the Community to borrowings, rather than budget revenue, as the means of financing new Community activities. In that period, the Council established three loan mechanisms, namely, Balance of Payments (BP) loans, Euratom loans and New Community Instrument (NCI) loans. The loans, which are granted under each of these mechanisms, are financed solely by borrowings contracted by the Commission on behalf of the Community. The introduction of these mechanisms constituted a significant addition to the loan mechanisms already in existence at the Community level prior to 1975, namely, the European Coal and Steel Community (ECSC) loans and the European Investment Bank (EIB) loans.

1.2. These new mechanisms may be summarized by reference to their objectives, and, the maximum level of borrowings authorized for each mechanism by the Council up to 31 December 1981.

1975

Balance of payments loans (3 000 million US \$ or 2 291 million ECU):
loans to Member States for the purpose of balance of payments support⁽²⁾.

1977

Euratom loans (1 000 million ECU):
loans to develop nuclear facilities for the production of electricity⁽³⁾.

1978

New Community Instrument loans (1 000 million ECU):
loans to promote investment within the Community in the energy, infrastructure and industrial sectors,

thereby reducing regional disparities and the level of unemployment⁽⁴⁾.

1981

New Community Instrument loans (1 000 million ECU, less EIB loans for the same purpose):
loans to promote investment for the reconstruction of the means of production and the economic and social infrastructure in the Italian regions affected by the 1980 earthquake⁽⁵⁾. The amount authorized by Council for this measure is in addition to the 1 000 million ECU granted to the NCI in 1978.

1981

Balance of payments loans (6 000 million ECU):
this replaces the 1975 mechanism and thus its provisions are only applicable to new BP loans to be granted to Member States⁽⁶⁾.

1981

New Community Instrument loans (80 million ECU, less EIB loans for the same purpose):
loans to promote investment for the reconstruction of the means of production and the economic and social infrastructure in the regions affected by the Greek earthquake in February and March 1981⁽⁷⁾.

In 1980, the Commission submitted to the Council a proposal for a revised NCI mechanism which notably envisaged the abolition of the limit on the level of NCI borrowings and the introduction of simultaneous borrowing tranches. The Council agreed in October 1981, following a review of the NCI activities carried out under the 1978 Decision, to approve in principle the continuation of the NCI mechanism. In March 1982, the Council authorized the

(1) EEC Treaty, Article 199: 'The revenue and expenditure shown in the budget shall be in balance'.

(2) Council Regulation (EEC) No 397/75 of 17 February 1975 (OJ No L 46, 20. 2. 1975).

(3) Council Decision 77/270/Euratom of 29 March 1977 (OJ No L 88, 6. 4. 1977).

(4) Council Decision 78/870/EEC of 16 October 1978 (OJ No L 298, 25. 10. 1978).

(5) Council Decision 81/19/EEC of 20 January 1981 (OJ No L 37, 10. 2. 1981).

(6) Council Regulation (EEC) No 682/81 of 16 March 1981 (OJ No L 73, 19. 3. 1981).

(7) Council Decision 81/1013/EEC of 14 December 1981 (OJ No L 367, 23. 12. 1981).

Commission to contract borrowings to a limit of 1 000 million ECU in principal⁽⁸⁾ for the NCI mechanism.

1.3. The volume of loans granted under these mechanisms in the period 1976-1981 is illustrated in Table 1.1.

TABLE 1.1
Loans granted in the period 1976-1981⁽¹⁾

Mechanism	(million ECU)						
	Year	1976	1977	1978	1979	1980	1981
Balance of payments		1 168	568	—	—	—	—
Euratom			96	71	149	182	358
New Community Instrument					179	303	328
Annual totals		1 168	664	71	328	485	686

(1) Sources:
Commission's balance sheet and revenue and expenditure account for
1978: COM(79) 221, Vol. II, pp. 270-273;
1979: COM(80) 233, Vol. II, pp. 302-307;
1980: COM(81) 223, Vol. II, pp. 292-297;
1981: COM(82) 233, Vol. II, pp. 319-325.

Scope, object and structure of report

1.4. This report is confined to those loans which are financed exclusively by Commission borrowings and which are granted under the BP, Euratom and NCI mechanisms, including the special emergency NCI loans for projects in earthquake-affected areas of Italy and Greece. It deals also with the interest rate subsidies⁽⁹⁾ which may be granted to certain NCI and EIB loans.

The report does not examine either the European Coal and Steel Community (ECSC) loans, or the loans granted to non-Member States, under the Financial Protocols between the Commission and those countries or under the European Development Funds.

1.5. The report assesses the procedures adopted in relation to the decision making for the loans and the financial management of the mechanisms both at the Commission level and between the Commission

and its agents, the EIB and the European Monetary Cooperation Fund⁽¹⁰⁾ (EMCF). These procedures are essentially determined by, firstly, the Council decisions establishing the mechanisms and secondly, the bilateral Cooperation Agreements between the Commission and the EIB, relating to the practical implementation of those Council decisions. The external audit provisions of the mechanisms have also been reviewed.

1.6. This report is structured not on the basis of a separate analysis of each borrowing and lending mechanism but rather by examining the mechanisms together with regard to a particular subject-matter.

Chapter 2 outlines the partial manner in which the mechanisms are presently included in the Community budget, as well as the Commission's proposals to alter this presentation by incorporating loans and borrowings into the Commission section of the Community budget.

Chapter 3 describes the objectives of the different mechanisms and the conditions fixed by the Council for their implementation.

(8) Council Decision 82/169/EEC of 15 March 1982 (OJ No L 78, 24. 3. 1982).

(9) (i) Council Regulation (EEC) No 1736/79 of 3 August 1979 (OJ No L 200, 8. 8. 1979) for the EMS interest rate subsidies on EIB and NCI loans to Italy and Ireland;
(ii) Council Decisions 81/19/EEC and 81/1013/EEC for the interest rate subsidies on NCI and EIB loans to Italian and Greek areas affected by earthquakes in 1980 and 1981 respectively.

(10) European Monetary Cooperation Fund (EMCF) was established by Council Regulation (EEC) No 907/73 of 3 April 1973 (OJ No L 89, 5. 4. 1973).

Chapter 4 analyzes the decision making procedures in force for the loans at the Commission and between the Commission and the EIB.

Chapter 5 examines the financial management procedures for the mechanisms.

Chapter 6 reviews the manner in which the external audit of the mechanisms has been defined.

Summary of the observations

Decision-making procedures

1.7. Euratom loans

(a) The Commission's EIB Inter-Service Group deliberations on projects are difficult to analyze in the absence of substantive minutes of their meetings.

(para. 4.37)

(b) The criteria which the EIB uses in its evaluation of a project are not explicit in the Cooperation Agreement between the Commission and its agent, the EIB.

(para. 4.37)

1.8. NCI loans

(a) The Commission in its role of deciding on the eligibility of projects, has not interpreted explicitly the Council's general eligibility guidelines for NCI loans.

(para. 4.38)

(b) As with Euratom loans, the Commission's EIB Inter-Service Group does not hold minutes of its deliberations on projects submitted for NCI loans.

(para. 4.39)

(c) Loans granted under the NCI mechanism appear equivalent to EIB loans except that the former are financed by Commission borrowings.

(para. 4.40)

(d) There is no consistency between the allocation of responsibilities decided for the NCI mechanism in 1978 when compared to those decided for the Euratom mechanism in 1977.

(para. 4.41)

(e) The Court considers that it would be preferable if, in the interests of consistency between mechanisms and due to the Community's direct financial responsibility for its borrowings, the Commission was granted responsibility for making the NCI loan decisions.

(para. 4.41.)

1.9. EMS interest rate subsidies

(a) The Cooperation Agreement adopted by the Commission and the EIB on the practical implementation of the EMS interest subsidies requires a number of important clarifications with regard to the decision-making process.

(para. 4.44)

(b) The Cooperation Agreement does not define the criteria used in the initial selection of projects for consideration for interest subsidies.

(para. 4.44 (i))

(c) The Cooperation Agreement does not define the criteria used in allocating the annual budgetary appropriations (200 million EUA) for the EMS subsidies between NCI and EIB loans.

(para. 4.44 (ii))

(d) The Cooperation Agreement does not define the Commission's interpretations of the Council's eligibility guidelines for interest rate subsidies.

(para. 4.44 (iii))

(e) It is the EIB decision to grant the NCI loan and/or EIB loan to a project which determines if that project shall receive an EMS interest subsidy financed by the Community budget.

(para. 4.45)

(f) This decision-making process appears contrary to Article 205 of the EEC Treaty wherein the Commission is charged with the implementation of the budget.

(para. 4.45)

Financial management

1.10. BP mechanism

(a) Contracts to be concluded by the Commission are not submitted for the approval of the Com-

- mission's financial controller prior to signature.
(para. 5.24)
- (b) The Commission's accounting officer should
- (i) ascertain the EMCF's method of verifying the BIS's (Bank of International Settlements) accounts.
 - (ii) Confirm with the lending banks and/or central banks of the beneficiary Member States the outstanding balances at the year-end for the loans and borrowings.
(para. 5.23)
- 1.11. Euratom and NCI mechanisms
- (a) There is no consistency between the Euratom and NCI mechanisms with regard to the arrangements for the financial management of the mechanisms.
(paras 5.9 to 5.11)
 - (b) DG XVIII administers the financial transactions associated with the above mechanisms independently of both the Commission's financial controller and accounting officer.
(para. 5.27)
 - (c) DG XVIII has its own accounting system independently of the Commission's accounting officer.
(para. 5.26)
 - (d) There is no involvement of the Commission's financial controller at the contract stage nor is his approval sought for the individual financial transactions relating to the loans and borrowings.
(paras 5.13 to 5.14 and 5.25)
 - (e) The concentration of functions at DG XVIII is in contradiction with a basic principle of internal control and with the Commission's own proposals on the 'budgetization' of loans and borrowings.
(paras 5.28 to 5.31)
- 1.12. EMS interest rate subsidies
- (a) The volume of budgetary appropriations ultimately utilized is dependent on the EIB's loan decision(s) rather than the Commission's eligibility decision.
(paras 5.16 and 5.32)
 - (b) The Commission does not possess original supporting documents for the payment of interest subsidies on EIB loans.
(paras 5.17 and 5.33)
 - (c) The Cooperation Agreement on EMS interest subsidies between the Commission and the EIB does not indicate how 75 % of the annual rate of interest was decided for the calculation of the present value of the interest subsidies.
(paras 5.18 and 5.34)
 - (d) There have been differences in the disposal of the interest rate subsidies by the EIB between Italian and Irish projects.
(paras 5.19 and 5.35)
- External audit of the mechanisms*
- 1.13. BP mechanism
- (a) The EMCF's directive to the BIS, its agent, should contain a clause pertaining to the Court's right of audit of the administration of the BP loans and borrowings.
(paras 6.2 to 6.6)
- 1.14. NCI mechanisms and EMS interest subsidies:
- (a) The bilateral Cooperation Agreements between the Commission and the EIB incorporated additional audit clauses which are contradictory to the audit provisions of Article 206 of the EEC Treaty and these clauses should be deleted.
(paras 6.4 to 6.7)
- General*
- 1.15. The introduction of these mechanisms may not be construed as the result of a Council decision of the financing of Community policies. Consequently, the attributions of responsibilities for the granting and administration of the loans differ from one mechanism to another.
(para. 7.1)
- 1.16. The Court of Auditors considers that it would be preferable if the Commission introduced internal procedures for the decision making and financial management of the loans and borrowings analogous to those procedures contained in the Financial Regulation.
(para. 7.6)

1.17. As a general policy, cooperation agreements/contracts agreed with third parties by the Commission or other Community institutions should auto-

matically incorporate an audit provision stating clearly that the Treaties audit provisions are applicable.

(para. 7.5)

CHAPTER 2

BUDGETARY PRESENTATION OF THE MECHANISMS

Budgetary situation

2.1. The Council decisions which established the borrowing and loan mechanisms in the period 1975-1981 explicitly stated for each mechanism that:

- (a) the loans granted under that mechanism would be exclusively financed by the borrowings contracted by the Commission on behalf of the Community;
- (b) the borrowings under each mechanism were to be utilized for the sole purpose of granting the corresponding loans.

These related conditions exclude the possibility that funds borrowed by the Commission may be diverted to finance budgetary expenditure such as the Social, Regional or Agricultural Funds.

2.2. The loans and borrowings for the NCI, Euratom and BP mechanisms are not subject to annual appropriations authorized by the budgetary authorities and contained in the Community budget, nor to the provisions of the financial regulation which are applicable to that budget. The volume of loans and borrowings contracted in any financial year depends on, firstly, the cumulative total of borrowings authorized by the Council for each mechanism and secondly, the eligible loan applications approved. No budgetary constraints are therefore placed on the loans and borrowings operations and it is the Council alone rather than the budgetary authorities jointly which determines their overall volume.

Budgetary guarantee

2.3. The Commission has a direct legal commitment to service and repay the borrowings it contracts on behalf of the Community. Therefore, if a loan beneficiary (NCI, BP or Euratom) defaults on the due dates for payment of either capital or interest to the Commission, it is the latter acting on

behalf of the Community which is obliged to finance these payments from its budgetary resources. The Commission section of the Community budget therefore includes token entries representing the budgetary guarantee on Community borrowings for the BP, Euratom and NCI mechanisms.

In addition to this budgetary guarantee, the 1975 BP mechanism included a guarantee from the non-beneficiary Member States to service and repay BP borrowings, according to predetermined percentages, should a Member State default on a BP loan. The 1981 BP mechanism does not contain the non-beneficiary Member States guarantee and it is the Community budget guarantee alone which is applicable.

Up to 31 December 1981, the budgetary guarantee has never been called upon for any of the mechanisms and this factor indicates the relative financial strength of the mechanisms.

Presentation in the budget

2.4. As a result of the foregoing, the presentation in the Community budget of the mechanisms in question is limited to the inclusion of:

- (i) token entries⁽¹¹⁾ denoting the budgetary guarantee to which
 - (a) Commission expenditure, resulting from defaulting loan beneficiaries, may be charged;
 - (b) Commission revenue, resulting from claims against defaulting loan beneficiaries, may be credited;
- (ii) Annex III to the Commission section of the Community budget

⁽¹¹⁾ By way of example, Euratom token entries in the 1981 Budget were: Expenditure: Article 3.2.9; Revenue: Article 9.4.1.

Information on the loans and borrowings contracted and their debt management is contained in this Annex, in accordance with Article 73 (5) of the Financial Regulation of 21 December 1977 ⁽¹²⁾.

Commission's proposals on budgetization

2.5. In 1978, the Commission introduced proposals ⁽¹³⁾ to Council with the object of amending the Financial Regulation of 21 December 1977 applicable to the general budget, thereby improving the budgetary presentation of loans and borrowings. When the present budgetary treatment of loans and borrowings, as outlined in 2.4, was taken into account, the Commission considered that from the point of view of:

- (a) the budgetary authorities this method did not give the required transparency with regard to the repayment of sums borrowed and lent and the repayment of costs,
- (b) the original lenders of the funds, the method did not define how the guarantee provided by the Community would operate to allow the obligations contracted to be met out of own resources.

2.6. The Commission in its proposal recommended two parts to the general budget.

Part I would continue to retain the token entry presentations to record any expenditure not covered by payments from loan beneficiaries and any revenue resulting from the Commission exercising its right to proceed against defaulters.

Part II would include the following facts for the financial year in question, the current financial year and the one prior to that:

- (i) the annual amounts of borrowing and related lending;
- (ii) the annual capital repayments to the Community, and by the Community to the original lenders;
- (iii) the annual interest payments paid or due to the Community, and paid or due by the Community to the original lenders;
- (iv) annual instalments to cover the issue costs incurred by the Community, and the sums due annually to the Community to cover the cost of managing these borrowing and lending operations as well as, on the expenditure side, payment of the same costs payable or due by the Community.

The entry in Part II of the general budget of the sums involved in borrowing and lending operations and the capital and interest (re)payments, would constitute the authorization, within the limits fixed by the Council in the basic Regulations, for borrowing, lending, repayment of capital and payment of interest and associated costs annually.

The Court, in its opinion, supported the Commission's proposal whilst requesting certain amendments to the text ⁽¹⁴⁾.

No Council decision has yet been taken on the Commission proposal.

CHAPTER 3

DESCRIPTION OF THE MECHANISMS

Summary

3.1. This chapter describes the objectives of each mechanism and the conditions applicable to the loans and borrowings granted under that mechanism.

Objectives of the mechanisms

BP Mechanism

3.2. A number of Member States encountered balance of payments difficulties in the latter half of

⁽¹²⁾ OJ No L 356, 31. 12. 1977.

⁽¹³⁾ OJ No C 160, 6. 7. 1978.

⁽¹⁴⁾ Transmitted to the Council on 27 July 1978 and published in OJ No C 139, 5. 6. 1979.

1973 and 1974 due to the increase in oil prices. To alleviate these difficulties and to redress the balance of payments situation, the Council decided in 1975 to introduce a new financial mechanism under which the Commission, acting on behalf of the Community, would borrow either directly from third countries and financial institutions or on the international market and subsequently on-lend those funds on identical terms to applicant Member States. In return the beneficiary Member States would agree to respect a series of economic policy conditions decided by Council and designed to remedy their balance of payments situation.

3.3. The new BP mechanism introduced in 1981 while following the same general principles as the 1975 mechanism, differs in certain technical respects. These differences include a ceiling of 6 000 million ECU on total cumulative borrowings; the possibility of disbursement of the loan in instalments and the inclusion of an early repayment clause in the loan contract. The objectives of the mechanism remain essentially unaltered however.

Euratom mechanism

3.4. The objective of the Euratom mechanism introduced in 1977 was to provide finance for the development of nuclear energy to produce electricity, so that the Community's dependence on external energy sources might be reduced. In view of the considerable financial resources required to assist in the development of nuclear energy and in particular the establishment of the necessary basic installations, the Council decided that recourse should be made by the Community to the capital market to borrow funds. These funds would in turn be granted to enterprises in the form of loans to finance projects relating to the industrial production of electricity in nuclear power stations and industrial fuel cycle installations.

NCI Mechanism

3.5. The NCI mechanism established by the Council in 1978, had the objective of promoting investment projects in the Community thereby contributing to greater convergence and integration of the economic policies of the Member States. The investment projects, in the energy, industry and infrastructure sectors, must accord with Community priorities, and reduce both regional disparities and unemployment levels.

3.6. Following the earthquakes in Italy⁽¹⁵⁾ in November 1980 and in Greece⁽¹⁶⁾ in February and March 1981, the Council decided to add to the existing 1978 NCI decision the provision for loans to be granted to promote investment in the reconstruction of the means of production and the economic and social infrastructures in the affected Italian and Greek regions. These NCI loans for projects in the earthquake-affected areas in Italy and Greece automatically benefit from annual interest rate subsidies of 3 % over a maximum period of 12 years.

In accordance with the 1978 Council Decision on the NCI, the Commission in 1980 made a proposal to the Council on the continuation of the NCI. The Council agreed in October 1981, following a review of the NCI activities carried out under the 1978 Decision, to approve in principle the continuation of the NCI mechanism. In March 1982, the Council authorized the Commission to contract borrowings of 1 000 million ECU to finance NCI loans.

EMS interest rate subsidies

3.7. The European Council resolution of 5 December 1978 on the establishment of the European Monetary System (EMS) included measures designed to strengthen the economies of the less prosperous Member States. The Commission was asked⁽¹⁷⁾ to submit a proposal providing interest rate subsidies of 3 % for NCI and EIB loans, on condition that the total capitalized cost of these subsidies, divided into annual tranches of 200 million EUA, would not exceed 1 000 million EUA over a period of five years. The Council decided in August 1979 on the introduction of the EMS interest rate subsidies. It was considered that the reduction of the cost to NCI and EIB loan beneficiaries, through the application of interest rate subsidies, would encourage investment in the less prosperous Member States of the Community participating fully and

⁽¹⁵⁾ Council Decision 81/19/EEC of 20 January 1981 (OJ No L 37, 10. 2. 1981), 'Community aid granted by way of exception for the reconstruction of regions affected by the Italian earthquake in November 1980.'

⁽¹⁶⁾ Council Decision 81/1013/EEC of 14 December 1981 (OJ No L 367, 23. 12. 1981), 'Community aid granted by way of exception for the reconstruction of regions affected by the Greek earthquakes in February and March 1981.'

⁽¹⁷⁾ The European Council also requested the Community institutions, by the utilization of the NCI, and the EIB to make available, for a period of five years, loans of up to 1 000 million EUA per annum to the less prosperous Member States fully and effectively participating in the European Monetary System.

effectively in the European Monetary System, namely, Italy and Ireland ⁽¹⁸⁾.

As with the NCI loans, the projects to benefit from the EMS interest rate subsidies must have as objectives the reduction of both regional disparities and unemployment.

Conditions applicable to the mechanisms

3.8. The Council decisions establishing the mechanisms (BP, NCI and Euratom) defined the conditions applicable to these mechanisms. For ease of reference, the description of these conditions has been structured not individually for each mechanism but rather by reference to the overall conditions applicable. This information is summarized in Table 3.1.

Matching principle

For all three mechanisms, the Commission borrows funds, on behalf of the Community, with the sole purpose of lending these funds to beneficiaries. The Commission may only borrow funds for each individual mechanism equal to the volume of loans it will grant. There is thus a direct matching for each mechanism between the level of borrowings and of loans.

Ceiling

The Council authorizes the maximum volume of borrowings under each mechanism and by definition due to the matching principle this limit also determines the level of the loans granted. Since 1975 these borrowing limits have been subject to upward revision by the Council. For instance, the ceiling on new BP borrowings which may be contracted under the 1981 mechanism is fixed at 6 000 million ECU calculated as capital only, whereas under the 1975 mechanism the ceiling was 2 291 million ECU (3 000 million US \$ at 31 December 1980 rates) calculated as capital and interest. In addition, the 1981 ceiling is on the basis of total outstanding borrowings, whereas the 1975 limit was on the basis of total accumulated borrowings.

The maximum potential volume of loans which may be granted under each mechanism, itself determined

by the total borrowings authorized by the Council, was as follows at 31 December 1981.

BP loans: 1981:	6 000 million ECU ⁽¹⁹⁾
1975:	3 000 million US \$ ⁽²⁰⁾
Euratom loans:	1 000 million ECU ⁽²¹⁾
NCI loans:	1 000 million ECU ⁽²²⁾
NCI 'earthquake' loans to Italy:	1 000 million, less EIB loans for the same purpose ⁽²³⁾
NCI 'earthquake' loans to Greece:	80 million ECU, less EIB loans for the same purpose ⁽²⁴⁾ .

The above ceilings are absolute limits authorized by the Council on total *accumulated* borrowings for each mechanism, with the exception of the 1981 BP mechanism, which is based on total *outstanding* borrowings.

Community financing of projects

Up to 31 December 1981 nearly all projects which received NCI or Euratom loans also benefitted from EIB loans, although the receipt of the latter is not a prerequisite to their receiving the former.

Guarantees

Public and/or private guarantees must be secured on the loans, except those granted under the BP mechanism. The Community's guarantee on its borrowings has already been referred to in paragraph 2.3.

Interest rate

For the BP and Euratom mechanisms, identical terms must apply to the borrowings and loans with regard to the payment of capital and interest. Initial and on-going costs associated with these operations

⁽¹⁸⁾ Council Decision 79/691/EEC of 3 August 1979, (OJ No L 200, 8. 8. 1979).

⁽¹⁹⁾ Council Regulation (EEC) No 682/81 of 16 March 1981 (OJ No L 73, 19. 3. 1981).

⁽²⁰⁾ Council Regulation (EEC) No 397/75 of 17 February 1975 (OJ No L 46, 20. 2. 1975).

⁽²¹⁾ Council Decision 80/29/Euratom, 20 December 1979 (OJ No L 12, 17. 1. 1980).

⁽²²⁾ Council Decision 80/1103/EEC, 25 November 1980 (OJ No L 326, 2. 12. 1980).

⁽²³⁾ Council Decision 81/19/EEC, 20 January 1981 (OJ No L 37, 10. 2. 1981).

⁽²⁴⁾ Council Decision 81/1013/EEC, 14 December 1981 (OJ No L 367, 23. 12. 1981).

are borne directly by the loan beneficiary. For the NCI mechanism, the loan terms must be fixed for the reimbursement of capital and the rate and payment of interest, so that the costs and expenses of both the borrowing and loan sides may be covered over the life of the borrowing and loan.

Interest rate subsidies

- (a) NCI and EIB loans⁽²⁵⁾, to Italy and Ireland only⁽²⁶⁾, may benefit from capitalized interest rate subsidies of 3% financed by the Community budget under the European Monetary System
- (b) NCI and EIB loans to Italy for the earthquake-affected regions benefit automatically over a period of 12 years from annual interest subsidies

(3%) which are financed by the Community budget⁽²⁷⁾.

- (c) NCI and EIB loans to Greece for the earthquake-affected regions benefit automatically over a maximum period of 12 years from annual interest subsidies (3%) which are financed by the Community budget⁽²⁸⁾.

No interest subsidies are granted to Euratom and BP loans.

3.9. The major conditions applicable for each type of mechanism discussed in this report, as well as the indication of the administrative responsibilities for the borrowings and loans are listed in Table 3.1 (page 12).

CHAPTER 4

DECISION-MAKING PROCEDURES: LOANS AND INTEREST RATE SUBSIDIES

Summary

4.1. The decision-making procedures established by the Council for the loans, differ from one mechanism to another. Whilst certain aspects of these procedures may be common to more than one mechanism, nevertheless it is more useful to outline separately the procedures relating to each mechanism. The borrowings contracted by the Commission are a consequence of the decision, be it by the Council, Commission or EIB, to grant a loan. The borrowing procedures are discussed in Chapter 5.

The basis for the decision-making procedures on the loans is essentially twofold. Firstly, the Council decision establishing the mechanism allocates the administrative, managerial and financial responsibilities. Secondly, the bilateral cooperation agreements between the Commission and its agents, notably the EIB, deals with the practical implementation of the Council decisions.

Balance of payments mechanism

4.2. The decision-making procedures for the BP mechanism are defined in:

- (a) Council Regulation (EEC) No 397/75⁽²⁹⁾ for those BP loans contracted in the 1975-1980 period;
- (b) Council Regulation (EEC) No 682/81⁽³⁰⁾ for new BP loans to be granted.

Whilst the 1981 mechanism differs from the 1975 mechanism in certain respects, the basic decision-making procedures as defined in the Council Regulations remain unaltered. Since no BP loans had been contracted up to 31 December 1981 under the 1981 mechanism then the description of procedures which follows relates to those BP loans granted to Italy and Ireland in 1976 and 1977 under the 1975 mechanism.

Commission's Role

4.3. The procedures which were followed by the Commission prior to the Council decision granting

⁽²⁵⁾ Council Regulation (EEC) No 1736/79 of 3 August 1979 (OJ No L 200, 8. 8. 1979).

⁽²⁶⁾ Council Decision 79/691/EEC of 3 August 1979, implementing Council Regulation (EEC) No 1736/79 (OJ No L 200, 8. 8. 1979).

⁽²⁷⁾ Council Decision 81/19/EEC of 20 January 1981, Article 3 (OJ No L 37, 10. 2. 1981).

⁽²⁸⁾ Council Decision 81/1013/EEC of 14 December 1981, Article 3 (OJ No L 367, 3. 12. 1981).

⁽²⁹⁾ OJ No L 46, 20. 2. 1975.

⁽³⁰⁾ OJ No L 73, 19. 3. 1981.

TABLE 3.1

Conditions applicable to the mechanisms at 31 December 1981

Mechanism Conditions	Balance of payments	Euratom	New Community Instrument (NCI)		
			1978 Decision	Italian earthquake	Greek earthquake
Objectives	Alleviate balance of payments difficulties in Members States	Encourage development of nuclear energy for producing electricity	Promote investment within the Community, by granting loans to projects in infrastructure, energy and industry sectors	Reconstruction of earthquake affected areas, by granting loans for the reconstruction of the means of production and the economic and social infrastructure in Italian regions affected by 1980 earthquake	Reconstruction of earthquake affected areas, by granting loans for the reconstruction of the means of production and the economic and social infrastructure in Greek regions affected by 1981 earthquake
Ceiling on borrowings	US \$ 3 000 million ⁽¹⁾ 6 000 million ECU ⁽²⁾	1 000 million EUA	1 000 million EUA	1 000 million ECU less EIB loans for same purpose	80 million ECU less EIB loans for same purpose
Matching principle (Borrowings and loans)	Yes	Yes	Yes	Yes	Yes
Interest subsidies applicable to loans ^(*)	No	No	Yes (Article 520 Italian and Irish projects only)	Yes Article 691	Yes Article 692
Joint financing of projects by the Communities	Not applicable	Yes — EIB loans	Yes — EIB loans	Yes — EIB loans	Yes — EIB loans
Administration (i) Borrowings (ii) Loans	The European Monetary Cooperation Fund's Agent ⁽³⁾ , — Bank of International Settlements (BIS)	(i) Commission (DG XVIII) (ii) EIB	(i) Commission (DG XVIII) (ii) EIB	(i) Commission (DG XVIII) (ii) EIB	(i) Commission (DG XVIII) (ii) EIB

⁽¹⁾ Council Regulation (EEC) No 397/75 of 17 February 1975.

1975 BP mechanism: The ceiling of 3 000 million US \$, or 2 291 million ECU at 31. 12. 1980 rules, is based on total *accumulated* loans, the ceiling including capital and interest.

⁽²⁾ Council Regulation (EEC) No 682/81 of 16 March 1981.

1981 BP mechanism: The ceiling of 6 000 million ECU is based on total *outstanding* loans; the ceiling includes capital only.

⁽³⁾ The European Monetary Cooperation Fund (EMCF) was established by the Council in 1973 (Decision 73/907/EEC of 3 April 1973 (OJ No L 89, 5. 4. 1973)) with the purpose of contributing to the progressive establishment of economic and monetary union between the Community Member States. The fund is directed and managed by a board of governors who are members of the committee of governors of the central banks of the Community.

^(*) The reference to budgetary articles refers to the 1982 budgetary classification.

the loan, consisted of negotiating and making proposals to the Council on:

- (a) the terms of the loan, identical terms applying both for the borrowing and loan in respect of capital and interest rates;
- (b) the economic policy conditions to be applied to the granting of the loan.

Terms

4.4. The Directorate-General of Economic and Financial Affairs (DG II) within the Commission conducted the negotiations with the financial institutions for the borrowings contracted in 1976-1977 under the 1975 mechanism. Following these negotiations the Commission consulted the Monetary Committee⁽³¹⁾ for its opinion on the terms. Taking into account the results of that consultation, the Commission submitted its formal proposal on the terms of the loan to the Council. If the Council decided unanimously on the terms of the loans, it then authorized the Commission to conclude on behalf of the Community the borrowing and lending contracts with the financial institutions and the representatives of the Member State, respectively. In contrast with the decision-making procedures for the Euratom and NCI mechanisms to be discussed in this chapter, the BP mechanism is the only mechanism where the Council, and not the Commission or the EIB, decides on each individual loan.

Economic policy conditions

4.5. The stated intention of the balance of payments support mechanism was to assist Member States in redressing their difficulties caused by the continuing rise in petroleum product prices. A Member State which was granted a BP loan agreed to respect certain economic policy conditions which were attached as a condition of the granting of the loan.

As was the case with the negotiations of the loan terms, DG II was responsible for drawing up the proposal on these economic policy conditions. The

Monetary Committee was consulted for its opinion prior to the submission of the proposal to the Council by the Commission. The Council decided on the Commission proposal, in principle, on the same date as it decided on the granting of the loan and its terms.

The Commission was responsible for verifying at regular intervals, in conjunction with the Monetary Committee, that the Member State's economic policy respected the conditions decided for the BP loan⁽³²⁾.

Euratom mechanism

4.6. The procedures relating to Euratom loan decisions are defined in the following documents which delineate the respective responsibilities of the Council, Commission and EIB.

- (a) Council Decision 77/270/Euratom of 29 March 1977, empowering the Commission to issue loans for the purpose of contributing to the financing of nuclear power stations and industrial fuel cycle installations⁽³³⁾.
- (b) Council guidelines of 29 March 1977 to the Commission, which are contained in the minutes of the Council meeting of 29 March 1977.
- (c) Cooperation Agreement⁽³⁴⁾, between the Commission and the EIB, concerning the practical implementation of the Council decision and guidelines.

Notification of investment

4.7. Under the investment notification procedure foreseen in Articles 41 to 44 of the Euratom Treaty, an undertaking engaged in the industrial activities listed in Annex II of the Treaty⁽³⁵⁾ communicates to the Commission, and for information purposes to the Member State in whose territory the proposed investment is located, investment projects relating to new installations and also to replacements and conversions. The Commission's Directorate-General

⁽³²⁾ Article 6, Council Regulation (EEC) No 398/75 of 17 February 1975 (OJ No L 46, 20. 2. 1975).

⁽³³⁾ OJ No L 88, 6. 4. 1977.

⁽³⁴⁾ EIB's letter of 5 August 1977 and the Commission's reply of 11 October 1977.

⁽³⁵⁾ Euratom Treaty, Annex II, lists amongst others 'nuclear reactors of all types and for all purposes'.

⁽³¹⁾ Established by Article 105 (2) of the EEC Treaty.

for Energy (DG XVII) examines the proposed investment and submits its opinion to the Commission. The Commission, following consultations with the undertaking, communicates its views to the Member State in question.

Application for a Euratom loan

4.8. Should the undertaking in question consider the possibility of a Euratom loan to finance part of the investment, discussions take place between DG XVII (Energy), DG XVIII (Credit and Investments), the EIB and the promoter's own bankers. If the undertaking then makes a formal application for a Euratom loan, the Commission submits the project to the EIB for an opinion in accordance with points 2 and 3 of the Cooperation Agreement.

Eligibility criteria

4.9. The criteria applied to projects to determine their eligibility for a Euratom loan are contained in the Council Decision 77/270/Euratom of 29 March 1977, and the Council's policy guidelines to the Commission⁽³⁶⁾.

(a) Community policy criteria:

the project:

- (i) must be notified to the Commission in accordance with the procedures outlined in Articles 41 to 44 of the Euratom Treaty;
- (ii) must satisfy, in the opinion of the Commission, the objectives and criteria of the Communities' energy and environmental policies;
- (iii) must relate to the industrial production of electricity in nuclear power stations and to industrial fuel cycle installations;
- (iv) must be in accordance with Community competition policies.

Priority is given to projects involving several Member States.

(b) Financial criteria:

- (i) The enterprise responsible for the project must be financially sound in the Commission's view, following the EIB's opinion.

(ii) First-class guarantees and security must be available.

(iii) Euratom loans are limited to 20% of the total cost of the project.

(iv) Since frequently a nuclear energy development project may benefit from both Euratom and EIB loans, a maximum percentage of total Community financing for any one project may be fixed.

These criteria are supplemented by the EIB's own criteria which it applies for the examination of the project. The conclusions of the EIB's analysis are incorporated in its recommendation to the Commission.

EIB's role

4.10. The EIB may receive an application for a Euratom loan either via the Commission or directly as part of an application for finance addressed to the EIB. In the latter case, the EIB shall inform the Commission.

The Cooperation Agreement for Euratom stipulates that the EIB shall apply the same financial, economic and technical criteria in assessing the merits of a project for a Euratom loan as it does in considering that same project for an EIB loan. These EIB criteria are not, however, specified in the Cooperation Agreement.

The EIB has a period of two months within which to give its recommendation to the Commission on a Euratom loan for a project. In general, a project which receives a Euratom loan has already, or will, benefit also from an EIB loan.

Commission's role

Commission's EIB Inter-Service Group

4.11. The EIB's opinion on a project for a Euratom loan is reviewed by the Commission's EIB Inter-Service Group. This permanent Inter-Service Group was created by the Commission in 1975 to deal with the developing contacts between it and the EIB. It acts as an advisory body to the Commission and whilst its opinion is non-binding on the Commission, it nevertheless plays a key role in the decision-making process within the Commission.

⁽³⁶⁾ Council minutes of 29 March 1977 on the implementation of the Euratom Decision 77/270/Euratom.

The Group is composed of the representatives of 18 Directorates-General within the Commission, including the Commission's financial controller. DG II is both chairman and secretary of the Group.

It examines all projects submitted to the Commission by the EIB either for a Commission opinion, as is the case with EIB loans in conformity with Article 21 of the EIB's Statutes, or for a Commission Euratom loan decision or eligibility decision for NCI loans and EMS interest rate subsidies.

The Commission's EIB Inter-Service Group does not, as standard practice, maintain minutes of its meetings. However, where there are conflicting opinions on a project within the Inter-Service Group, the written submissions of the Directorates-General concerned are circulated to the members of the Group.

The Commission's decision-making procedures, following the submission of the Inter-Service Group's opinion on a project, vary according to the mechanism in question be it an EIB, NCI or Euratom loan or EMS interest subsidy.

Commission's decision on Euratom loan

4.12. If the Commission's EIB Inter-Service Group, having studied the EIB's recommendation and examined the project from their respective viewpoints, decides unanimously to give a favourable opinion on a Euratom loan for the project, then the Commission's approval is by 'written' procedure introduced by DG XVIII. The DG XVIII proposal to the Commission incorporates:

- (a) a description of the project;
- (b) the EIB's recommendation;
- (c) reference to the Inter-Service Group's opinion.

If opinion is divided within the EIB Inter-Service Group then the decision is taken at a Commission meeting. Following the Commission's decision to grant a loan, DG XVIII is authorized to contract the necessary borrowings.

New Community Instrument mechanism

4.13. The procedures relating to loan decisions under the 1978 NCI mechanism are defined in the following documents, which indicate the respective

responsibilities of the Council, Commission and EIB:

- (a) Council Decision 78/870/EEC of 16 October 1978⁽³⁷⁾;
- (b) Statutes of the European Investment Bank⁽³⁸⁾;
- (c) Cooperation Agreement of 27 November 1978 between the EIB and the Commission, including the annexed explanatory note to the Agreement of the same date.

EMS interest rate subsidies of 3% may be granted on NCI and EIB loans⁽³⁹⁾ for eligible projects in Italy and Ireland⁽⁴⁰⁾. These subsidies, which are financed by the Commission budget, were established in 1979 and the annual budgetary appropriations are fixed at 200 million EUA. The procedures relating to these subsidies are outlined in paras 4.24 to 4.34.

4.14. The introduction in 1980 and 1981 by the Council of NCI loans for projects in the earthquake-affected areas of Italy and Greece has added a further dimension to the NCI mechanism. Although the allocation of responsibilities for these loans between the Commission and the EIB remains unaltered, there are differences in the decision-making procedures. These differences, when compared to the procedures for the 1978 NCI loan mechanism, are outlined in para. 4.23.

These loans automatically benefit from annual interest rate subsidies of 3% over a maximum period of 12 years. Again differences in procedures for these interest rate subsidies, when compared to the procedures for EMS interest subsidies, are outlined in paras 4.35 to 4.36.

Application for an NCI loan

4.15. All applications for NCI loans are submitted to the EIB either directly, or through the Commission or the Member State. The Commission is then requested by the EIB to give its decision on the eligibility of the project for an NCI loan.

Eligibility criteria

4.16. Article 2 of the 1978 Council Decision on the NCI states that the Council, acting unanimously,

⁽³⁷⁾ OJ No L 298, 25. 10. 1978.

⁽³⁸⁾ Protocol on the Statute of the EIB, EEC Treaty.

⁽³⁹⁾ Council Regulation (EEC) No 1736/79 of 3 August 1979 (OJ No L 200, 8. 8. 1979).

⁽⁴⁰⁾ Council Decision 79/691/EEC, implementing Council Decision 1736/79 (OJ No L 200, 8. 8. 1979).

shall authorize each tranche of NCI borrowings and lay down the guidelines by which the Commission shall decide on the eligibility of projects for NCI loans. The eligibility guidelines which the Council fixed for the two borrowing tranches totalling 1 000 million EUA authorized to date (31 December 1981) for the NCI, were as follows:

- (a) the investment must be consistent with Community rules applicable in the relevant areas;
- (b) the investment must contribute to resolving the Community's main structural problems, and, in particular to reducing the regional imbalances in the Community and to improving the employment situation.

In addition to these eligibility guidelines, the Council also decided for each borrowing tranche the types of investments which were to be granted NCI loans in the energy, infrastructure and industrial sectors ⁽⁴¹⁾.

Commission's role

Inter-Service Group

4.17. All requests, communicated to the Commission (DG II) by the EIB, for a decision on the eligibility of a project for an NCI loan, are sent to the Commission's EIB Inter-Service Group for opinion. Within the Group, DG XVI (Regional Policy) and DG XVII (Energy) have been delegated particular responsibility for the examination of the infrastructure and energy projects, respectively.

In the 1979-1981 period the EIB's request to the Commission for a decision on the eligibility of a

project for an NCI loan has frequently been preceded by an EIB request to the Commission for an opinion on a EIB loan for that same project.

4.18. Apart from information individual Directorates-General of the Commission may have procured on a proposed project due to regular contact with National Administrations and organizations within Member States, two basic documents, which are communicated by the EIB to DG II, form the basis of the Group's appreciation of a project:

- (a) EIB's information note to the Commission requesting the latter's opinion on an EIB loan for a project. This note gives a general description of the project;
- (b) EIB note to the Commission requesting for the same project, the Commission's eligibility decision for an NCI loan.

This note

- (i) updates briefly the nature of the project (e.g. changes in timetable for completion of project, modifications, etc.),
- (ii) indicates why the EIB considers the project eligible for an NCI loan,
- (iii) outlines the general financing plan, by indicating the percentage participations of EIB, NCI, other Community funds and State funds,
- (iv) indicates the amount of EIB loans already granted to the project.

Commission's decision on eligibility

4.19. Article 2 of the 1978 Council Decision stipulates that the Commission shall decide whether or not projects are eligible for NCI loans in accordance with the eligibility guidelines (see 4.16 above) laid down by the Council. If the Inter-Service Group gives a favourable opinion on a project, then the Commissioner with responsibility for the Economic and Financial Affairs Directorate takes the NCI eligibility decision on behalf of the Commission. If opinion within the Group is divided, then the project is discussed and decided at Commission level.

⁽⁴¹⁾ Article 2, Council Decision 79/486/EEC of 14 May 1979 (OJ No L 125, 22. 5. 1979), and Article 1, Council Decision 80/1103/EEC of 25 November 1980 (OJ No L 326, 2. 12. 1980).

Energy investment covers projects which contribute to greater self-sufficiency, security and diversification of Community energy supplies and which ensure the development, exploitation, transportation and storage of energy supplies, with particular attention being paid to energy conservation and to the development of alternative energy sources.

Infrastructure investment covers transport, telecommunications, agricultural improvements, water supply works and environmental protection.

Industrial investment covers factories constructed with a view to future requirements and housing, provided that they form part of a total project of economic and industrial development presenting a regional interest.

If the Commission eligibility decision is negative, then no NCI loan may be granted by the EIB to the project; if the decision is positive, then the EIB examines and decides whether and on what terms to grant the loan.

EIB's role

4.20. If the Commission declares a project eligible for an NCI loan then it is the EIB which decides whether or not to grant the loan. The EIB decision is taken in conformity with its own statutes and usual criteria⁽⁴²⁾. It applies the same criteria in examining projects for NCI loans as it does for EIB loans.

If the project is eligible for both EIB and NCI loans then the EIB determines the appropriate financing for the project⁽⁴³⁾:

- (a) whether an NCI loan only;
- (b) whether an EIB loan only;
- (c) whether EIB + NCI loans and their respective shares.

This provision is significant since, apart from minor exceptions, all projects which have received an NCI loan up to 31 December 1981, have also received an EIB loan.

4.21. The loan decisions are taken by the EIB's board of directors acting on the proposal of their management committee. The members of the board of directors are nominated by the Member States⁽⁴⁴⁾ and the Commission also nominates a director to the board. If the management committee should decide not to recommend to the board of directors an NCI loan for a project which the Commission has already declared eligible, then the EIB informs the Commission of the decision. The Commission may then consult with the EIB and delegate an official to examine the dossiers. The management committee, however, retains the right to maintain its position⁽⁴⁵⁾. The Court understands that this situation has not occurred up to 31 December 1981. Where the EIB does decide to grant an NCI loan,

the loan contract is signed by both the EIB and Commission.

4.22. Point 3.1 of the explanatory letter annexed to the Cooperation Agreement acknowledges that it is the Commission which decides on the eligibility of projects as stipulated in the Council decision on the NCI. However, it also states that since the EIB examines and processes the individual projects with the potential loan beneficiaries then the smooth functioning of the NCI mechanism is dependent on the EIB's services being able to pronounce *a priori* on the eligibility of projects presented for NCI loans. The EIB therefore sought within the terms of the Agreement indications as to how the Commission would interpret the Council's eligibility guidelines, namely, reducing regional imbalances and the level of unemployment by identifying the type of project, its siting and the desired socio/economic impact of the project. The Commission has not made explicit these criteria.

NCI 'earthquake' loans

4.23. The procedures for the NCI 'earthquake' loans are modelled on those in force for the 1978 NCI decision as outlined in paras 4.13 to 4.22 above, namely, the Commission decides on eligibility, the EIB decides on whether or not to grant the loan.

To date, 31 December 1981, only the NCI loans to Italian earthquake-affected areas have been the subject of a Cooperation Agreement on the practical implementation of the Council Decision of 20 January 1981.

There have in effect been two Cooperation Agreements:

- (i) a tripartite Cooperation Agreement between Italy, the EIB and the Commission, dated 3 February 1981;
- (ii) a bilateral Cooperation Agreement dated 30 March 1981 between the EIB and the Commission incorporating additional provisions to those contained in the Cooperation Agreement on the NCI dated 27 November 1978 (see para. 4.13).

An additional provision included in the Cooperation Agreement of 30 March 1981 foresees that where a project, which has already been granted an NCI loan by the EIB, is either partially or totally not completed, then the Italian Ministry of the Treasury may substitute another project with the agreement of the EIB and Commission.

⁽⁴²⁾ Article 5, Council Decision 78/870/EEC of 16 October 1978 (OJ No L 298, 25. 10. 1978) and Cooperation Agreement, EIB/Commission of 27 November 1978, para. 9, explanatory letter to the Cooperation Agreement of 27 November 1978, point 5.1

⁽⁴³⁾ Cooperation Agreement of 27 November 1978, para. 10.

⁽⁴⁴⁾ Statute of the EIB, Article 11 (2).

⁽⁴⁵⁾ Point 5.2 of explanatory letter annexed to the Cooperation Agreement.

European Monetary System's interest rate subsidies

4.24. The decision-making procedures with regard to the EMS interest rate subsidies are defined in the following documents, which delineate the respective responsibilities of the Commission, EIB and Member State:

- (a) Council Regulation (EEC) No 1736/79 of 3 August 1979 on interest subsidies for certain loans under the European Monetary System⁽⁴⁶⁾;
- (b) Council Decision 79/691/EEC of 3 August 1979, implementing the above Regulation⁽⁴⁷⁾;
- (c) Cooperation Agreement of 17 September 1979, between the Commission and the EIB.

4.25. The Council decided⁽⁴⁸⁾ that Ireland and Italy fulfilled the dual conditions of being the least prosperous Member States as well as fully and effectively participating in the European Monetary System. Therefore, up to 31 December 1981, only EIB and NCI loans for eligible projects in Italy and Ireland have benefited from the EMS interest subsidies.

4.26. The Council decided in order to facilitate the selection of projects which might benefit from interest subsidies that the Member States, in conjunction with the Commission, would establish indicative programmes which would specify in particular, the overall amount and the categories of investment aimed at⁽⁴⁹⁾.

To respect this provision, the Member States concerned (Italy and Ireland) initially submitted their regional development programmes for their infrastructure sector to the Commission.

Eligibility criteria

4.27. The eligibility guidelines for interest rate subsidies, which are defined in Article 5 of Council Regulation (EEC) No 1736/79 of 3 August 1979, are as follows:

- (a) the investment shall be consistent with the Community rules applicable in the relevant sectors;

⁽⁴⁶⁾ OJ No L 200, 8. 8. 1979.

⁽⁴⁷⁾ OJ No L 200, 8. 8. 1979.

⁽⁴⁸⁾ Council Decision 79/691/EEC of 3 August 1979 (OJ No L 200, 8. 8. 1979).

⁽⁴⁹⁾ Article 3, Council Regulation (EEC) No 1736/79 of 3 August 1979.

- (b) the loans shall be concentrated on the financing of infrastructure projects and programmes;
- (c) the investment shall contribute to resolving the structural problems affecting the State concerned and, in particular, to reducing regional imbalances and to improving the employment situation;
- (d) the investment shall be compatible with the provisions of the Treaty governing competition.

These criteria to a certain degree reflect the eligibility guidelines for NCI loans (see para. 4.16).

Selection of projects

4.28. The initial pre-selection of projects is undertaken by the EIB in conjunction with the Member State concerned.

This is indicated by Article 4 of Council Regulation (EEC) No 1736/79 which states:

'Applications for interest subsidies provided for in this Regulation shall be submitted for the opinion of the Member State on the territory of which the project is to be carried out';

and by the clause in the Cooperation Agreement which states:

'When the EIB receives, in accordance with its statutes, a loan request relating to a project which at first sight would qualify for a loan subsidy... the EIB will request from the Member State concerned an opinion on the loan and from the Commission the decision on the eligibility for an interest subsidy'⁽⁵⁰⁾.

Member State opinion

4.29. Following this pre-selection of projects to be considered for interest subsidies, the EIB requests the opinion of the Member State, on whose territory the project is to be carried out. If the Member State opinion is favourable⁽⁵¹⁾, then the EIB requests the Commission eligibility decision on the project. The granting of an interest rate subsidy is therefore conditional on the Member State's favourable opinion.

⁽⁵⁰⁾ Article 6, Cooperation Agreement, 17 September 1979.

⁽⁵¹⁾ Article 5, Council Regulation (EEC) No 1736/79 of 3 August 1979 (OJ No L 200, 8. 8. 1979).

*Commission's role***Inter-Service Group**

4.30. Where the Member State's opinion is favourable, the EIB submits the project to the Commission for a decision on its eligibility. The project is examined by the Inter-Service Group to establish its conformity with the eligibility guidelines. In its request to the Commission for an eligibility decision, the EIB refers, where applicable, to previous Commission decisions and opinions on NCI and/or EIB loans for the same project.

Commission's decision on eligibility

4.31. If the Inter-Service Group gives an unanimously favourable opinion on eligibility, then the Commissioner with responsibility for Economic and Financial Affairs (DG II) is delegated to decide on behalf of the Commission and communicate this decision to the EIB. If the opinion is not unanimous within the Group, then the project is discussed and decided at Commission level.

Should the Commission decide that a project is eligible, then this decision will result in a commitment on the Commission budget if the following conditions are respected;

- (a) the loan contract, be it EIB or NCI, will be signed;
- (b) on signature, the Member State is still a Member of the EMS;
- (c) the budgetary appropriations are available.

If the Commission decides that a project is not eligible, then no EMS interest rate subsidy may be granted to that project by the EIB should the project receive an NCI or EIB loan.

EIB's role

4.32. The initial pre-selection of projects by the EIB in conjunction with the Member State has already been referred to in para. 4.28. The eventual decision by the EIB to grant a subsidized loan in accordance with Article 6 of Council Regulation (EEC) No 1736/79 is conditional however on:

- (a) the Member State opinion being favourable;

- (b) if so the Commission deciding that the project is eligible.

It is then at the discretion of the EIB's board of directors, acting on a proposal of its management committee, to take the decision on whether to grant the project a subsidized loan, as outlined in para. 4.21.

4.33. If the EIB decides to grant the subsidized EIB or NCI loan, it informs the Commission of the date of signature of the contract. Within two months of the contract date, the Commission is obliged to transfer the amount calculated by the EIB as the interest subsidy, provided the conditions referred to in para. 4.31 have been respected.

4.34. In the period 1979-1981, an average of 88 % of EMS interest rate subsidies was allocated to EIB loans, whilst 12 % was granted to NCI loans.

Interest rate subsidies on NCI and EIB 'earthquake' loans to Italy and Greece

4.35. As stated in para. 4.23, a Cooperation Agreement between the Commission and the EIB has only been made for loans to Italian earthquake-affected areas. There were no payments of interest rate subsidies from the Commission budget in 1981 for either EIB and NCI 'earthquake' loans to Italy, although loan contracts were concluded.

4.36. The decision-making procedures for these interest rate subsidies differ from those of the EMS interest rate subsidies in the following respects:

- (i) the submission by the Member State to the EIB of a project for an EIB or NCI loan constitutes its favourable opinion on the project for a subsidy⁽⁵²⁾;
- (ii) it is the Commission which decides on the granting of the interest rate subsidy in contrast to the EMS subsidies where the Commission only decides on eligibility⁽⁵³⁾;
- (iii) there are no separate eligibility criteria associated with these interest subsidies in contrast with the EMS interest subsidies. This is because

⁽⁵²⁾ Article 4, Tripartite Cooperation Agreement of 3 February 1981.

⁽⁵³⁾ Article 3, Council Decision 81/19/EEC of 20 January 1981 (OJ No L 37, 10. 2. 1981).

a project in an earthquake-affected zone which is granted an NCI and/or EIB loan, automatically benefits from the annual interest rate subsidy of 3 % ⁽⁵⁴⁾;

- (iv) if a project is either partially completed or not undertaken, the Italian Ministry of the Treasury may substitute another project which, if agreed by the Commission and EIB, will receive not only the loan but also the interest subsidy granted to the project originally agreed ⁽⁵⁵⁾.

These interest rate subsidies also differ in relation to their method of calculation and means of disbursement by the Commission and these differences are examined in paras 5.20 and 5.36.

Observations

Euratom loans

4.37. Whilst the decision-making procedures at the Commission in their formal aspects are quite clear, the nature of the Commission's services examination is difficult to analyze in view of the absence of minutes of the Commission's EIB Inter-Service Group's meetings (see para. 4.17).

Due to this absence of minutes, it is not clear on what basis the Commission's EIB Inter-Service Group evaluates the EIB's recommendation on a project since the EIB's specific (economic, financial and technical) evaluation criteria for projects are not explicit in the Cooperation Agreement. Within the context of the decision-making framework agreed by the Commission and the EIB, the Court considers that the EIB's evaluation criteria should be explicitly outlined in the Cooperation Agreement.

NCI loans

4.38. The decision-making procedures relating to an NCI loan for a project consist essentially of two phases:

- (i) the Commission decision on the eligibility of the project for an NCI loan;

- (ii) if that Commission decision is favourable, the EIB decision on whether or not to grant the NCI loan.

With regard to (i), the Cooperation Agreement's explanatory letter included the provision whereby the EIB would be informed by the Commission in objective terms of its interpretations of the Council's eligibility guidelines, namely, the reduction of regional imbalances and the level of unemployment. The Court has been informed by the Commission that the EIB has not invoked this provision and that the Commission has not explicitly established such criteria.

The eligibility guidelines decided by the Council for NCI loans are of a general nature. The Court considers therefore that the Commission, when it interprets these guidelines, should define the eligibility criteria it applies to assess whether a project conforms or not to the Council's guidelines. The elaboration of such criteria should precede the Commission's decision-making process and, in particular, the examination by the Commission's EIB Inter-Service Group.

4.39. It is difficult to analyze the nature of the Commission's Inter-Service Group's evaluation of projects for NCI loans and whether the evaluation is carried out by reference to criteria agreed within the Group but not documented. This is due to several factors.

Firstly, as already indicated, the Commission has not defined the criteria it uses to interpret the Council's eligibility guidelines.

Secondly, neither DG XVI (Regional Policy) nor DG XVII (Energy) make a written report to the Group of their detailed examination of the infrastructure and energy projects.

Thirdly, the minutes of the Inter-Service Group's meetings consist of a list of decisions taken (i.e. favourable, unfavourable, reserve, etc.) with no commentary on projects examined.

4.40. To date, loans granted under the NCI mechanism to projects have complemented the loans granted by the EIB under its own system. This is evidenced by the fact that in the period 1979-1981, nearly all the NCI loans granted were to projects which already had benefited, or were in the course of benefiting, from EIB loans. This occurrence is not accidental but rather reflects the following elements.

⁽⁵⁴⁾ Article 2, Council Decision 81/19/EEC of 20 January 1981 (OJ No L 37, 10. 2. 1981).

⁽⁵⁵⁾ Article 6, Tripartite Cooperation Agreement of 3 February 1981.

Firstly, the fact that the EIB, in addition to deciding on its own loans, also decides on the NCI loans.

Secondly, the fact that the EIB applies the same financial, economic and technical criteria in its assessment of projects for both NCI and EIB loans.

Thirdly, the similarity between the NCI's eligibility guidelines, i.e. reducing regional disparities and the level of unemployment, and the EIB's tasks i.e. granting loans and guarantees which facilitate the financing of projects for developing under-developed regions.

Fourthly, the fact that the Commission has not made explicit its own interpretations of the Council's general eligibility guidelines.

Fifthly, the close resemblance between the sectors and regions identified for investment under both the NCI and EIB systems.

From the foregoing the NCI mechanism appears equivalent all but in name to the EIB own resources loans, except that for the NCI it is the Commission which borrows the necessary funds.

4.41. The present allocation of responsibilities for the NCI mechanism is that the Commission borrows the funds and decides on the eligibility of projects, whilst the EIB decides on whether or not to grant NCI loans to those projects. Following an NCI loan decision by the EIB, which may occur only after a positive Commission eligibility decision, the Commission is obliged to co-sign with the EIB the NCI loan contract according to point 7.1 of the letter accompanying the Cooperation Agreement.

The Court considers that it would be preferable if the Commission was allocated also the responsibility for deciding on the granting of the NCI loans. Such an allocation of responsibilities would be more logical and consistent with that in force for the Euratom mechanism under which the Commission borrows the funds, decides on the loans to be granted, whilst the EIB acts as the Commission's agent by analyzing the projects and administering the loans granted.

Apart from being a more logical and consistent allocation of responsibilities, it would also reflect the Commission's financial responsibility for the borrowings it contracts under the NCI mechanism on behalf of the Community, a responsibility reflected in the token-entry in the Commission section of the Community budget as well as by the following articles.

Article 5 of Council Decision 78/870/EEC of 16 October 1978 states:

'The Bank shall carry out the transactions under this mandate on behalf of, for and at the risk of the Community.'

Point 17 of the Cooperation Agreement states:

'The Bank's responsibility is limited to the correct execution, in conformity with banking practice, of the abovementioned duties.'

Point 8.1 of the explanatory letter annexed to the Cooperation Agreement, dated 17 October 1978, between the Commission and the EIB states:

'It will be necessary for the Community budget to assume responsibility for the delays in the transfer of capital repayments and interest payments.'

With regard to the Commission's replies (Annex 2) the Court wishes to underline that its remarks envisage a rationalization of the decision-making procedures for the loans and borrowings mechanisms. This rationalization would mean that the same allocation of responsibilities would apply to the NCI mechanism as have applied to the Euratom mechanism since 1977, i.e. the Commission borrowing and deciding on the granting of the loans, and the EIB acting in an advisory role.

The Court, furthermore, is not convinced of the arguments made by the Commission in its reply with regard to the so-called significant differences between the Euratom and NCI mechanisms. The Commission reply ignores the fact that the EIB plays an important role for the Euratom mechanism, firstly, by giving its opinion on projects to the Commission and secondly, by administering the loans granted. In the Court's view, the EIB could equally well exercise these functions for the NCI.

4.42. Identical considerations apply for the NCI 'earthquake' loans to Italy and Greece with regard to the allocation of the decision-making powers for the loans (see para. 4.41).

The Council Decision, dated 15 March 1982, on the NCI mechanism which authorized the Commission to borrow 1 000 million ECU to finance NCI loans, incorporates the same division of responsibilities as under the 1978 NCI mechanism⁽⁵⁶⁾.

⁽⁵⁶⁾ Council Decision 82/169/EEC of 15 March 1982 (OJ No L 78, 24. 3. 1982).

EMS interest rate subsidies

4.43. After the initial selection of projects by the EIB as foreseen in the Cooperation Agreement, the decision-making procedures relating to EMS interest subsidies consist essentially of three phases:

- (a) the Member State opinion on an interest subsidy for the project;
- (b) if that Member State opinion is favourable, the Commission eligibility decision on the project;
- (c) if the eligibility decision is favourable, the EIB decision whether to grant the project a subsidized loan, the subsidy being financed directly from the Commission budget.

4.44. The Court, having reviewed the decision-making procedures in force, is of the opinion that the initial pre-selection of projects for consideration for interest rate subsidies, prior to any eligibility decision, should be made by the Commission rather than the EIB, since it relates to budgetary appropriations. Furthermore, the following aspects should be clarified:

- (i) the criteria used in that initial pre-selection of projects;
- (ii) the criteria used in allocating the total annual budgetary appropriations (200 million EUA) for the EMS interest rate subsidies between NCI loans and EIB loans;
- (iii) the criteria, as with the NCI loans, used in assessing the conformity of projects submitted with the Council's eligibility guidelines.

With regard to (i) and (ii) above, there is a selection of projects. The eligibility criteria for NCI loans and EMS interest rate subsidies are similar; the EIB's assessment criteria for NCI and EIB loans are identical; all EIB and NCI loans granted to Italy and Ireland for infrastructure investment are theoretically eligible for EMS interest rate subsidies. However, not all EIB and NCI loans for Italian and Irish projects receive interest rate subsidies. A selection is required therefore if only due to the level of annual budgetary appropriations (200 million EUA) available.

4.45. The present allocation of responsibilities, with regard to EMS interest rate subsidies between the Commission and the EIB raises a problem of principle. The EMS interest subsidies are financed by the Commission part of the Community budget. Therefore, in accordance with Article 205 of the EEC Treaty, the Commission is responsible for the implementation of that budget on its own responsibility and within the limits of the appropriations.

However, neither the Council decision nor the Cooperation Agreement for the EMS interest rate subsidies state that the Commission shall decide on the subsidies, rather they stipulate that the Commission decides on eligibility and the EIB decides on the subsidized loans. The Commission eligibility decision may, and generally does, result in the granting of the interest subsidy. It is the EIB, by its decision on whether or not to grant an NCI or EIB loan to a project, which in effect determines whether, and to what extent, the Commission's budgetary appropriations are utilized ⁽⁵⁶⁾.

The Court asks the Commission whether this situation is not in contradiction with Article 205 of the Treaty. It may not be rectified simply by amending the Council Decision to indicate explicitly that the Commission shall decide on the subsidies. Rather it requires a re-allocation of the decision-making powers for the NCI loans from the EIB to the Commission as recommended by the Court in para. 4.41.

The Court wishes to point out in reply to the Commission's remarks (Annex 2) that once the Commission has given its eligibility decision, it has little discretionary power over the volume of interest rate subsidies paid in any period. If the 'three conditions' are considered, then only one is dependent on the Commission namely, attesting to the availability of appropriations. With regard to the signature of the loan contracts, that is entirely at the discretion of the EIB for its own loans (88 % of appropriations on

⁽⁵⁶⁾ Article 8 of the Cooperation Agreement states that a favourable eligibility decision taken by the Commission implies a commitment on the Community budget on condition that (a) the loan contract is signed, (b) the Commission has not notified the Bank that the Member State concerned has ceased to participate fully and effectively in the European Monetary System or has not fulfilled other condition included in the Regulation, and (c) that the budget appropriations required for the payment of the interest rate subsidy are sufficient.

EMS interest rate subsidies 1979-1981) whilst for NCI loans, once the Commission has given a favourable eligibility decision for an NCI loan for a project, it is obliged to co-sign the loan contract with the EIB as already noted (4.41, first paragraph). With regard to the condition as to whether the Member State is effectively and fully participating in the EMS, then this is also clearly outside the scope of the Commission.

Interest rate subsidies on NCI and EIB 'earthquake' loans

4.46. Whilst the provisions of the Council Decision on interest rate subsidies for Italy, in comparison with the Council Regulation on EMS interest rate subsidies, would appear to be more precise by stating that the Commission shall grant the interest subsidies, in reality the same situation is valid as for the EMS subsidies.

Firstly, all EIB and NCI loans to the earthquake-affected areas automatically benefit from interest rate subsidies, unlike the EMS subsidies where only certain loans to Italy and Ireland may benefit.

Secondly, and conditional on the availability of budgetary appropriations, it is the EIB decision to grant the NCI or EIB loans which determines whether the interest rate subsidy applies and if so to what extent.

Whilst in this case the formal power to decide on the granting of interest rate subsidies is for the Commission and thus the Treaty's provisions (Article 205) are respected, nevertheless it is the EIB loan decision which effectively determines whether the Commission's budgetary appropriations for the interest rate subsidies are utilized. The same considerations as in para. 4.41 therefore apply with regard to the re-allocation to the Commission from the EIB of the power to decide on the NCI loans.

CHAPTER 5

FINANCIAL MANAGEMENT OF THE MECHANISMS

Summary

5.1. This chapter outlines the financial and administrative procedures, which follow as a result of the loan decisions described in Chapter 4. These arrangements, in common with the decision-making procedures, vary from one mechanism to another and are essentially dependent on:

- (i) the Council decision establishing the mechanism, with regard to the overall allocation of responsibilities, and
- (ii) the bilateral Cooperation Agreements, with regard to the practical implementation of the Council's decision,
- (iii) internal management arrangements decided by the Commission.

Balance of payments mechanism

Borrowings

5.2. All the BP borrowings granted to date, 31 December 1981, were contracted in the 1976-77 period. These borrowings, which financed the BP loans to Member States, were initially negotiated by

the Directorate of Economic and Financial Affairs (DG II) on behalf of the Commission. As noted in paras 4.3 to 4.6, the terms concluded, notably, the interest rate and duration, were identical for both the borrowing and loan contracts.

Administration of the mechanism

5.3. Although the Commission undertakes the borrowings it is not responsible for the treasury and accounting functions relating to the BP mechanism. The Council assigned the responsibility for making the necessary arrangements for the administration of the BP loans and borrowings to the European Monetary Cooperation Fund (EMCF)⁽⁵⁷⁾. The EMCF in turn, appointed an agent⁽⁵⁸⁾ the Bank of International Settlements (BIS), to carry out the actual administration.

⁽⁵⁷⁾ Article 10, Council Regulation (EEC) No 398/75 implementing Council Regulation (EEC) No 397/75 concerning Community loans.

⁽⁵⁸⁾ EMCF's statutes, Article 3, 'The Board of Governors (of the EMCF) may delegate to an agent the responsibility for the execution of technical aspects of the Fund's operations'.

5.4. On signature of the borrowing and loan contracts by the Commission, the lending banks transfer the funds directly to the Bank of International Settlements (BIS), for disbursement to the central bank of the beneficiary Member State. Similarly, the Member States' repayment of capital and payments of interest and expenses are transferred direct by the central bank to the BIS for subsequent transfer to the lending banks. Therefore, neither the funds borrowed and lent by the Commission, on behalf of the Community, nor the debt servicing operations related to those borrowings and loans, pass through the Commission's treasury and accounts at any stage.

5.5. The EMCF issued a directive in March 1976 to its agent, the BIS, on the administration of the BP loans and borrowings, under which the Commission receives from the BIS for each transaction relating to the repayment and servicing of a BP loan and borrowing⁽⁵⁹⁾:

- (i) copies of telexes sent to the central banks of the beneficiary Member States indicating the due dates for payment of capital and/or interest;
- (ii) written confirmation of the receipt by the BIS from the Member State(s) of the amounts due and their subsequent transfer by the BIS, on behalf of the Commission, to the lending banks;
- (iii) bank statements relating to the BIS accounts, showing the transfer from the central bank to the BIS's accounts and subsequent transfer from the BIS to the lending banks.

5.6. The annual report prepared by the BIS on BP loans and borrowings is submitted to the EMCF's board of governors for approval. A Member of the Commission, or its representative, may be present at the board of governors' meeting in conformity with Article 1 of the EMCF's statute. The EMCF then transmits the report to the Commission, requesting

⁽⁵⁹⁾ Article 6

'15 working days before each due date (for capital and/or interest payments) the Agent shall, in the name of the Fund give notification thereof to the Central Bank of the country which is in debt to the Community.'

Article 7

'The agent shall, in the name of the Fund, immediately inform the Commission (DG II) of the operations it has carried out for the account of the Community.'

Article 8

'The agent shall prepare and deliver to the Board (of the EMCF) the report, which the Fund is to draw up at the end of each calendar year for the information of the Commission, on the financial operations it has carried out during the year in connection with borrowing and lending operations.'

the latter's approval of the report within one month. This report details:

- (i) receipts and payments for each loan granted and borrowing contracted;
- (ii) loans and borrowings outstanding at the year-end.

Euratom and NCI mechanisms

Borrowings

5.7. Under both the Euratom and NCI mechanisms the Council authorizes the Commission to undertake the necessary borrowings. The proceeds of those borrowings then finance the corresponding Euratom and NCI loans. The Commission delegates to DG XVIII (Credit and Investments) the responsibility for negotiating and contracting the required borrowings on behalf of the Commission.

Administration of the mechanisms

NCI and Euratom borrowings

5.8. Once the borrowings are concluded, DG XVIII is then responsible for the administration of these Euratom and NCI borrowings. This involves the servicing of the debt by the interest payments, capital repayments and the payment of other associated costs. For this purpose, DG XVIII maintains its own bank accounts and these accounts are separate from the accounts under the responsibility of the Commission's accounting officer.

NCI and Euratom loans

5.9. The EIB carries out the administration of both the Euratom and NCI loans. With regard to Euratom loans, the Commission in 1977 granted a mandate to the EIB for the latter to act as Euratom's agent in the administration of the loans. Whereas the responsibility for the administration of the NCI loans was granted to the EIB by the Council decision which established the NCI mechanism in 1978.

5.10. On conclusion of the borrowing contracts for either Euratom and NCI, the funds are transferred to the EIB by DC XVIII for disbursement by them

as Euratom or NCI loans to the beneficiaries. The EIB then ensures:

- (a) the receipts of capital repayments and interest payments;
- (b) the transfer of the amounts received (less the EIB commission) to the Commission, so that the latter in turn may service its borrowings and make repayments.

The EIB receives 0.125 % per annum on the outstanding balance of the loan as commission for its services and this commission is included in the interest rate charged on the Euratom or NCI loan to the promoter. The Commission does not therefore incur this expense itself.

5.11. Within the context of its mandate as Euratom's agent and in accordance with point 6 of the Cooperation Agreement, the EIB submits an annual report to the Commission on the execution of the mandate. The Commission itself submits to the Council and the European Parliament an annual review of its borrowing policy together with the budget estimates⁽⁶⁰⁾.

The Commission prepares, in conjunction with the EIB, an annual report on the NCI which is transmitted to the Council and Parliament.

Accounting systems

5.12. DG XVIII maintains its own accounting system for both Euratom loans and borrowings since it is responsible for the decision making on both the loans and borrowings. However, for the NCI, DG XVIII holds an accounting system for the borrowings only, since the loans are the responsibility of the EIB.

Financial control

5.13. The approval of the Commission's financial controller is not sought by DG XVIII for the contracts on the loans and borrowings concluded under the Euratom and NCI mechanisms.

5.14. The financial transactions associated with the Euratom and NCI mechanisms and carried out by DG XVIII are not subject to the approval of the Commission's financial controller.

NCI 'earthquake' loans

5.15. Since these loans are being granted within the general framework of the New Community Instrument (NCI) as established in 1978, then the above procedures defined for the NCI also applies for these NCI loans to earthquake-affected areas of Italy and Greece.

EMS interest rate subsidies

5.16. The EMS interest rate subsidies are financed directly by the Commission budget, Article 570⁽⁶¹⁾, and therefore are subject to the internal Commission procedures for commitments and payments as defined in the Financial Regulation applicable to the general budget of the European Communities.

Following an EIB decision to grant a subsidized NCI and/or EIB loan to a project and the signature of the loan contract, the interest subsidy must be transmitted to the EIB within two months. For that purpose, the EIB transmits its calculation of the interest rate subsidy to the Commission (DG II). The latter, as authorizing officer, in conformity with the procedures laid down in the Financial Regulation, then submits the commitment and payment orders to the financial controller for approval and to the accounting officer for the disbursement and accounting functions.

5.17. The Commission is aware of the terms applied to NCI loans granted, being a co-signatory of the loan contract. Therefore on receipt of the EIB's calculation of the present value of the interest rate subsidy for an NCI loan, DG II (authorizing officer) verifies the calculation and subsequently transmits the commitment and payment orders to Financial Control, together with the original supporting documents as required by the Financial Regulation⁽⁶²⁾. However, for EIB loans which absorbed approximately 88 % of the budgetary appropriations between 1979 and 1981 for EMS interest rate subsidies, the situation is different. In these cases, DG II, as authorizing officer, possesses neither the EIB loan contracts nor the notices of disbursement.

5.18. The interest rate subsidies are not paid on an annual basis from the Commission budget for each individual loan contracted but rather as a lump sum

⁽⁶⁰⁾ Article 4, Council Decision 77/270/Euratom of 29 March 1977.

⁽⁶¹⁾ Article 520, 1982 Community budget.

⁽⁶²⁾ Article 41 of the Financial Regulation of 21 December 1977: 'The payment order shall be accompanied by original supporting documents'.

payment to cover all future interest payments due on each individual loan. The method of calculation of this present value of the interest rate subsidy was agreed by the Commission and the EIB in the bilateral Cooperation Agreement:

'The compound interest rate to be applied to calculate the present value of the subsidy is equal to 75 % of the annual rate of interest which the loan would have borne if it did not benefit from a subsidy' ⁽⁶³⁾.

5.19. The utilization of the EMS interest rate subsidies, after transfer by the Commission to the EIB, has varied:

In relation to Irish projects, the Irish beneficiaries have received the interest subsidy amount. They subsequently make the due interest payments on the NCI or EIB loan to the EIB at the full interest rate.

In relation to the Italian projects, the subsidy has been retained by the EIB. The Italian beneficiaries' interest payments on NCI and/or EIB loans to the EIB are consequently at the subsidized rate. The EIB itself reimburses to the Commission the difference between the full interest rate and the subsidized interest payments it receives from the Italian beneficiaries. Consequently, the EIB rather than the loan beneficiary retains at its disposal the balance of the present value amount.

Interest rate subsidies on 'earthquake' loans

5.20. The major difference between these interest rate subsidies on NCI and EIB loans when compared with the EMS interest subsidies is that the former are paid out by the Commission as the interest payments fall due.

For NCI loans, the Commission receives interest payments at the subsidized rate via the EIB from the loan beneficiaries. It then finances the difference, which is equal to the interest rate subsidy, direct from the Commission budget when it is making the interest payments due on the NCI borrowings.

For EIB loans, the Commission pays from the budget to the EIB, at each due date, the difference between the full interest rate and the subsidized interest rate agreed in the EIB loan contract with the beneficiary.

⁽⁶³⁾ Article 11, Cooperation Agreement between the Commission and the EIB of 17 September 1979.

Observations

BP mechanism

5.21. The Commission is responsible, on behalf of the Community, for the funds which it has borrowed to finance BP loans. This responsibility is reflected by:

- (a) the budget token entries;
- (b) the submission by the EMCF to the Commission of (i) details of all transactions, (ii) the annual report for approval;
- (c) the inclusion of BP loans and borrowings in the Commission's balance sheet as Commission assets and liabilities.

5.22. The Commission has no accounting system in place for the BP loans and borrowings since the funds do not pass through the Commission's bank accounts. The creation of a Commission accounting system, because it would be based on BIS data, would simply duplicate that already in existence at the BIS.

5.23. BP loans and borrowings are included in the Commission's balance sheet and within the context of the preparation of that balance sheet, the Court considers that the Commission's accounting officer should:

- (a) ascertain by what method the EMCF 'verify the accuracy of the accounts and the information contained in the annual report prepared by its agent, the Bank of International Settlements' ⁽⁶⁴⁾;
- (b) confirm with the lending banks and/or the central banks the outstanding balances at the year-end for the loans and borrowings contracted.

5.24. The contracts for the BP loans and borrowings concluded in the 1976-77 period were concluded, following the Council's approval, by the Directorate-General of Economic and Financial Affairs (DG II) on behalf of the Commission. There was no involvement of the Commission's financial controller.

The Court considers it would be preferable if the loan and borrowing contracts to be concluded by the Commission on behalf of the Community, were

⁽⁶⁴⁾ EMCF letter of 13 January 1981 accompanying the 1980 Annual Report.

submitted to the Commission's financial controller for approval prior to signature, in view of the Community's liability for these loans and borrowings, as expressed in the token entries in the Commission budget.

The introduction of these internal procedures is particularly relevant in view of the re-activation of the balance of payments support mechanism in 1981. The ceiling of 6 000 million ECU on total outstanding BP loans fixed by the Council, indicates that there are likely to be renewed applications from Member States for BP loans.

Euratom and NCI mechanisms

Financial control

5.25. The Council decisions ⁽⁶⁵⁾ which established the Euratom and NCI mechanisms, both included the provision that the financial control of the Commission's accounts should be in accordance with the Financial Regulation applicable to the general budget of the European Communities. In practice, this provision has not been applied.

- (i) DG XVIII (Credit and Investments) does not submit the loan and borrowing contracts for the Euratom and NCI mechanisms to the Commission's financial controller for the latter's approval;
- (ii) DG XVIII's financial administration for Euratom loans and borrowings, and NCI borrowings are not subject to the examination and approval of the financial controller.

Therefore, there is no involvement of the Commission's financial controller in the financial management of the Euratom loans and borrowings and NCI borrowings despite the Commission's financial responsibility and the Council decisions.

Accounting systems

5.26. DG XVIII has developed its own accounting system for the loans and borrowings. The Commis-

sion's accounting officer, as is the case with the financial controller, is not involved in the financial operations conducted by DG XVIII relating to the loans and borrowings. DG XVIII operates independently of the Commissions' accounting officer as is evidenced by the bank accounts which are held outside the control of the Commission's accounting officer.

5.27. DG XVIII undertakes both the treasury and accounting functions for the NCI borrowings and the Euratom loans and borrowings and this situation is in direct contrast to the accounting functions in relation to budgetary revenue and expenditure where the Commission's accounting officer is responsible.

This poses evident problems for the Commission's accounting officer in the preparation of the Commission's balance sheet, if the accounting officer does not have the means of verifying the accounts presented by DG XVIII for inclusion in that balance sheet.

The Court considers moreover that the existence of an independent accounting system at DG XVIII which is effectively outside the control of the Commission's accounting officer, is not compatible with sound financial management.

Application of the Financial Regulation

5.28. The basic principle underlying effective internal control in relation to a particular activity is an adequate segregation of functions. This segregation of functions, as foreseen in the Treaty, is reflected in the Financial Regulation of 21 December 1977 applicable to the general budget of the European Community by the division of responsibilities between the authorizing officer, accounting officer and the financial controller. The corresponding functions in relation to the Euratom and NCI mechanisms at the Commission are, however, the sole responsibility of DG XVIII. This applies to the negotiating and contracting of the Euratom borrowings and loans, the NCI borrowings, as well as to the treasury and accounting functions relating to those operations. The Commission's accounting officer and financial controller have no roles analogous to those they exercise for the revenue and expenditure of the general budget.

5.29. This concentration of functions at DG XVIII for the Euratom loans and borrowings and for the NCI borrowings is not only in contradiction with the principles of sound internal control but also with the Council Decisions establishing the Euratom and NCI mechanisms, which state that the

⁽⁶⁵⁾ *NCI*: Article 6, Council Decision 78/870/EEC of 16 October 1978 (OJ No L 298, 25. 10. 1978).
Euratom: Article 5, Council Decision 77/270/Euratom of 29 March 1977 (OJ No L 88, 6. 4. 1977).

financial control of the Commission's accounts shall be in accordance with the Financial Regulation.

5.30. The Court considers that until loans and borrowings are integrated into the Community budget and are subject to the provisions of the Financial Regulation of 21 December 1977, as proposed by the Commission⁽⁶⁶⁾ and advocated by the Court of Auditors⁽⁶⁷⁾, internal procedures need to be introduced for the loans and borrowings analogous to those for budgetary commitments and payments under the Financial Regulation. This would involve the financial controller in the decision-making procedures for the loans and borrowings and the accounting officer in the treasury and accounting functions. The introduction of such procedures would be consistent with the Commission's own proposals to the Council on the budgetization of loans and borrowings, and would segregate the functions within the Commission of the authorizing officer, financial controller and accounting officer; functions which are at present concentrated at DG XVIII.

5.31. The above observations also apply for the NCI loans for projects in earthquake-affected zones of Italy and Greece, since the system introduced for the NCI mechanism in 1978 remains unaltered.

EMS interest subsidies

5.32. As the Cooperation Agreement states, a positive Commission eligibility decision for an interest rate subsidy will result in a budgetary commitment and payment provided the three conditions mentioned in para. 4.31 are fulfilled. Therefore, it is the EIB loan decision rather than the Commission eligibility decision which determines the actual volume of budgetary appropriations which are committed and paid.

5.33. As pointed out in para. 5.17, DG II, as authorizing officer, possesses neither the EIB loan contracts nor the notices of disbursement of the loan for the payment of EMS interest rate subsidies on EIB loans.

The Commission is thus unable to confirm the correctness of the calculation since they do not possess original supporting documents attesting to the validity of the loan terms contained in that calculation. The Court considers that the Commission should

ensure the inclusion of adequate provisions in the Cooperation Agreement which would allow the Commission to respect the procedures for supporting documents required by the Financial Regulation.

5.34. The Cooperation Agreement gives no indication as to how and on what basis 75 % of the annual rate of interest, which the loan would have borne if it did not benefit from a subsidy, was chosen as the compound interest to be applied to calculate the present value of the subsidy. This situation exists in spite of the considerable budgetary appropriations (200 million EUA per year) involved. This percentage has a direct influence on the level of budgetary appropriations paid out by the Commission as EMS interest subsidies to the EIB. In the interests of sound financial management therefore and in view of the financial significance of this percentage, the Court considers that the justification for its choice should be made explicit.

The Court does not consider that the Commission's reply has adequately answered the Court's request that the percentage (75 %) chosen should be justified.

5.35. The Court, having noted the differences in treatment by the EIB dependent on whether the interest subsidies are paid on EIB/NCI loans to either Italy or Ireland, considers that the Commission, being ultimately responsible for these budgetary appropriations, should have ensured that the Cooperation Agreement stipulated:

- (a) precise indications as to how the EIB should dispose of the interest subsidy funds transferred to it by the Commission;
- (b) that the EIB should render an annual financial report to the Commission on the utilization of the interest subsidies.

Interest rate subsidies on 'earthquake' loans

5.36. No observations may be made on the practical workings of these interest rate subsidies due to the fact that the Commission made no payments under this measure in 1981. However, the payment of these interest rate subsidies on an annual basis would appear more preferable to the payment system for the EMS interest subsidies on the present value basis. The payment on an annual basis notably avoids the difficulties inherent in calculating and agreeing the present value of the interest rate subsidies, as stated in paras 5.18 and 5.34.

⁽⁶⁶⁾ OJ No C 160, 6. 7. 1978.

⁽⁶⁷⁾ OJ No C 139, 5. 6. 1979.

CHAPTER 6

EXTERNAL AUDIT OF THE MECHANISMS

Summary

6.1. Audit responsibility for the mechanisms has been defined in the case of Euratom and NCI mechanisms within the context of the Council decisions establishing those mechanisms; for the BP mechanism no reference is made to the audit of the loans and borrowings contracted; for the interest rate subsidies which are financed directly by the Commission, they are subject to the audit provisions contained in the EEC Treaty and Financial Regulation.

BP mechanism

6.2. The European Monetary Cooperation Fund (EMCF) which was established by the Council in 1973, was entrusted with making the necessary arrangements for the administration of the loans and borrowings contracted under the BP mechanism. Because the EMCF is a Community organization it is subject to the audit provisions of the EEC Treaty. It delegated by its Directive of 9 March 1976 the responsibility for this administration to the Bank of International Settlements (BIS) in Basle, an organization outside the Community.

Euratom mechanism

6.3. Audit responsibility for the Euratom loans and borrowings which are contracted by the Commission on behalf of the Community, is defined in Article 5 of the Council Decision 77/270/Euratom which established the mechanism, as:

'Financial control and audit shall be carried out in accordance with the Financial Regulation applicable to the general budget of the European Communities.'

NCI mechanism

6.4. Audit responsibility for the NCI mechanism is defined in Article 6 of Council Decision 78/870/EEC of 16 October 1978 as follows:

'The financial control and audit of the Commission's accounts shall be carried out in accordance with the Financial Regulation applicable to the general budget of the European Communities.'

EMS interest subsidies and interest subsidies on 'earthquake' loans

6.5. Since both these interest rate subsidies are financed directly by the Community budget, then they are subject to the audit provisions contained in Articles 206 (a) of the EEC Treaty and the Financial Regulation. Therefore, the Council Regulations establishing these subsidies do not refer to the audit of the subsidies.

Observations

BP mechanism

6.6. The Court considers, in view of the BIS's responsibility as agent of the EMCF for the administration of the BP mechanism, that the latter's directive to the BIS should include an appropriate clause protecting the Community's right of audit of the administration of the BP loans and borrowings.

NCI mechanism and EMS interest rate subsidies

6.7. In spite of the audit provisions contained in the Council decisions on the NCI mechanism and the audit provisions for the EMS interest rate subsidies as outlined in 6.5 above, the bilateral Cooperation Agreements which were concluded between the Commission and the EIB incorporated additional clauses.

For the NCI, Article 18 of the Cooperation Agreement states:

'The financial control of these operations, included in the Bank's Special Section, shall be carried out in accordance with the audit procedures foreseen in the EIB statutes for all its activities'.

This clause is included notwithstanding the fact that the EIB grants the NCI loans, firstly, on behalf of, for and at the risk of the Community, and secondly, with the proceeds of borrowings contracted by the Commission.

The Court considers that this clause is in direct contradiction to Article 206 of the EEC Treaty, as amended in 1975, and therefore should be deleted.

For the EMS interest rate subsidies, Article 16 of the Cooperation Agreement states:

'With regard to the EIB, the financial control of the operations carried out within the context of this Agreement, shall be according to the verification and discharge procedures foreseen in its statutes.'

This clause is included notwithstanding the Commission's direct responsibility for the implementation of the Community budget as contained in Article 205 of the EEC Treaty. It is in contradiction with Article 206 of the EEC Treaty and therefore should be deleted.

6.8. The Court recommends that as a general policy, a contract granting a mandate to an organization to act as the Community's agent, should automatically incorporate a clause whereby the agent explicitly accepts, and agrees to respect, the application of the Treaty's audit provisions to the activities for which it is being granted a mandate. The inclusion of such an audit clause would have as a double objective firstly, to clarify the audit procedures to be followed and secondly, to avoid the inclusion of provisions which are in contradiction with the Treaty's audit provisions.

The Court has noted with satisfaction the Commission's reply to point 6.7 but observes that no reply has been made to the Court's observations in point 6.8.

CHAPTER 7

GENERAL OBSERVATIONS

On the basis of the detailed observations contained in Chapters 4, 5 and 6, the following observations of a general nature may be formulated concerning the loans and borrowings.

Introduction of mechanisms

7.1. The introduction of these mechanisms in the period 1975 to 1981 may not be construed as the result of an explicit decision or policy decided by the Council with regard to the manner in which Community policies are to be financed and, in particular, the choice between financing those policies either through the revenue of the Community budget or by way of Commission borrowings on behalf of the Community.

Neither may the establishment of these mechanisms be construed as the result of a consistent Community policy on loans and borrowings. The attribution of responsibilities for the granting and administration of the loans differs from one mechanism to another, without the basis for that differentiation being clear.

New Community Instrument

7.2. The New Community Instrument was established in 1978 as a new measure to promote investment within the Community and it was the EIB which was allocated the responsibility for granting

the NCI loans. This responsibility was granted to the EIB despite the fact that firstly, these NCI loans are financed by Commission borrowings and secondly, the EIB already has its own established loan mechanism financed from its own resources. If the NCI was envisaged as an innovative force then it might have been preferable to have structured the NCI outside the scope of already existing Community loan mechanisms, such as the EIB's. It may be a consequence of the structure chosen that the vast majority of projects (excluding 'earthquake' projects) which have received NCI loans, have also received EIB loans.

Euratom

7.3. The attribution of responsibilities for the NCI mechanism differs from that decided for the Euratom mechanism in 1977. For the Euratom mechanism, as with the NCI, it is the Commission which is responsible for contracting the borrowings. However, in contrast with the NCI, it is the Commission which also decides on the granting of the Euratom loans. This system was chosen for the Euratom mechanism notwithstanding the fact that the EIB also grants its own loans to frequently the same energy projects.

EMS interest rate subsidies

7.4. A lack of consistency in the attribution of responsibilities is reflected also in the situation for the EMS interest rate subsidies. Due to the fact that

these interest rate subsidies are financed by the Community budget, then all decisions relating to the utilization of budgetary appropriations should be within the Commission's power. On examination, however, it may be discerned that the final decisions to commit and pay budgetary appropriations on the EMS interest rate subsidies, as well as the timing and the level of utilization of those appropriations, are dependent on the EIB's decisions rather than the Commission's. This is because even when the Commission decides a project is eligible for an interest rate subsidy, the implementation of that decision by the actual granting of a subsidy (and the level of the subsidy) is determined by the EIB's decision on whether to grant a loan to that project.

External audit

7.5. As with the lack of consistency on the attribution of responsibilities for the various phases of the loans and borrowings and associated interest rate subsidies, the definition of the audit of the mechanisms has also varied. The Court considers that it is the EEC Treaty's audit provisions which apply to the audit of the mechanisms and therefore bilateral Cooperation Agreements between the Commission and its agents must respect these audit provisions. The Court considers it necessary that the duties and responsibilities of both the Commission and the Court of Auditors with regard to the audit of the agent's disposal of the Commission's funds, budgetary and non-budgetary, be clearly understood and carried out.

Budgetization

7.6. The loans and borrowings contracted under each mechanism are not included in the Community

budget. The overall volume of their operations is determined therefore not by annual appropriations included in the budget but rather by a ceiling on total borrowings which the Council fixes for each mechanism. In 1978, the Court of Auditors gave a favourable opinion on the Commission's proposal to Council to amend the Financial Regulation applicable to the Community budget by including appropriate provisions for the loans and borrowings. The Council, to date 31 December 1981, has not acquiesced to this Commission proposal on 'budgetization' of loans and borrowings.

Notwithstanding the present non-inclusion of the loans and borrowings of the BP, Euratom and NCI mechanisms in the Community budget, the Court of Auditors considers that it would be preferable if the Commission would introduce appropriate internal procedures for the decision making and financial management of the loans and borrowings analogous to those procedures contained in the Financial Regulation, which are applicable to the revenue and expenditure of the general budget.

The Court has noted that the Commission in its replies (point 5.25, first paragraph, points 5.28 to 5.31, point 7.6) makes frequent reference to the internal control unit recently established within DG XVIII and responsible to its Director-General. However, when the Court refers to the application of internal procedures analogous to the Financial Regulations, it is referring to the introduction of the Commission's financial controller and accounting officer in DG XVIII's financial operations.

The above comments were adopted by the Court of Auditors at its meeting of 19 July 1982.

Luxembourg, 6 August 1982.

For the Court of Auditors

Pierre LELONG

President

ANNEX I

FINANCIAL ANNEX

1. BP loans
2. Euratom loans
3. NCI loans
4. EMS interest rate subsidies

1. BP LOANS

Table 1

BP loans to Member States

Duration of loan	Interest rate %	Million ECU (1)	
		Italy	Ireland
1976-1982	8.25	208.5	62.9
1976-1983	7.25	157.0	47.0
1977-1982	7.625	20.8	6.3
1977-1982	7.5	180.9	—
1977-1984	7.75	271.4	—
1977-1982	7.625	69.5	20.9
Totals		908.1	137.1

(1) Note

1. BP loans outstanding at 31 December 1981 as stated in the Commission's Revenue and Expenditure Account 1981, Vol. II, page 320, COM(82) 233 final.
2. BP borrowings:
In the period 1976-1977, US \$ 1 600 million and DM 500 million was borrowed by the Commission and on-lent to Member States as BP loans.

2. EURATOM LOANS

Table 2.1

Euratom loans granted in the period 1977-1981 (1)

Year	Number of loans	Million ECU
1977	3	102.1
1978	2	83.7
1979	9	153.2
1980	10	182.5
1981	17	364.6
Totals	41	886.1

(1) Source:

Commission's Revenue and Expenditure Account 1981, Vol. II, page 322. COM(82) 233 final. Loan amounts stated are those amounts outstanding at 31 December 1981. No capital repayments had been made on the loans up to 31 December 1981.

Table 2.2
Annual distribution of Euratom loans to projects in Member States in the period 1977-1981 (1)

Member State	1977	1978	1979	1980	1981	Million ECU
Belgium	—	—	2	5	11	294.9
France	2	—	6	5	5	360.4
Germany	1	1	—	—	—	117.9
Italy	—	1	1	—	1	112.9
Totals	3	2	9	10	17	886.1

(1) *Source:* Commission's Revenue and Expenditure Account 1981, Vol. II, page 322. COM(82) 233 final.

Loan amounts stated are those amounts outstanding at 31 December 1981. No capital repayments had been made on the loans up to 31 December 1981.

Note:

The number of loans granted to Member States outlined above should not be equated with the number of nuclear energy projects financed. In effect, as a project may consist of several phases extended over many years, then it may receive more than one Euratom loan over its lifetime.

3. NCI LOANS

Table 3.1
NCI loans in the period 1979-1981

Year	Number of projects			Million ECU (1)
	Energy	Infrastructure	Italian earthquake	
1979	2	5		179.3
1980	9	4		303.2
1981	7	6	3	328.4
Totals	18	15	3	810.9

(1) *Note:*

The amounts indicated are the value of the NCI loans granted in each financial year.

Table 3.2
Distribution of NCI loans to projects in Member States in the period 1979-1981

Member State	Number of projects	Million ECU (1)
Denmark	1	9.7
France	1	40.2
Ireland	9	153.5
Italy	22	506.0
United Kingdom	3	163.0
Totals	36	872.4

(1) *Note:*

The amounts indicated are the NCI loans outstanding at 31 December 1981 as stated in the Commission's Revenue and Expenditure Account 1981, Vol. II, pages 324-325.

4. EMS INTEREST RATE SUBSIDIES

Table 4.1

EMS interest rate subsidies paid on NCI and EIB loans

Year	Interest rate subsidies (million ECU) on		Number of projects benefiting	
	NCI loans	EIB loans	NCI projects	EIB projects
1979	22.4	177.5	5	29
1980	29.6	167.4	7	46
1981	18.2	175.0	9	36
Totals	70.2	519.9	21	111

Table 4.2

EMS interest rate subsidies accorded to Italian and Irish projects in the period 1979-1981

(million ECU)

Year	Interest subsidies on <i>Italian</i> projects receiving		Interest subsidies on <i>Irish</i> projects receiving	
	EIB loans	NCI loans	EIB loans	NCI loans
1979	119.8	14.1	57.7	8.4
1980	108.7	21.2	58.7	8.4
1981	111.5	15.1	63.5	3.1
Totals	340.0	50.4	179.9	19.9

*ANNEX II***COMMISSION OF THE EUROPEAN COMMUNITIES****REPLIES TO THE SPECIAL REPORT BY THE COURT OF AUDITORS
ON LOANS AND BORROWINGS*****I. OBSERVATIONS ON THE DECISION-MAKING PROCEDURES*****Point 4.37: Euratom loans: Minutes of the Commission's EIB Inter-Service Group meetings**

The Commission's EIB Inter-Service Group records the results of its weekly meetings on each project decision to be put before the Commission. Whenever any major questions arise, they are mentioned in the summary record of the meeting. The Commission appreciates that the Court might wish the discussions of the EIB Inter-Service Group to be reported in more detail: appropriate arrangements will be made and the minutes of meetings will in future set out the main points discussed more fully.

The Commission's procedure for taking decisions on applications for Euratom financing is based on an assessment of the investment projects with respect to their conformity with the provisions of the Euratom Treaty and secondary legislation, the Council's decisions and guidelines, the Cooperation Agreement with the EIB and the latter's recommendation on each of the projects in question.

The Inter-Service Group which prepares the Commission's decisions records its conclusions on each project — unanimous approval without discussion or list of problems and divergences of view prompting reservations or adverse opinions.

Explicit reference in the Cooperation Agreement to the criteria used by the EIB in evaluating projects

In granting loans as the executive agent for Euratom, the EIB applies the provisions embodied in Council decisions and in the texts annexed to the Council minutes as well as those laid down in its Statute. The Cooperation Agreement refers explicitly to those texts and lays down such arrangements as are not specified in them.

Point 4.38: NCI loans: Explicit interpretation of the Council's general guidelines on eligibility for NCI loans

To interpret the general eligibility guidelines laid down by the Council the Commission applies all the Community rules, policies and priorities relating to the areas concerned; the Bank is kept fully informed and it has all the relevant documentation.

The Commission keeps the Bank informed of the various ways in which it applies the guidelines set by the Council, as required by Article 5 of the Cooperation Agreement.

With regard to the eligibility guideline which requires investments to conform to the relevant Community rules, the Commission makes those rules known to the Bank and explains their content: this applies particularly to the rules on competition and the opening-up of markets, protection of the environment, restrictive or priority conditions relating to sectors such as energy or agriculture, the demarcation of zones and regions regarded as sensitive, opinions on investments notified to the Commission in accordance with the provisions of the Community Treaties, for which an application for financing has been made, etc.

As for the guideline on investment as a contribution to solving the Community's main structural problems and in particular to eliminating regional disparities and improving the employment situation, there is a steady flow of documents both to the Council and the EIB in which the Commission sets out the broad objectives of Community policy and the measures that should be taken to solve the main structural problems.

In the two specific fields of energy and infrastructures, the Commission has preferred not to subject the application of a financial instrument to formal criteria, the definition of which would inevitably be in some degree arbitrary and imperfect. If, on the other hand, in later applications of the NCI more specific policies were to be developed or more restricted projects implemented than is the case in the two fields now covered, the Commission would take utmost care to ensure that the criteria for aid were defined with all the precision necessary.

Point 4.39: NCI loans: Minutes of the Inter-Service Group meetings

There are already sufficiently detailed summary records to enable the decision-making process to be traced back in cases where problems have arisen. However, as with Euratom loans, the Commission will arrange for the minutes of meetings to record more fully the main points discussed.

The Commission's decisions relating to applications for NCI financing are based on an assessment of the investment projects with respect to conformity with the provisions of the EEC Treaty and secondary legislation, the Council's decisions and guidelines and the cooperation agreement with the EIB.

The Inter-Service Group which prepares the Commission's decisions records the results of its discussions on each project — unanimous approval without discussion or list of problems and divergences of view prompting reservations or adverse opinions. The same arrangements (see 4.37 above) will be made for the EIB Inter-Service Group's discussions about NCI loans.

Point 4.40: Difference between NCI loans and EIB loans

In view of the experimental nature of the NCI operations under the first tranches of borrowings, the close link between the two instruments was desirable and beneficial. The Commission would stress that the development of NCI loans has had the effect of supplementing the EIB's activities. Subsequent developments, however, will show the NCI evolving along its own lines: the first step in this direction was taken in allowing NCI I to finance housing in certain cases. In the future, the Commission envisages a more specific application of the instrument in areas less well covered by EIB aid. This is evidenced by the areas of application defined in the recent Council decision. The NCI will have a role distinct from that of the EIB in the financing of certain classes of investments relating to the rational use of energy or investments by small and medium-size businesses, notably non-industrial and outside classified regions (NCI II decisions of 15 March 1982 and 26 April 1982).

Point 4.41: NCI loans: Divergence between the decision-making procedures for the NCI instrument (1978) and for the Euratom instrument (1977)

The difference between the Euratom and NCI procedures is that Euratom projects are far fewer but involve much larger sums than those of the NCI, and they relate to a special category of

promoters with massive financial resources particularly well-suited to back-to-back operations. Because of these special features of Euratom operations the Commission is able to handle applications for financing and the grant of loans without additional personnel, whereas full-scale management of NCI applications and loans by the Commission would require a large number of new staff with the appropriate administrative framework, which would thus duplicate the Bank's facilities.

If, then, the Commission asked for the Euratom procedure to be applied to the NCI, as the Court of Auditors suggests, it would have to take on a large number of additional staff. (*This also applies to points 5.26, 5.27 and 5.28 to 5.31.*)

This is why Article 172 (4) of the Euratom Treaty provides that loans will be granted without any specific body being set up, whereas the EEC Treaty, which lays the legal foundation for NCI operations (Article 235), makes provision for the establishment of the EIB (Article 129) with the task of contributing to the balanced development of the common market by granting loans for the financing of projects in all sectors of the economy (Article 130).

The Commission feels that the Court of Auditors should bear in mind these very clear-cut differences between NCI and Euratom projects and realize that they call for different procedures.

Responsibility for decisions to grant NCI loans

The Council decided that the Bank should be made responsible, under a cooperation agreement, for granting loans in pursuance of its Decision 78/870/EEC. This allocation of powers does not leave the Commission with no responsibility in the decision-making procedures relating to the grant of NCI loans.

This responsibility is as follows:

- the Commission decides on the eligibility of each project; any project found ineligible by the Commission will not receive an NCI loan;
- under Article 9 of the Agreement it can seek consultation with the Bank before a final decision on the application is taken;
- the director nominated by the Commission on the board of directors of the EIB has a say in decisions on the grant of NCI loans;
- the Commission, acting on behalf of the Community, signs NCI loan contracts jointly with the EIB; without this signature, which confirms the eligibility decision, no contract can enter into force. It is clear that even apart from the decision on eligibility, the Commission remains in full control of its position until the contract is signed.

In view of these possibilities of intervention by the Commission in a joint decision-making process, and bearing in mind the comments made at 4.41 above, the Commission believes that it is fully shouldering its responsibilities in this matter. The Commission would also add that the Commission and the EIB frequently hold working meetings on questions relating to the application of the NCI or to Euratom loans at various levels including that of the President and Management Committee of the EIB and the Member of the Commission responsible (at present the Vice-President of the Commission responsible for economic and financial affairs).

Point 4.44: Interest subsidies

(i) Selection criteria for projects to be considered for interest subsidies

The Commission considers that in practice the definition of the area of eligibility for interest subsidies ('primarily infrastructure projects') is clear enough and allows a sufficiently careful selection of projects. It would further point out that projects proposed for interest subsidies are also subject to the general Community rules, policies and priorities (respect for competition, opening-up of public markets, etc.) and the rules relating to specific fields (energy,

agriculture, environment, etc.). The EIB is familiar with all these rules and applies them when selecting applications.

Like the Commission's opinions and decisions on the grant of loans, decisions on eligibility for an interest subsidy are taken with reference to all the criteria set by the Community's policies, with which the EIB is well acquainted. The basic criteria for interest subsidies are stricter than those for loans.

(ii) *Criteria for the division of annual budget appropriations for interest subsidies between NCI and EIB loans*

The value of NCI and EIB loans receiving subsidies is proportionate to the relative size of the two instruments.

(iii) *Interpretation in the Agreement of the Council's guidelines on eligibility for interest subsidies*

For the same reasons as given at (i) and (ii) above, the Commission takes the view that there is no need to define more precise criteria in the Cooperation Agreement.

Point 4.45: The EIB's decision on the grant of a loan determines whether an interest subsidy is granted

The decision-making procedure appears to be in contradiction with Article 205 of the EEC Treaty, which makes the Commission responsible for the implementation of the budget

It is the Commission which decides in the first instance whether or not a project can be taken into consideration. Without the approval of the Commission, there can be no interest subsidy; hence the subsidy does in fact depend on the Commission.

To elaborate on this point, the joint signature of a subsidized loan contract by the Commission and the EIB (acting alone or jointly with the European Economic Community, depending on whether it is an EIB or an NCI loan) commits the EEC only conditionally, since only two of the three conditions on which a decision on eligibility depends are satisfied at the stage of signature; the third, which relates to the availability of the necessary budget appropriations can be fulfilled only when the loan is actually disbursed to the promoter. Until all the terms of the loan are known, the Commission retains the right to refuse actual payment.

In view of this mechanism for safeguarding its position, the Commission considers that it implements the budget 'on its own responsibility and with the limits of the appropriations' (Article 205 of the EEC Treaty).

II. FINANCIAL ADMINISTRATION

Point 5.23: The Commission's accounting officer should examine the methods of verification employed by the EMCF

The Commission's accounting officer should confirm the end-of-year balances for loans and borrowings with the lending banks and/or the central banks of the Member States

The Commission carries out a formal check of the information contained in the annual report submitted by the EMCF against the schedules of due dates for each borrowing/lending operation and the documents sent in by the BIS in respect of each redemption or interest payment in accordance with the directive issued by the EMCF to its agent in March 1976.

A procedure whereby the Commission asks the lending banks or the central banks to confirm the data in the report submitted by the EMCF will not cause any special difficulty and arrangements will be made for such a procedure to be introduced.

Point 5.24: Balance of payments mechanism: contracts to be concluded by the Commission are not submitted to the Financial Controller beforehand

With regard to the conclusion of borrowing contracts, the introduction of a procedure for obtaining the approval of the Financial Controller would not be technically feasible. Up to the point where agreement is reached, the conclusion of contracts is an ongoing process of negotiation with the lenders. The Commission thinks that the object of the Court of Auditors would be satisfied if the Financial Controller were to be consulted before the negotiations are concluded. It will arrange for this to be done. Loans are granted by the Council on the same terms as the initial borrowing.

Point 5.25: Involvement of the Financial Controller in NCI and Euratom borrowing and lending activities

Whilst it acknowledges the truth of the Court's remarks, the Commission must stress that it is for reasons of operational efficiency that it has hitherto entrusted the internal audit of Euratom and NCI borrowings and lendings to a special in-house audit unit at the Commission. The Commission's role as a financial intermediary between applicants for loans and the lenders requires it to react promptly to market conditions and the needs of the undertakings. Under these circumstances it has attached great importance to close coordination between the functions of management, internal audit and accounting.

As regards financial control proper, the Commission would point out that the Financial Controller is himself involved in the control of NCI and Euratom operations as follows:

- he is systematically notified of all borrowings authorized by the Member of the Commission responsible at the time the contracts are concluded;
- he is involved in decisions on the eligibility of projects for loans, being a member of the Inter-Service Group responsible for them. In particular, his task is to check that they are compatible with the objectives set by the Council for each tranche.

The Commission accepts that the role of the Financial Controller in borrowing and lending activities needs to be strengthened. It has already given instructions that the Financial Controller's approval must be sought for other financial operations, notably for the signature of NCI contracts by the Commission.

The additional controls it will be introducing should help to improve efficiency in the management of funds.

In a more general vein, the Commission thinks that the nature of the borrowing and lending operations with respect both to management procedures and objectives is such that the procedures laid down in the Financial Regulation must be applied. However, if these procedures are not to hamper borrowing and lending operations, they must be applied with suitable flexibility.

Point 5.26: The organization of Euratom and NCI accounting at the Commission

The Commission proposes to take steps to integrate the recording of borrowing and lending operations into the general accounting system by means of monthly link accounts.

It would add, moreover, that, contrary to what is stated in point 5.12, Commission staff do have full economic, technical, financial and accounting information for NCI loans.

Points 5.26 and 5.27: Management of bank accounts by DG XVIII

The bank accounts for NCI and Euratom operations are in the names of the European Economic Community and the European Atomic Energy Community respectively. As in the case of the

EAEC, which also has accounts in its name, the statements will in future be forwarded to the Commission's accounting officer each month by the managing department.

By its Decisions of 28 May 1973, 7 March 1979 and 26 October 1977, the Commission delegated responsibility for borrowing and lending operations — and the corresponding cash operations — to the Member of the Commission holding this portfolio, the Director-General for Credit and Investments and to certain officials.

The Commission has taken note of the Court's remarks on the management of bank accounts and will make arrangements for the officials directly responsible for the collection of revenue and the payment of expenditures to be subordinate to the accounting officer and answerable to him.

Points 5.28-5.31: Application of the provisions of the Financial Regulation and the need for additional rules

On 15 June 1978, the Commission sent a proposal to the Council for the integration of borrowing and lending operations in the budget. This has received a favourable opinion from the Court of Auditors and the European Parliament. Once the Council has accepted the principle of integration in the budget, the Commission will propose the necessary administrative arrangements. The proposals will be drawn up on the basis of the internal rules which have been applied in this connection since 1 October 1981 and which are based on the experience gained with ECSC operations and over the last five years in the handling of Euratom and NCI financial operations.

While the present Financial Regulation remains applicable to borrowings and loans, the Commission undertakes — without impairing the efficiency of the operations concerned — to reflect clearly in its internal procedures and structures the separation of functions between the authorizing officer, the accounting officer and the financial controller.

Points 5.16-5.32: EMS interest subsidy: volume of budget appropriations

As already stated earlier, no interest subsidy can be paid without the Commission's decision on eligibility.

Points 5.17-5.33: Supporting documents for interest subsidies on EIB loans

The Commission and the Bank are currently studying this question with a view to finding a solution that will satisfy the Court of Auditors.

Points 5.18-5.34: Determination of the rate

The EIB has already explained the reasons for this rate to the representatives of the Member States, who accepted it.

The 75 % rate was chosen when the Commission-EIB agreement was drafted. It was seen as a balanced compromise by both the Commission and the Bank. The choice was also discussed with the representatives of the Member States, who accepted it. More recently, in 1981 and 1982, the development of interest rates, in particular the sharp rise in short-term rates, has shown that a review of the method of fixing the rate might be necessary. Talks are being held with the EIB to see how the rate might be revised.

Points 5.19-5.35: Differences in the allocation of interest subsidies

As was pointed out in connection with the European Regional Development Fund in the Commission's replies to the 1979 Annual Report of the Court of Auditors (page 250, point 1.35), the procedures for paying interest subsidies must meet the needs of investors: 'some investors prefer to have additional financial support immediately at the cost of maintaining the initial rate of interest throughout the duration of the loan; others opt instead for a reduction in the long-term interest burden'.

It would therefore be inappropriate to impose one or other of these solutions in an official text. The choice is deliberately left to the investors: 'the important factor is to provide an incentive for the achievement of the investment projects which are subsidized in this way'.

The Commission will ask the EIB to produce a detailed annual report on the way in which interest subsidies have been paid.

III. EXTERNAL AUDIT

Points 6.2 and 6.6: BP mechanism: the EMCF directive to the BIS should include a clause protecting the Community's right to verify the administration of 'balance of payments' loans and borrowings

The Court's request does not seem to take account of the fact that the responsible officials of the EMCF and the BIS are largely the same people. Moreover, the BIS's task in connection with 'balance of payments' borrowings and loans is merely to make the borrowing and lending operations official and enter them in the accounts. The BIS performs no function of its own in this connection: the arrangements are such that the funds paid to it by the lenders are transferred on the same date to the recipients designated by the Council. The Commission receives full details of these operations, and that information is available to the Court of Auditors and can be verified in connection with the confirmation of the bank balances at the end of the year (referred to at 5.23 above).

Points 6.4 and 6.7: NCI mechanism and interest subsidies

The clauses on external audit in the agreements between the Commission and the EIB are contrary to Article 206 of the EEC Treaty

The Commission has taken note of the Court's request on this point and, together with the EIB, will seek a solution to the question of the external audit of Community loan operations which will enable the Court of Auditors to carry out its examination satisfactorily.

IV. GENERAL OBSERVATIONS

Point 7.1: The assignment of responsibilities for the granting and administration of loans differs from one instrument to another

The introduction of the Euratom, NCI and EMS mechanisms is the outcome of Council decisions on how to meet the Community's needs and priorities in the promotion of investment. The assignment of responsibilities derives from the nature of each instrument, as explained in earlier points.

Point 7.6: Internal procedures similar to those laid down in the Financial Regulation

The Commission shares the Court's opinion on this point. Its concern about the matter prompted it to introduce internal rules with effect from 1 October 1981 covering all Euratom and NCI financial activities within the Directorate-General for Credit and Investments.

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HIGHER EDUCATION IN THE EUROPEAN COMMUNITY
A HANDBOOK FOR STUDENTS

1981 Edition

This handbook for students has been prepared, for the assistance of students and their advisers to bring together in all Community languages the basic information needed by those considering a period of higher education in another Member State.

The Handbook contains an entry for each of the Member States of the Community. Each entry consists of two main sections, a descriptive text and an appendix. The text gives general information on the structure of the higher education system, its institutions and the types of qualifications obtainable, on admission conditions and application procedures, and on fees, language requirements and grants, as well as an indication of important social elements such as social security counselling, accommodation, etc. The appendix to each country entry contains a list of addresses of organizations and institutions from which further information and/or application forms may be obtained, a bibliography of national information material, in most cases a table of subjects taught at each institution, and a glossary per national entry for the explanation of terms that have not been translated.

In addition to the national entries, the Handbook contains separate entries for the College of Europe at Bruges and the European University Institute at Florence.

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