Decision of Eurostat on deficit and debt

Securitisation operations undertaken by general government Decision

Context

In the context of the Excessive Deficit Procedure monitoring, and following bilateral consultations with Member States, Eurostat has observed over the years various cases of securitisation of fiscal claims and of securitisation contracts with specific features, such as with DPP (deferred purchase price), with substitution clauses or with ad-hoc guarantees. Such securitisations have led to uncertainties as to whether the proposed recording in national accounts, in application of the existing guidance, would enter in conflict with the general principles of ESA 95 and whether comparability of the deficit and debt data was ensured between Member States.

In a number of instances, the observed securitisation operations seemed to have been purportedly designed to achieve a given accounting result, irrespective of the economic merit of the operation, whereas government had often not carried out a genuine transaction in substance, with limited transfer of risks and rewards. A specific task force led by Eurostat, with experts from various European countries, worked on the issue in 2005 and 2006, which led to the preparation of this Eurostat decision. After a substantial peer review process during the second half of 2006, the Committee on Financial and Balance of Payment Statistics (CMFB) was consulted on the issue, and provided its opinion to Eurostat in March 2007.

It is recalled that Eurostat published on 3 July 2002 an initial decision on the accounting treatment of securitisation, after consultation of the CMFB.

This second decision specifies the criteria applicable for deciding whether a securitisation operation should be recorded as borrowing or as disposal of an asset:

- for fiscal claims (tax receivables and social contribution receivables),
- for securitisation with Deferred Purchase Price (DPP) or equivalent clauses,
- for securitisation with substitution clauses, and
- for securitisation with specific guarantees.

Reminder on securitisation

Securitisation is where a unit, named the originator, transfers the ownership rights over financial or non-financial assets, or the right to receive specific future cash flows, to another unit (named the securitisation unit) that pays in exchange the originator from its own sources of financing.

Securitisation units set up specifically for a securitisation are often called special purpose vehicles (SPV), but existing entities can also undertake such arrangements. In order to finance the purchase of the financial or non-financial assets, or of the right to receive specific future flows, the securitisation unit borrows on its own account and not on behalf of the originator. Typically it issues bonds called "asset backed securities". The securitisation unit uses income or proceeds generated by the transferred asset or by the specific future flows, or by the sale of the transferred assets, to service its debt. Usually the lenders to the SPV will have a direct and legal claim on those assets, or on those flows, in the event of the SPV not paying the interest and principal due.

Securitisations have been traditionally undertaken by private corporations as well as by governments as a mean to achieve low cost of borrowing, because of the additional legal protection granted to the bond holder, and to attain balance sheet objectives. Private corporations have various reasons to undertake securitisations such as: improving capital solvency requirements; source of funding; enhancing financial ratios; or portfolio risk management. Governments often have other reasons such as fiscal policy constraints, improvement of public management, or rationalization of government property.

Until the early 2000s, government securitisations were infrequent and included only cases of financial assets such as loans granted by government or arrears in respect of tax or social contribution. However since 2000

several new types of securitisation transactions have occurred. Some arrangements covered the transfer of future flows not evidenced by an asset.

An important feature of securitisation arrangements is the allocation of the excess of the return on assets transferred (income and holding gains/losses) over the debt service, and whether this excess is returned to the originator in part or in totality, or is retained by the SPV owners. Mechanisms that arrange for the return of the excess, or of some of the excess, bear various names such as "deferred purchase price" (DPP) or "last tranche".

Applicable ESA 95 rules

The most important issue in national accounts is to determine whether the proceeds received by government are borrowing or disposal of an asset. It should be noted that when a disposal of an asset is recognized, an impact on the government deficit (net lending / net borrowing) may arise, when the asset is a nonfinancial asset or if it is determined that a revenue should accrue. One essential criteria is whether there has been a sufficient transfer of risks and rewards such that the operation can be considered as a sale. One important consideration is whether the "income flow" securitised is linked to an existing asset already recorded in the ESA 95 balance sheet, or not.

As part of the analysis of the problem, determining the classification of the SPV can also prove decisive, if the SPV is considered as a part of government or not, on the basis of criteria such as the autonomy of decision and/or its main activity.

Substance over form in drawing of account

National accounts principles (ESA 95) imply that the accounting treatment of operations should reflect economic reality (nature of entities and their economic behaviour), and not legal or administrative criteria. In case of potential or apparent conflict between ESA 95 provisions, national accounts decidedly give priority to substance over form, in a manner that prevents Member States to reach intended specific accounting results, by way of skilful design of legal arrangements for a given operation.

While the legal manifestation of an entity or of a transaction is relevant for the analysis of an accounting situation, it is a fundamental principle of the ESA 95 system that economic reality prevails over legal form. The system should allow to "see through" artificial arrangements designed for achieving a determined accounting purpose.

The principle of primacy of the economic reality over the legal features as a decisive focus in the national accounts system is notably expressed in ESA 95 paragraph 2.02: *"The units and groupings of units used in national accounts must be defined with reference to the kind of economic analysis for which they are intended, and not in terms of the types of unit usually employed in statistical inquiries. These latter units (enterprises, holding companies, kind-of-activity units, local units, government departments, non-profit institutions, households, etc.) may not always be satisfactory for the purposes of national accounts, since they are generally based on traditional criteria of a legal, administrative or accounting nature"*.

National accountants' practice recognized since long the need to reflect the economic reality when drawing accounts. The SNA 1993, the international equivalent of the ESA 95, also occasionally recognizes this explicitly, for instance in SNA 1993 paragraph 6.118 (on leases), in SNA 1993 paragraph 8.67 (on the measurement of compensation of employees) or in SNA 1993 paragraph 4.44 (on artificial units). In addition, the SNA 1993 makes abundantly clear that national accounts take inspiration from business accounting, notably with respect to the accrual principle: see SNA 1993 paragraph 1.58 and following.

The prescription that substance prevails over form is not specific to the statistics sphere and national accounts. Business accounting itself has a tradition of recommending for substance to prevail in case of conflict, so to achieve a faithful representation of reality. As an example, the *Framework for the Preparation and Presentation of Financial Statement* that introduces the *International Financial Reporting Standards* (IFRS) of the IASB (*International Accounting Standards Board*) states in its paragraph 35: "*If information is to represent faithfully the transactions and other events that it purports to represent, its is necessary that they are accounted for and presented in accordance with their substance and economic reality and not merely their legal form. The substance of transactions or other events is not always consistent with that which is apparent from their legal or contrived form. For example, an enterprise may dispose of an asset to another party in such a way that the documentation purports to pass legal ownership to that party; nevertheless, agreements may exist that ensure that the enterprise continues to enjoy the future economic benefits*

embodied in the asset. In such circumstances, the reporting of a sale would not represent faithfully the transaction entered into (if indeed there was a transaction)."

ESA 95 paragraphs

ESA 2.02

ESA 4.14 and 4.74

ESA 6.51

ESA 5.129

Securitisation of fiscal claims

The issue

Some governments have undertaken to securitize fiscal claims (i.e. tax or social contribution receivables), notably fiscal claims in arrears. The issue is how such securitisation should be accounted for, given the specific nature of those claims (they do not originate by mutual agreement) and given the fact that ESA 95 allows, for applying the accrual principle for taxes and social contributions, using a time adjusted cash method.

A question is how to record securitisation proceeds for fiscal claims in arrears, in case when their value differs in the ESA balance sheet, or when none was in practice ever recorded. The securitisation of fiscal claims being in concept a financial transaction (either borrowing or a disposal of a financial asset), should it be permitted that a government revenue be recorded in national accounts (i.e. reducing government deficit) at time of securitisation? Or should fiscal claims be deemed not sellable in the system owing to their nature and/or owing to their specific recording for taxes foreseen in ESA 95, as amended by Regulation 2516/2000?

Methodological analysis

Securitisation of future revenue

The Manual on Government Deficit and Debt (MGDD) clarifies that securitisation of future revenues (cash flows not related to existing assets) must be recorded as borrowing: "*to be treated as the sale of an asset, a necessary condition is that the receipts must be derived from a non-financial asset (like revenue from an asset and its future resale) or from a financial asset (like interest and reimbursement of loans) that exists in the government's balance sheet before the arrangement starts."* Only the securitisation of past revenues (which led to an appearance of a financial asset) can be recorded as a disposal of an asset.

The securitisation of oil proceeds cannot be reported as a sale of oil, as the oil has not yet even been extracted, and must be considered as borrowing. Similarly, securitisation in a given period of future taxes, i.e. taxes that accrue in future (e.g., mostly on future income or on future events), cannot be considered as revenue of that period but as borrowing. However, securitisation of tax receivables (i.e. future tax proceeds resulting from taxes already accrued) might conceivably be recorded as sale of an asset instead of as borrowing.

Nature of fiscal claims

The issue of the securitisation of fiscal claims is complex because of the specific nature of those claims. Taxes are uniquely established by the taxing powers of governments and can only be raised by governments. It is often unclear to what extent the originator transfers the control as well as the risks and rewards of these claims.

The securitisation (or the outright sale) of fiscal claims transfers some risks and rewards of the "asset", to the extent that the investor is exposed to some risks and rewards in as much as he will receive all or part of cash flows (paid by taxpayers) that are to a large extent uncertain.

However, fiscal receivables can be seen as a specific case of assets given that in the ESA 95 only general government, the institutions of the European Union or the Rest of the World can levy taxes (ESA 95 paragraphs 4.14, 4.77). This would seem to mean that post-securitisation tax revenue must be attributed to

general government in the national accounts system, whatever the specific collection arrangements under a securitisation. However, in the ESA 95, social contributions may be considered the resource of any sector. Securitisation operations involving such flows have been observed in practice. Nonetheless, given the proximity between taxes and social contributions, if securitisations of fiscal claims are to be recorded as borrowing by convention, it would also apply to social contributions collected by government as well as by private units or by other non government units (at least for compulsory social contributions).

In practice, government usually retains the responsibility for collection of securitised fiscal claims, which might imply that the underlying risks and rewards of collection rests within government. One question would be whether one can operationally distinguish or separate the retaining of collection tasks from the taxing powers (i.e. the ability to impose the tax) and/or from the bearing of risks/rewards on the instrument.

- A government retaining the collection tasks seems able to influence the actual collection rate, and thus the performance of the "asset", by deploying more or less resources for ensuring maximizing payments of arrears. In particular, government might be alone in deciding the means to be used to recover the claims, which might be less stringent (notably, for social reasons) than those used by private recovery agencies.
- The effective economic disposal of such fiscal claims supposes that government forfeited most if not all its rights, inclusive the right to implement a tax amnesty or cancellations. Otherwise it would seem that government has *de facto* not yet abandoned the effect that its general taxing powers have on the specific claims that have been allegedly sold.

Ownership of an asset would in general require control on that asset, as a precondition for reaping the risks and rewards attached to the asset. And it is questionable if control on fiscal claims can generally be deemed to be transferable by government. The investor might not have access to the names of the taxpayers, owing to legal or other confidentiality reasons, or might not be in a position to influence the performance on the assets (by allocating resources on recoveries or deciding on the types of follow-up actions to recover claims). In those circumstances, it seems questionable that the investor holds the original asset (the fiscal claim in arrears).

Accounting difficulties arising from Regulation 2516/2000 on the recording of taxes

If fiscal claims were to be deemed transferable as any other asset, a complex accounting difficulty would arise, due to the specific ESA 95 provision for recording taxes and social contributions excluding the “uncollectible part”, that might lead to heterogeneity of treatment across Member States.

Reminder on Regulation 2516/2000 on the recording of taxes (uncollectible part)

Regulation 2516/2000 of the European Parliament and of the Council amends the ESA 95 original text for the accrual recording of taxes and social contribution in order to ensure that taxes and social contributions expected not to be collected should not impact the net lending / net borrowing (article 2). Regulation 2516/2000 directs that in practice two data sources may be used (article 3):

- tax assessment with the use of a coefficient, and
- cash receipts with appropriate time adjustment.

Regulation 2516/2000 also directs that "over a reasonable amount of time" the two methods should lead to an equivalent impact on the net lending / net borrowing (article 2).

Valuation or existence of the fiscal claim in ESA 95 balance sheet

One consequence of Regulation 2516/2000 is that the ESA 95 balance sheets (of both government and the taxpayers’) record fiscal receivables at a reduced value, and not at the face value of the claims (ESA 95 para. 5.129). In addition, the time adjustment in many cases has been interpreted by many compilers to mean the administrative time lag between the accrual event and the normal liquidation ("simple time adjusted cash method") and not the further delays arising from the effect of the existence of claim delinquencies ("weighted time adjusted cash method"). Thus, in case the simple time adjusted cash method is used by compilers, delinquent claims are *de facto* not recorded in the national accounts balance sheets, contrary to when the weighted time adjusted cash method is used.

Potential conflict between ESA 6.51 and Regulation 2516/2000

According to the ESA 95 general principles, the differences between the disposal value and the balance sheet value must generally enter the revaluation accounts, and ESA 6.51 explicitly extends this to loans (AF.4) or receivables (AF.7). Thus, if considered as a disposal of an asset, the securitisation of fiscal claims should lead to entries in the revaluation account.

However this recording might create scope for conflict with Regulation 2516/2000 article 2 (i.e., the two methods should lead to an equivalent impact on the net lending / net borrowing "*over a reasonable amount of time*"), considering the risk of systematically underestimating tax revenue, including over the long run:

- Recording entries in the revaluation account can plausibly be found not to conflict with Council Regulation 2516/2000 article 2 when differences in valuation are small, might be of either sign, and thus might tend to compensate over repeated securitisation events, i.e. in cases when the "weighted time adjusted cash method" or the "assessment method" are applied for measuring tax revenues in national accounts.
- This, however, would not be the case, when the "simple time adjusted cash method" is applied: recording entries in other economic flows would then conflict with Council Regulation 2516/2000 article 2 (unless artificial matching entries would be also entered in the revaluations accounts in periods subsequent to the securitisation).

Compilation techniques

As a general principle, compilation techniques cannot lead to differences in recording. All securitisations should be treated the same, irrespective of whether a simple or weighted time adjusted cash method or an assessment method is used. Thus, the possible accounting difficulties resulting from the fact that the securitised assets might not have existed in the first place would need to be appropriately addressed.

If the rule that securitisations of fiscal claims were to be borrowing by convention was not adopted, and a disposal of a financial asset were to be recorded in some circumstances, then an issue is how to record the difference in valuation: whether the general rule of ESA 6.51 should prevail, and no revenue should be recorded at time of securitisation, or whether a narrow and specific interpretation of Regulation 2516/2000 might lead to an entry in government revenue at time of securitisation.

Government revenue on securitisation

If the rule that securitisations of fiscal claims were to be borrowing by convention was not adopted, and considering the need to abide to Council Regulation 2516/2000, a government revenue would need to be recorded in the accounts in case of securitisation (for the case the "simple time adjusted cash method" is used by compilers), and more plausibly at time of securitisation.

However, since securitisation operations are, in substance, balance sheet transactions (either borrowings or disposals of an asset), it would seem rather anomalous that a government revenue be recorded in national accounts at time of securitisation (i.e. reducing government deficit). This would provide scope for government to be able to conveniently generate accounting revenue at will, by mere financial engineering, and put at risk the comparability of the data across Member States. Finally, the measurement of government deficit would largely depend, from one year to the next, on the compilation choice made by the national compiler, which seems unjustifiable and may even create adverse incentives for national authorities to select one suboptimal compilation method against another.

Another alternative to revise backward government tax revenue series, each time a securitisation of tax claims (meeting the other criteria for recognizing a sale) is carried out, is not palatable. Such revisions are disturbing to users and, as a matter of principle, revisions in data should generally not reflect new events but only new information on the appropriate measurement of past events.

Thus, there cannot be any impact on the deficit at time of securitisation of fiscal claims, and the securitisation proceeds must lead to an increase in debt. Cash receipts forwarded to the securitisation unit are to be recorded, first, on the inflow side, as government revenue in the accounts of government, as if no securitisation had occurred, and, second, on the outflow side, as debt servicing (with a part recorded as interest, which is a government expenditure, and the remainder as a financial transaction: debt redemption). Thus, an impact on the deficit will be recorded in subsequent accounting periods following the securitisation, for that latter amount of proceeds forwarded to the securitisation unit and corresponding to debt redemption.

Decision

Eurostat has decided that all securitisation of fiscal claims should be treated as borrowing, because of the likely direct or indirect control that government would keep, and because it is appropriate that
all securitisations of fiscal claims be treated the same (in consideration of the fact that the various compilation techniques should not lead to heterogeneity of treatment for EDP reporting) taking into account the principles set by Regulation 2516/2000.

Securitisation with Deferred Purchase Price (DPP)

The issue

Securitisations undertaken by government commonly comprise a deferred purchase price (DPP) clause, or equivalent (such as last tranche), that foresees the allocation to the originator of part or all of the excess between the actual proceeds on securitised assets or future income flows, and the cost of debt.

The type of securitisation operations covered typically involves a payment to government for the sale of a government asset for an initial price lower than its true market price (difference called here the "sale discount"), with the obligation of the purchaser to pay a second instalment to the government at the end of the operation. When the final revenue or proceeds for the SPV, after all assets have been sold or cash flow received and all operating costs have been covered, is more than the initial sale price, some or all of the difference (called here "surplus") will be transferred to the originator, here government, according to some pre-determined conditions or formula.

Eurostat has observed that the surplus is often allocated in its entirety to government ("100% DPP"). It seems questionable that a sale could be recognized in national accounts in cases of 100% DPP, given that the originator retains all rewards on the asset, while the transfer of risks is itself in part mitigated by the authorized sale discount of up to 15%.

The main issue to be clarified is whether the existence of a DPP to be paid to government in the context of the securitisation operation could possibly constitute a reason for classifying the securitization proceeds as government borrowing, or whether some thresholds should be considered.

Methodological analysis

Some cases of actual contracts have been observed in Member States, where securitisation SPVs are non-profit entities and where the remaining cash, after all bond-holders have been reimbursed and all expenses paid, has either reverted to the originator or has been disposed of in some other way (such as a donation to charity).

The guidance of the original MGDD chapter on securitisation operations undertaken by government seemed somehow incomplete and not to have taken enough into account, at an operational level, the principle that in the context of a transfer of assets, the rewards must be transferred to the purchaser of the assets, if the transfer is to be considered as a true sale.

On the one hand, the original MGDD chapter clearly indicates that for a true sale to be recognized, the rewards must be transferred: "*the purchaser, not the government, must be allowed to benefit if the income is higher than expected when buying the asset, and must suffer the consequences if the income is lower*". It seems that it cannot be argued that the purchaser of the assets can be deemed to benefit from the profits of the securitisation operation in those cases in which all the surplus of the operation will be transferred at some stage to government through a DPP (100% DPP). However, on the other hand, footnote 7 as well as the equilibrium of the section 4.1 page 9 of the original MGDD chapter could suggest that a 100% DPP is implicitly allowed to be consistent with a sale criterion.

When looking back at ESA 95 general principles, a sale cannot be recognized in national accounts in cases of a 100% DPP, given that the originator retains all rewards on the asset. Although some of the risks are transferred, this is mitigated by the authorized sale discount of up to 15%. In case of some assets such as real estates, which prices tend to increase over time, the risk of loss is extremely limited for holding periods in excess of a few years. The 15% discount can also noticeably mitigate the risk of an initial mis-pricing of such assets, an important consideration for short holding periods. Thus it appears clearly that a 100% DPP conflicts with the notion of a sale, and the MGDD chapter footnote is found to be an anomaly.

It could also seem questionable that the purchaser of the assets can be deemed to benefit from the profits of the securitisation operation in those cases in which some of the surplus, though not all, of the operation will be transferred at some stage to government through a DPP. However, at the same time, the original MGDD chapter expands heavily on the rule to apply for judging if a securitisation is borrowing or is a disposal of an asset in case a DPP exists, by way of using the 85% criteria.

Setting a threshold beyond which the presence of a DPP would justify classifying the securitisation as borrowing would be necessary, because 100% DPP at least should justify a borrowing recording. A threshold set so that the DPP would not exceed the sale discount, would seem natural in that the seller should not be permitted to get more than the market price as measured at time of sale. On the other hand, thresholds are arbitrary and can be prone to provide unhealthy incentives for contract specifications.

Another option is to consider that a sale recording in the context of securitisation requires that all risks and rewards be in substance transferred, with the implication that the existence of a DPP is a sufficient condition to lead to a borrowing recording. According to ESA 95 principles, when an asset is sold, it is natural that only the purchaser of the asset should reap the benefit of an increase in the value of the asset after the sale, and that the seller should not retain in substance claims or special rights in the asset after the sale, with a potential to materially affect the return on the asset obtained by the acquirer.

Decision

Eurostat has decided that all securitisation with a deferred purchase price clause, or a similar arrangement should lead to the classification of a securitisation operation as government borrowing, because such clauses are evidence that not all the risks and rewards of the operation have been transferred to the purchaser.

Securitisation with substitution clauses

The issue

Some government have undertaken securitisations that comprise a substitution clause, which typically involves an option to substitute the transferred assets, according to pre-determined conditions and modalities, if it turns out ex-post that the securitised assets do not exist.

This issue is whether the existence of a substitution clause (except for marginal cases deriving from technical and material errors) in a contract concerning securitisation operations involving the government is a sufficient condition to classify the operation as government borrowing, to the extent that the existence of such a clause can have a bearing on the actual transfer of risks and rewards between the selling and purchasing entities.

The issue is also whether a securitisation operation can be considered as a sale of asset if the existence of the assets concerned is not beyond all doubt at the time of their transfer.

Methodological analysis

In the private sector, clauses concerning the substitution of assets are sometimes observed in arrangements relating to securitisation of claims, notably in the case of commercial claims carried out by non-financial corporations. It is a kind of safety measure, as the acquiring unit is generally not in a position to check beforehand the complete materiality of the claims. These clauses might also help reduce litigations costs between parties, thus improving the economics of securitisations.

However, to the extent that a portfolio of claims is transferred, the market price for the portfolio contains a certain discount for assets that might turn out to be worthless for various reasons. Hence, there seems to be only a limited necessity for a substitution clause. This is particularly the case for governments, which are trustworthy parties and which can also adequately limit, by way of administrative and legal actions, disputes and litigation costs.

It is also questionable if assets whose ownership is under dispute at the time of the sale (being the object of a procedure in front of a judicial body) could be included in the portfolio transferred by government to the acquiring unit. Assets being disposed of should be fully assessed and their existence considered unquestionable. If a judicial body is entitled to take a final decision, it would seem that such an assessment has not been fully made.

In case substitutions of assets provide additional insurance against credit risks, due to changes of the creditworthiness of the debtor, or against market risks due to changes in market prices over time, such clauses (other than case of material errors) change the transfer of risks. Moreover, the practical implementation of such substitution clauses can in itself determine a shift in the balance of risks and rewards between the buyer and seller. This would notably be the case when assets with low market value would be replaced with assets with higher market values (because they carry a lower credit risk), although their

nominal values could be equal or very similar. This can be the case when old claims are replaced with younger claims. In this case, one could wonder why government accepts the existence of such a clause. An extreme case could be that all assets originally included in a securitisation operation are substituted. The replacement could significantly reduce the risks or even potentially make the operation risk free for the purchasing entity. Governments may have for reputational reasons an interest to generously action substitution clauses.

Decision

Eurostat has decided that all securitisation with a clause in the contract referring to the possibility of substitution of assets (except for marginal cases deriving from technical and material errors) should lead to the classification of the operation as government borrowing.

Securitisation with specific guarantees

The issue

Some government have provided, in the context of securitisation operations, ad-hoc guarantees ex-post in the case of one or more events or government actions that are specifically or almost specifically related to the SPV and do not apply to economic units more generally. The issue is whether this justifies a classification or a reclassification of the operation as borrowing and when, if the guarantee was granted by the government ex post (e.g., in order to compensate for a failure of the SPV to repay the bonds issued).

The section of the original MGDD chapter on securitisation dealing with guarantees specifies that the granting, in the context of securitisation operations, of a guarantee by government to a securitisation unit covering the risks that are supposed to be borne by the SPV entails that the transfer of assets is not considered as a true sale.

Methodological analysis

In general, the granting by government of a guarantee to an SPV implies an incomplete transfer of risks and demonstrates that there is no effective change in ownership of the assets. Therefore, in the case of a securitisation operation undertaken with an SPV, this would imply the classification of the SPV in the general government sector, or the recording of an implicit loan from the SPV to government. Such guarantees can be provided in practice by way of various means, including by use of derivative contracts.

While the original MGDD chapter is clear for cases when the SPV receives outright financial assistance, or promises thereof, from government, when it has difficulties to repay the issued bonds, the MGDD chapter needs to be clarified for the accounting treatment of "compensation" payments in the case of one or more events or government actions that are specifically or almost specifically related to the SPV (and not applicable to other economic units more generally).

The original MGDD chapter stipulates exceptions to the general rules concerning guarantee:

- for guarantees related to natural disasters, terrorism or war (provided that the guaranteed amount does not exceed the value of the transaction).
- for "*guarantees given to protect against the risk of government changing the law or taking other action that reduces the value of the securitised assets"*, when *"such guarantees would not be restricted to a change in conditions related to the specific assets transferred to the securitisation unit but would have a larger impact, similar to coverage of exceptional events."* If the guarantee would not have a "larger impact", governments could at any time change some of the conditions and use this as an opportunity to take back some or most of the risks of the operation.

In the original MGDD chapter, Eurostat already decided that if the securitisation contract stipulates ex ante a government compensation to the SPV in the case of one or more events or government actions that are specifically or almost specifically related to the SPV and do not apply to economic units more generally, the operation should be classified as government borrowing.

One might wonder why government would decide to intervene in favour of a unit which is not part of government and with which it has no obvious property link, after a sale of assets in the context of a securitisation operation. One possible reason, is that government has an interest in the SPV being able to reimburse its debt, notably so that the SPV would have been able to maintain, for instance, its favourable rating, with an aim to preserve a reputation capital.

In this situation, one should carefully look at whether the fact that government provided a guarantee to the SPV, and only to the SPV, after the securitisation (and not before) may or may not be a reason for reclassifying the SPV inside government.

In addition, the original MGDD chapter does not seem to cover cases of "indirect guarantees", where a government unit is not providing a guarantee on the debt or revenue of the securitisation unit but takes the commitment to provide in any case (unconditionally and possibly even at the outset of the operation) resources to an entity (or another government unit) that has securitised future revenues from assets. This would be the case, for instance, when an SPV, facing a shortage of liquidity which would prevent it from repaying the bondholders, would then be able to borrow on the financial markets only with a guarantee from government, or when there may be transfers from central government to sub-national governments units (local and regional).

The provision of a guarantee ex-post should lead to a reclassification of the operation, independently of whether the compensation exceeds or not the alleged damage, owing to the difficulty to ensure that the action and the compensatory payment was not designed to provide benefits to the SPV.

Decision

Eurostat has decided that if the government compensates (for instance in the form of cash, a debt assumption, or a direct or indirect guarantee) the SPV ex-post, although this was not required according to the contract, the operation should be reclassified as government borrowing with (possibly) an impact on the general government surplus/deficit in the year of the compensation.