



# T2S financial statements for the fiscal year 2017

August 2018

T2S operating statement (in €)<sup>1</sup>

## Financial results for the fiscal year

	Notes	2017	2016
<b>Revenues</b>	1	63,051,227	15,316,323
T2S fees charged to customers	2	61,997,698	15,295,296
Other income	3	1,053,529	21,027
<b>Expenses</b>		<b>(124,689,156)</b>	<b>(102,049,333)</b>
Services provided by the 4CB	4	(81,435,316)	(82,551,759)
Services provided by the ECB	4	(6,798,958)	(8,751,811)
Insurance costs and other expenses	5	(3,367,379)	(1,658,626)
Amortisation of T2S platform	6	(33,087,503)	(9,031,016)
Interest charged by NCBs	7	-	(56,121)
<b>Net Surplus/Deficit</b>		<b>(61,637,929)</b>	<b>(86,733,010)</b>

T2S financial situation (in €)<sup>1</sup>

## Year-end balances

Assets	Notes	2017	2016
T2S platform	8	360,705,950	390,127,267
Current accounts		19,157,420	7,122,184
Accounts receivable	9	-	150
Accrued income	10	5,430,942	2,926,455
Prepaid expenses		-	1,595,000
<b>Total Assets</b>		<b>385,294,312</b>	<b>401,771,056</b>

Liabilities	Notes	2017	2016
Pre-financing of T2S by the Eurosystem	11	490,393,816	469,069,077
Provisions for 4CB expenses	12	68,749,823	41,336,214
Other provisions	13	79,234	-
Accrued expenses	14	22,094,572	25,750,969
Accumulated deficit		(196,023,133)	(134,385,204)
<b>Total Liabilities</b>		<b>385,294,312</b>	<b>401,771,056</b>

<sup>1</sup> Figures might not add up due to rounding.

## Explanatory notes

The notes on the 2017 T2S financial statements provide explanations and additional information about the figures in the T2S operating statement and the T2S financial situation report for 2017.<sup>2</sup>

## Notes on the accounting policies

The T2S financial statements have been prepared in accordance with specific accounting policies developed by the T2S Board (Market Infrastructure Board). These policies are based on generally accepted accounting principles.

The T2S financial reporting framework covers standards for the annual T2S operating statement (expense and revenue accounts), the annual T2S financial situation report (asset and liability accounts), and the related disclosures.

## T2S platform

Owing to their integral characteristics, both the hardware and software of the T2S system are treated homogeneously and represented as a single tangible asset under “T2S platform”. The latter represents the carrying amount of the T2S platform. The value of the T2S platform is made up of the capitalised development costs paid to the European Central Bank (ECB) and the four service-providing central banks (4CB), capitalised interest incurred during the construction phase, and any additional development costs incurred during the operational phase, e.g. for new releases, after deduction of accumulated amortisation amounts and any impairment losses. Impairment tests are taking place annually as of the end of the migration phase (September 2017); impairment losses are recorded when the book value is lower than the asset’s expected recoverable amount.<sup>3</sup>

## Amortisation

The amortisation method reflects the pattern in which the asset’s future economic benefits are expected to be consumed. The method was based on the (expected) proportion of settlement volumes already migrated in T2S during the migration phase (completed in September 2017), and is thereafter based on a linear method from January 2018 to September 2027 (ten years after the end of migration).

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<sup>2</sup> For an introduction to, and further information on, the T2S financial statements, please refer to the [explanatory note](#) for the fiscal year 2015, which was prepared in parallel with the 2015 T2S financial statements.

<sup>3</sup> The recoverable amount of an asset is the greater of its “fair value less costs to sell” and its “value in use”.

## Pre-financing of T2S by the Eurosystem

This item relates to the amounts owed to the Eurosystem national central banks (NCBs) that have been pre-financing T2S, namely the covered costs incurred for both the development and the operation of T2S. This liability effectively reflects the expectation that the participating central banks will eventually be reimbursed for the development and operational costs included in the T2S pricing envelope (the total amount to be recovered through fees, including capital cost). The reimbursement will be funded by cash surpluses generated from T2S usage fees paid by T2S customers (central securities depositories (CSDs) and Eurosystem central banks). Reimbursement will begin once the collected fees exceed the annual operational expenses.

## Operating statement

During the operational phase, the T2S operating statement shows a net surplus or deficit, depending largely on whether the T2S fees are sufficient to cover the T2S operational costs, the amortisation of the T2S platform, impairment losses, if any, and other expenses. A deficit could trigger an extension of the amortisation period and/or a price increase in order to reach full cost recovery within the given cost recovery period (see Section 1.2). A surplus would make it possible to repay the pre-financing loan given to T2S by the Eurosystem central banks (see Section 1.1.3). The yearly surplus/deficit is reflected in the net accumulated surplus/deficit account.

## Income/expenses

Income and expense items are recognised once earned/incurred. In the operational phase of T2S, all operational costs are expensed as incurred to the T2S operating statement, while additional development costs (e.g. for new releases) are capitalised to the T2S platform and reported in the T2S financial situation report.

## Accrued income and expenses

Procedures are in place to calculate and establish, at each year-end, the costs incurred by T2S but not yet reimbursed to the service providers, as well as income not yet collected but earned in the reporting year.

## Post-balance-sheet events

This refers to relevant events that occurred after the reporting period which have a material impact on the reports for that period.

## Cost recovery

In 2010 the Governing Council of the ECB decided that T2S would be developed and operated under the principle of full cost recovery. The T2S Board regularly monitors developments that may affect the prospects of cost recovery. The cost recovery target is based on: i) the T2S pricing policy (see Schedule 7 (Pricing) of the T2S Framework Agreement and of the Currency Participation Agreement);<sup>4</sup> ii) a given cost recovery period; iii) the total costs for developing and operating T2S; and iv) the usage of T2S resources which generate revenues for T2S.

While the use of T2S resources is dependent on market dynamics, the Governing Council of the ECB aims to steer costs and adjust pricing in order to ensure that T2S is in a position to recover all, and only, its total costs in the long term. On 21 June 2018 the Governing Council of the ECB decided to extend the cost recovery period to the end of 2029 and increase the prices as of 2019 in order to ensure full cost recovery.<sup>5</sup> This decision was in response to the need to adjust the T2S pricing policy to the actual volume, cost, and revenue situation (see the [announcement for more information](#)).

## Notes on the Financial Statements

### 1 Revenues

The revenues for 2017 consist of T2S fees charged to customers and other income.

### 2 T2S fees charged to customers

The account “T2S fees charged to customers” shows the net revenues earned in 2017 by T2S. No discounts were applied in 2017 since the “fee holiday” regime (reduction of the monthly fees by one third) for the 9 CSDs that had signed the contract with the Eurosystem (the T2S Framework Agreement) by 30 April 2012 expired in November 2016. For those CSDs, as well as for the other 13 that had signed the contract by 30 June 2012, the prescribed one-off joining fee<sup>6</sup> was also waived.

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<sup>4</sup> Both documents are available on the T2S website, [www.t2s.eu](http://www.t2s.eu), under “Legal documents” in the section entitled [Key documents](#).

<sup>5</sup> See the T2S Framework Agreement, Section 2 (T2S pricing policy) of Schedule 7 (Pricing).

<sup>6</sup> See the T2S Framework Agreement, Section 5.9 (One-off joining fee) of Schedule 7 (Pricing).

## T2S revenues (in €)

Fiscal year	2017	2016
Gross revenues	61,997,698	18,767,583
Discount for fee holiday	-	(3,427,287)
T2S fees charged to customers	61,997,698	15,295,296

### 3 Other income

The other income for 2017 relates to a correction of the erroneous attribution of development costs for Release 1.2 in 2016 to the costs for "Services provided by the 4CB". These costs should have been capitalised and assigned to the T2S platform.

### 4 Services provided to T2S

As of its launch in mid-2015, T2S has been incurring annual operational costs which are paid to the service providers: to the 4CB for the running and maintenance of the T2S platform and to the ECB for its coordination activities. The costs for 2017 amounted to €88,234,274. These amounts include a provision for the costs from the 4CB service provider being higher than initially budgeted for (see note 11.1).

### 5 Insurance costs and other expenses

On 18 October 2017, the Governing Council decided to discontinue the T2S liability insurance coverage. The T2S insurance coverage was terminated on 18 December 2017.

In 2015, expenses for insurance services in an amount of €695,000 were wrongly reclassified from expenses for "Services provided by the ECB" and deferred to 2016 and 2017. In 2016, expenses for insurance services in an amount of €900,000 were wrongly reclassified from expenses for "Services provided by the ECB" and deferred to 2017. The deferred expenses are accounted for in the financial year 2017 and impact the net surplus/deficit for the year.

### 6 Amortisation

See note 8, "T2S platform".

## 7 Interest charged by national central banks

T2S owes interest to the Eurosystem NCBs for the loan that financed both the development of the platform and the commencement of T2S operations. The Eurosystem (pre-)financing effectively covers the liabilities of T2S vis-à-vis the T2S service providers (the 4CB) and the ECB for its T2S coordination functions.

Interest is accrued at year-end based on the annual weighted average balance of the pre-financing liability and on the annual average rate applied to the ECB's main refinancing operations (MRO rate). The accrued interest is compounded at year-end on the principal amount of the pre-financing of T2S by the Eurosystem.

The table below shows the balance of the Eurosystem's pre-financing of T2S. The increase is due to additional pre-financing payments to allow T2S to pay its operational costs to the service providers, and to the respective increase in interest owed by T2S.

In 2017 the interest rate applied was 0.0%. For this reason, no interest was calculated for 2017. An error in the calculation for 2016 is reflected in an additional attribution of €413 in 2017. This amount is booked under "Insurance costs and other expenses" and increases the pre-financing balance.

### Pre-financing payments for 2017 and respective compound interest (in €)

2017 opening balance	469,069,077
Payments for pre-financing	21,324,325
Revision of 2016 interest	413
Closing balance	490,393,816

## 8 T2S platform

As at the end of 2017, the T2S asset value comprised: (i) capitalised costs incurred during the development phase up to the launch date, (ii) accumulated amortisation, (iii) capitalised interest incurred during the development phase, and (iv) additional development costs related to change requests.

The present value of the T2S platform for the beginning of 2017 reflects the correction of the development costs for Release 1.2. The new value of the T2S platform following this additional capitalisation requires an increase in the 2016 amortisation of €23,836 which is booked in 2017 in "Insurance costs and other expenses".

The amortised amount for 2017 of €33,087,503 (2016: €9,054,852 including the revision) reflects the share of volumes that were migrated by the end of 2017 (the migration was completed in September 2017).

### Changes to the value of the T2S platform in 2017 (in €)

Year	Event	Amount
2017	Opening balance	390,127,267
2017	Additional capitalisation of development costs for 2016	1,053,529
2017	Additional amortisation for 2016	(23,836)
2017	Capitalisation of development costs	2,636,494
2017	Amortisation	(33,087,503)
2017	<b>T2S platform closing balance</b>	<b>360,705,950</b>

No impairment test was conducted in 2017. The T2S Board decided to start impairment testing after the end of the migration phase (end-2017), once the information on the full potential of T2S revenues would be available. Meanwhile, a reassessment of the T2S financial situation resulted in the above-mentioned decision of the Governing Council to realign the T2S pricing policy.

#### 9 Accounts receivable

As at 31 December 2017, the accounts receivable balance was zero. All the invoices were paid during the course of 2017.

#### 10 Accrued income

Accrued income reflects T2S revenue in December 2017 that had not yet been billed at year-end 2017.

#### 11 Pre-financing of T2S by the Eurosystem

The balance of the pre-financing of T2S corresponds to the loan that T2S received from the Eurosystem NCBs to cover the costs of developing, running and maintaining the T2S platform, plus the accumulated interest on the loan (see note 5). The cost recovery target (see Section 1.2) corresponds to the full balance of the pre-financing. On 31 December 2017, the outstanding loan with the Eurosystem amounted to €490,393,816 (2016: €469,069,077).

#### 12 Provisions for 4 CB expenses

An annual provision was set aside to cover an expected increase in service provider costs during the migration phase, relating to an increased use of resources for testing and migration activities. For fiscal year 2017, €27,413,609 was set aside, which brings the total for "Services provided by the 4CB" to €81,435,316, for the fiscal year. As at 31 December 2017, the total provision amounted to €68,749,823 (2016: €41,336,214).

### 13 Other provisions

Other provisions of €79,234 were set aside to cover an amount erroneously invoiced to CSDs in 2015 and 2016.

### 14 Accrued expenses

Accrued expenses relate to operational costs incurred in 2017 for which no invoice had been received by year-end. On 31 December 2017, a total amount of €22,094,572 was accrued (2016: €25,750,969).

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For specific terminology please refer to the [ECB glossary](#).

## **INDEPENDENT AUDITOR'S REPORT**

TARGET2-Securities

To: The Chairperson of the Market Infrastructure Board and its Members

Sonnemannstraße 20

60314 Frankfurt am Main

29 August 2018

### **Opinion**

We have audited the financial statements of TARGET2-Securities (the entity), which comprise the financial situation report as at 31 December 2017 and the operating statement and other explanatory notes. The financial statements have been prepared by the Market Infrastructure Board acting for the Eurosystem based on the TARGET2-Securities Financial Reporting Framework as approved on 24 March 2017 by the Governing Council of the European Central Bank.

In our opinion, the accompanying financial statements of the entity for the year ended 31 December 2017, are prepared, in all material respects, in accordance with the principles of the TARGET2-Securities Financial Reporting Framework as approved by the Governing Council.

### **Basis of Opinion**

We conducted our audit in accordance with International Standards of Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the entity in accordance with the ethical requirements that are relevant to our audit of the financial statements in Germany, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Emphasis of Matter**

#### **Basis of Accounting**

We draw attention to the explanatory notes to the financial statements section 1.1, which describe the basis of accounting. The financial statements are prepared to assist the Eurosystem in meeting its financial reporting requirements originating from the TARGET2-Securities Framework Agreement. According to Article 20 "Obligations of the Eurosystem related to the provision and use of the T2S Services" in Chapter 2 of the TARGET2-Securities Framework Agreement the Eurosystem shall provide the contracting Central Securities Depositories (CSD) with financial statements, reports and other information on TARGET2-Securities on a regular basis that fairly represent the business and financial conditions, result of operations and state of the cost recovery in relation to TARGET2-Securities on the respective dates or for the respective periods covered by such financial statements, reports and other information. As a result, the financial statements may not be suitable for another purpose.

We draw attention to the explanatory notes to the financial statements section 1.1.1, and here specifically to the fact that until the end of the migration phase to TARGET2-Securities in September 2017 an impairment test for the valuation of the T2S platform was not foreseen to take place, which is consistent with the principles laid down in the TARGET2-Securities Financial Reporting Framework.

Our opinion is not modified in respect of these matters.

### **Other matters**

We draw attention to the fact that the automated billing process in TARGET2-Securities is in the remit of the 4CB and therefore a full audit of the billing related information technology of the TARGET2-Securities platform could not be performed. However, we do not have any evidence of material misstatements due to a potential malfunction of the billing related information technology of the TARGET2-Securities platform.

### **Responsibilities of the Eurosystem and those charged with governance for the TARGET2-Securities Financial Statements**

The Market Infrastructure Board acting for the Eurosystem is responsible for the preparation and fair presentation of the financial statements in accordance with the TARGET2-Securities Financial Reporting Framework as approved by the Governing Council of the European Central Bank, and for such internal control as the Eurosystem determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Market Infrastructure Board acting for Eurosystem is responsible for assessing the entity's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the Eurosystem either intends to liquidate the entity or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the entity's financial reporting process.

### **Auditor's Responsibilities for the Audit of the Financial Statements**

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional skepticism throughout the audit.

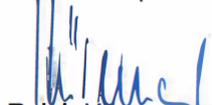
We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the entity to cease to continue as a going concern.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Yours sincerely,

Baker Tilly GmbH & Co. KG  
Wirtschaftsprüfungsgesellschaft (Düsseldorf)



Ralph Husemann  
Wirtschaftsprüfer



Dr. Stefan Fischer  
Wirtschaftsprüfer

