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REPORT

on the Special Report No 6/2000 of the European Court of Auditors concerning the granting by the Community of interest subsidies on loans by the European Investment Bank to small and medium-sized enterprises within the framework of its temporary lending facility, accompanied by the Commission's replies (C5-0023/2001 – 2001/2015(COS))

and on the Special Report No 3/1999 of the European Court of Auditors concerning the management and control of interest-rate subsidies by the Commission, accompanied by the Commission's replies (C5-0158/2001 – 2001/2015(COS))

Committee on Budgetary Control

Rapporteur: Christopher Heaton-Harris

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PROCEDURAL PAGE

By letter of 5 July 1999, the European Court of Auditors had forwarded to Parliament its Special Report No 3/1999 on the management and control of interest-rate subsidies by the Commission, accompanied by the Commission's replies (2001/2015(COS)).

At the sitting of 2 May 2001 the President of Parliament announced that she had referred the report to the Committee on Budgetary Control as the committee responsible and the Committee on Industry, External Trade, Research and Energy for its opinion (C5-0158/2001).

By letter of 19 April 2000, the European Court of Auditors forwarded to Parliament its Special Report No 6/2000 concerning the granting by the Community of interest subsidies on loans by the European Investment Bank to small and medium-sized enterprises within the framework of its temporary lending facility, accompanied by the Commission's replies (2001/2015(COS)).

At the sitting of 18 January 2001, the President of Parliament announced that she had referred the report to the Committee on Budgetary Control as the committee responsible and the Committee on Industry, External Trade, Research and Energy for its opinion (C5-0023/2001).

The Committee on Budgetary Control had appointed Christopher Heaton-Harris rapporteur at its meeting of 29 August 2000.

It considered the draft report at its meetings of 25 April, 29 May and 18 June 2001.

At the last meeting it adopted the motion for a resolution unanimously.

The following were present for the vote: Diemut R. Theato, chairman; Christopher Heaton-Harris, rapporteur; Helmut Kuhne, Emmanouil Mastorakis (for Herbert Bösch), Jan Mulder (for Lousewies van der Laan), Heide Rühle (for Bart Staes), Esko Olavi Seppänen (for Marianne Eriksson), Rijk van Dam, Michiel van Hulst.

The Committee on Industry, External Trade, Research and Energy decided on 26 March 2001 not to deliver an opinion.

The report was tabled on 25 June 2001.

The deadline for tabling amendments will be indicated in the draft agenda for the relevant part-session.

MOTION FOR A RESOLUTION

European Parliament resolution on Special Report No 6/2000 of the European Court of Auditors concerning the granting by the Community of interest subsidies on loans by the European Investment Bank to small and medium-sized enterprises within the framework of its temporary lending facility, accompanied by the Commission's replies (C5-0023/2001 – 2001/2015(COS)) and Special Report 3/1999 on the management and control of interest-rate subsidies by the Commission accompanied by the Commission's replies (C5-0158/2001 – 2001/2015(COS))

The European Parliament,

- having regard to Special Report No 3/1999 of the European Court of Auditors concerning the management and control of interest-rate subsidies by the Commission, accompanied by the Commission's replies (C5-0158/2001¹),
 - having regard to Special Report No 6/2000 of the European Court of Auditors concerning the granting by the Community of interest subsidies on loans by the European Investment Bank to small and medium-sized enterprises within the framework of its temporary lending facility, accompanied by the Commission's replies (C5-0023/2001²),
 - having regard to Rule 47(1) of its Rules of Procedure,
 - having regard to the report of the Committee on Budgetary Control (A5-0215/2001),
- A. Whereas in June 1993 the European Council launched the so-called Copenhagen facility by asking the European Investment Bank (EIB), in conjunction with the Commission, to earmark one billion ECUs in loans to increase the competitiveness of European small and medium-sized enterprises; whereas interest subsidies were fixed at 200 base points, or 2%, were extended to beneficiaries for a period of five years and were restricted to investment projects involving the creation of jobs;
- B. Whereas on 19 April 1994 a cooperation agreement was drawn up between the Commission and the EIB which sets out a number of provisions including those regarding the definition of the subsidised SME loans, agents and intermediaries, conditions for granting interest subsidies, cost and expenses incurred, as well as records and reporting; notes that provisions should have been clearer, especially those regarding management and control issues;
- C. Whereas the Facility only became fully operational in autumn 1994 by which time interest rates had started to fall in most Member States;
- D. Whereas the structure to continue to administer the Facility will need to be in place until the middle of 2002;
- E. Whereas loans could not be combined with other loans at reduced rates offered by the EIB under other agreements or with ECSC loans; notes that the Court of Auditors

¹ OJ C 217, 29.7.1999

² OJ C 152, 31.05.2001

pointed out that an exception was agreed between the EIB and the Commission for ERDF aid at an inappropriate level and therefore had no legal value; questions why this derogation was not applied to all Member States;

- F. Whereas in paragraph 57 of its discharge resolution of 10 April 1997¹ for the 1995 financial year, Parliament asked the Court of Auditors and the Commission to issue opinions at the earliest opportunity on the management and effectiveness of the Copenhagen facility,
- G. Whereas the Court of Auditors submitted two special reports, namely on the management and control of interest-rate subsidies by the Commission² and on the granting of interest subsidies on loans by the EIB³, regrets the quality of answers submitted by the Commission;
- H. Whereas in drawing up its special report the Court of Auditors visited all Member States of the Union, carried out checks in respect of beneficiary SMEs and of financial intermediaries in six Member States and noted a number of weaknesses including the following:
- i. impact on investment and job creation: the overall effectiveness of the scheme is questionable, as it was impossible to demonstrate, at microeconomic level, a causal link between job creation and interest subsidies;
 - ii. management and control systems: the appraisal system, based on delegation to intermediaries, was weak, as subsidies were paid on the basis of sworn declarations made by the recipients themselves, no penalties were envisaged for intermediaries who sent inaccurate declarations and neither the EIB nor the Commission carried out adequate compensating checks;
 - iii. equality of access: the Court found that the scheme did not give equality of access to customers across the Union, as banks without global loans contracts with the EIB were excluded from the scheme, whilst some agents or intermediaries did not publish the facility widely, preferring to choose the applicants themselves;
 - iv. interest-rate subsidies in general: points out that, in its Special Report 3/1999 on the management and control of interest-rate subsidies, the Court of Auditors judged that there is a risk that intermediaries' remuneration would exceed those stipulated and that the aid intended for beneficiaries would thereby be reduced proportionately;
- I. Whereas, according to article 3 of the Council decision⁴ on the Copenhagen facility, the Commission should present to Parliament and Council a yearly report evaluating the implementation of the decision;
- J. Whereas the Commission concludes, in its fifth report on the implementation of the Copenhagen facility⁵, under lessons to be learned, that in hindsight the self-certification of job creation would appear to have its drawbacks and may in some cases have resulted

¹ OJ L 162, 19.6.1997

² Special report 3/1999, OJ C217, 29.7.1999

³ Special report 6/2000, OJ C 152, 31.5.2000

⁴ Council decision 94/217/EC of 19 April 1994, OJ L107, 28.04.1994

⁵ COM(2000) 376 final, 22.06.2000

in the over-declaration of jobs;

- K. Whereas the Court cast doubt on the effectiveness of the programme to create jobs, the Commission stated that the subsidy represented extremely good value for money, declaring that 53 789 new jobs were created; questions the assumptions by which the Commission arrived at this figure;
- L. Whereas on 15 February 2001 the Commission presented an evaluation¹ on the effectiveness of interest-rate subsidies in the light of the Court's special report 03/1999 on the matter;
- M. Whereas the Commission identifies strong points of interest-rate subsidies such as low budgetary costs, leverage effect, additionality and symbol of Community support as well as weak points including risk of inefficient allocation of resources, cumbersome administration, risk of discrimination, low visibility and the fact that control and transparency are not always ensured;
- N. Whereas the European Investment Fund (EIF) established in 1994, following the Edinburgh summit of December 1992, aims to promote medium and long term investment in SMEs by guaranteeing loan finance or by acquiring, holding or managing equity in venture capital funds and Trans-European Networks by providing loan guarantees;

European Investment Bank

- 1. Regrets that, although the Commission bears the overall budgetary and political responsibility for interest-rate subsidies, the EIB:
 - (a) Management controls: allowed an unsupervised system to operate whereby payments were calculated and made by national agents on the basis of sworn statements by applicants on an actual and uninterrupted increase in the number of jobs; notes that on-the-spot checks by the Court of Auditors revealed that for 20% of all cases audited², the number of jobs that were truly eligible was lower than the number being subsidised; notes that, as the Commission and EIB interpret the rules differently, they disagree with the Court on the error rate given;
 - (b) Competition: under time-constraints imposed by the Council, worked with its existing customers as financial intermediaries over other banks, thereby distorting competition; notes that banks used the facility to promote their own interests, for example to retain existing or attract new clients;
 - (c) United Kingdom: of the 28 recipients audited in the United Kingdom, the Court found six cases, amounting to €149 000, where the eligibility period extended beyond 30 June 1997, and found ten cases where recipients had received too much subsidy for including VAT paid on the purchase of capital goods in their calculations; notes that this type of error was not found in any other country;
 - (d) Spain: although article 4 of the cooperation agreement stipulates that an SME subsidised loan can not be combined with other subsidised loans a derogation was

¹ COM(2001) 86 final, 15.2.2001

² In 23 of the 114 cases audited, the Court found that the number of jobs truly eligible was lower than the number subsidised

agreed and only applied to one Member State; recalls that intermediaries in other Member States do not seem to have known about the existence of this derogation;

2. Calls on the EIB to present, at least on an annual basis, to the Parliament and Commission:
 - (a) Democratic accountability: the annual report of the Audit Committee to the Board of Governors; welcomes that the EIB has begun to publish details of its evaluations on its Internet site; encourages the EIB to continue and extend the publication of its executive summaries of audits and evaluations on its web-site;
 - (b) European Investment Fund: encourages the EIB to take further steps to allow full access by the Court of Auditors to the EIF in the near future; calls for an agreement to be reached before the end of June 2001;
 - (c) Instructions: clear and consistent rules for applications and eligibility criteria which will reduce ambiguities thereby ensuring that individuals and companies in Member States are treated in the same manner;

European Commission

3. Regrets that, citing the principle of avoiding duplication of work, the Commission abdicates much of the ex-ante and ex-post controls to the EIB which acts on the Union's behalf; notes that as regards its management of interest-rate subsidies in general, the Commission:
 - (a) Ex-ante controls: rubber-stamps proposals for projects submitted by the EIB and does not check the eligibility of projects;
 - (b) Monitoring: hardly carries out any controls and relies excessively on its agent, the EIB; recalls that delegating management is not tantamount to delegating responsibility;
 - (c) Ex-post evaluation: does not analyse progress reports of investments under way, relies on a high utilisation rate as a proxy for effectiveness and confines itself to drawing up a list of projects implemented and sums spent, rather than carrying out impact analysis of subsidies;
4. Notes that as regards the management of the Copenhagen facility, the Commission did not carry out adequate compensatory checks of the EIB's management and control system;
5. Calls on the Commission to report to the discharge authority by 15 October 2001:
 - (a) Co-operation with EIB: on ways to increase cost-effective controls on loans managed on its behalf by the EIB;
 - (b) Ex-ante, monitoring and ex-post controls: on steps to improve monitoring during each stage of the project and programme cycle;
 - (c) Alternatives: on alternative mechanisms that are cost-effective, in the light of the conclusion of the Commission's report¹, on the general usefulness of interest-rate subsidies, which states that the question of abandoning interest-rate subsidies

¹ COM(2001) 86 final, 15.2.2001

should be addressed; recalls that budgetary resources approaching €3 billion have been devoted, in favour of other instruments, as regards the following Community programmes involving interest-rate subsidies:

<i>Measures designed to combat Market failure:</i>	ECSC conversion (Article 56)
	TENs
	Edinburgh facility for SMEs
	Development co-operation for ACP countries
	Economic development for MEDA and Slovenia
	ERDF
<i>Measures designed to deal with External shocks</i>	Natural disasters (Italy, Greece, Kalamata and Madeira)
	European Monetary System
	Peace and reconciliation in Ireland
	Reduction in disparities (EEA)
	Reconstruction in the Balkans (FYROM and Bosnia)

Council

6. Asks the Council to refrain from imposing ill-conceived and unworkable programmes on the EIB and Commission;
7. Notes that in the conclusions of the Presidency to the Stockholm summit of 23-24 March, the Council agreed that the EIB should open up lending to Russia for selected environmental projects in Kaliningrad and Saint Petersburg; notes that, in addition to the EIB, the so-called 'Northern Dimension Environmental Partnership' scheme will comprise the European Commission, the European Bank for Reconstruction and Development, Nordic Investment Bank, World Bank and Baltic States including Russia; expresses reservations as to the feasibility, sustainability and practicalities of this scheme; calls on all parties to ensure that rigorous control mechanisms are in place including a clearly defined cooperation agreement;

European Bank for Reconstruction and Development

8. Recalls that the idea of the EBRD, to foster the transition from command towards market-oriented economies and to promote private enterprise, was first announced at the European Parliament on 25 October 1989; notes that in contrast to the Commission, the EBRD lays strong emphasis on central ex-ante control by its Chief Economist and independent ex-post evaluation of projects; welcomes the importance given to the principles of additionality and conditionality by the EBRD; looks forward to examining the Bank's effectiveness in promoting private enterprise in Central and Eastern Europe and the Commonwealth of Independent States, following an audit by the Court of Auditors;

Court of Auditors

9. Invites the Court to report in its annual report for 2000 on progress by the Commission, European Investment Bank and Member States in remedying the weaknesses highlighted in this resolution and in its special reports; looks forward to examining the audit on venture capital funds supported by the Commission;



10. Instructs its President to forward this resolution to the Council, the Commission, the Court of Auditors and the European Investment Bank.

EXPLANATORY STATEMENT

1. At its meeting in Copenhagen, in June 1993, the European Council asked the European Investment Bank, in conjunction with the European Commission, to add ECU 3000 million to the temporary lending facility of ECU 5000 million adopted in Edinburgh in December 1992. ECU 1000 million from this sum was devoted to strengthening the competitiveness of SMEs by providing interest subsidies of up to a maximum of 3% per year for 5 years, the granting of which would be linked to job creation.
2. The setting up of the scheme was a political decision to send business leaders and citizens a message of support and encouragement for the creation of jobs. It insisted on urgency and stressed the need for the scheme to be implemented rapidly.

Was the scheme successful?

3. The success of the scheme seems impossible to quantify. The Court of Auditors highlighted a number of problems, many of which stem from the speed at which it was implemented. The main criticisms of the Court focussed on the following points:
 - a) Management and control systems were weak, and neither the EIB nor the Commission carried out adequate compensating checks.
 - b) The rules for applicants were not clear and consistent, which led to much confusion.
 - c) The EIB and the Commission concluded an Unwritten Agreement to arrange a derogation for the combination of this subsidised loan with other Community subsidised loans. Not only was this legally questionable, but Spain was the only Member State to benefit.
 - d) Distortion of competition, as banks without global loan contracts with the EIB were excluded.
 - e) Numerous breaches of regulations occurred. For example, during company takeovers, banks taking financial risks chose projects according to their own criteria, which they would have financed anyway. The “first come, first served” principle meant that project applications were rushed and involved investments where the financing and forecast impact on jobs was already known.
 - f) On-the-spot checks by the Court revealed that the number of jobs that were truly eligible was lower than the number subsidised. There is considerable dispute over the total number of ineligible jobs, with the Court claiming 20%, the EIB 8% and the Commission that the whole audit was flawed.
4. Of all the institutions, only the Commission persistently maintains that the scheme achieved its objectives, arguing that the scheme created 53,789 jobs on a microeconomic level. This may be proven statistically but, in terms of actual jobs created, the Court of Auditors insists that no causal relationship between the subsidies and job-creation can be established and that the subsidy was too low to make any real difference anyway. This conclusion is supported by the EIB and the Council and the consensus is that grants, rather than interest subsidies, are a better means for supporting small and medium-sized enterprises.
5. The EIB and the Commission claim that the Council imposed an unworkable programme on them at very short notice, which gave rise to the problems described above. The Council should note the lessons to be learned from this experience and should be particularly vigilant with any future initiatives.