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Directorate D Government Finance Statistics (GFS)

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Statistics Lithuania
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Subject: Ex-post advice concerning the statistical treatment of a PPP project for the renewal and maintenance of street lighting in the town of Lentvaris, Trakai District Municipality

Ref.: Your letter of 29 March 2023/SD-308

Dear Ms Petrauskienė,

Following your letter in reference and after analysing the documentation provided, Eurostat with this note is delivering its opinion on the statistical treatment of the PPP agreement in subject.

A. Description of the case

With a note dated 29 March 2023, the Lithuanian statistical authorities formally requested Eurostat's ex-post advice concerning the statistical treatment of a PPP project for the renewal and maintenance of the street lighting infrastructure in the town of Lentvaris, Trakai District Municipality.

The Trakai District Municipality administration (from now on, the Authority) and a private party (the PPP Partner) signed the partnership agreement on 5 August 2022. The contract signed foresees the renewal and maintenance of the street lighting infrastructure in Lentvaris town. The renewal of the street lighting infrastructure will be done "within 12 months from the date of signature of the contract", with a planned capital investment of EUR 1.322.195,8 (excluding VAT) (Annex 2, page 46).

The PPP Partner will be responsible for providing maintenance and repair services for a period of 14 years following the investment phase.

The Authority will remunerate the PPP Partner through periodic fixed payments, which will amount to a total of EUR 2.570.603 (excluding VAT) over the 14-year contract period (Annex 1, page 46). Additionally, the PPP Partner will receive further payments based on the indexation of all costs related to the provision of services following the construction phase.

B. The accounting issue

The Lithuanian statistical authorities asked Eurostat for an ex-post opinion concerning the appropriate statistical recording of the project in national accounts and in the EDP statistics.

The Lithuanian statistical authorities provided Eurostat with a copy of the agreement, in Lithuanian and English, as well as their opinion regarding the accounting classification.

In their own analysis of the PPP contract, the Lithuanian statistical authorities concluded that this project should be recorded off the balance sheet of government.

C. Documentation provided

The Contract's Index includes the following documents related to this contract, all dated on August 5, 2022:

- Contract for the renewal and maintenance of the street lighting
- Private entity proposal (Annex 1)
- Investment Execution Plan (Annex 2)
- Lighting Infrastructure Transfer act (Annex 3)
- Risk allocation matrix between Parties (Annex 4)
- Remuneration calculation Procedure (Annex 5)
- Events of non-compliance and penalties (Annex 6)
- Direct agreement (Annex 7)
- Guarantee of performance of the contract (Annex 8)

Eurostat received an English translation of all the above documents, except for Annex 7 (Direct agreement). Eurostat received the full version of the contract (including Annex 7) in Lithuanian.

Eurostat also received:

- The analysis of the statistical treatment of this PPP prepared by Statistics Lithuania
- Amendment to the above contract, signed by the parties on 28 February 2023.

On 22 June 2026, Eurostat requested some clarifications and a readable version of the Financial Business Model. The Lithuanian statistical authorities provided the missing documentation on 18 July 2023.

D. Methodological analysis and clarification by Eurostat

In the following paragraphs, Eurostat will analyse the PPP Agreement under the lens of the provisions included in each chapter of the Guide to the Statistical Treatment of PPPs,[1] published jointly by the EIB and Eurostat in September 2016 (hereafter PPP guide). The subsequent paragraphs will be numbered to correspond with the Themes in the PPP Guide for a structured evaluation.

D.1 - The main features of a PPP

The definition of a PPP included in the PPP Guide requires that, for statistical purposes, the Authority is classified inside the general government sector, and the PPP Partner is classified outside the general government sector.

The Trakai District Municipality is obviously part of the general government sector.

[1] https://www.eib.org/attachments/thematic/epec_eurostat_statistical_guide_en.pdf

As for the PPP Partner, Baltled UAB, it is a privately-owned entity established in 2005, with most of its capital (95%) owned by another private entity, EJ Energy UAB.

The PPP Partner was selected through an open tender procedure, which was launched four times. Only one bidder participated in the last one.[2]

The Trakai District Municipality is labelled "the Public entity" in the contract examined, and it will be labelled "the Authority" in this advice; the PPP Partner (Baltled UAB) is labelled as "the Private entity" in the contract examined, and it will be labelled "the Partner" in this note, in line with the terminology used in the PPP Guide.

The parties involved in this PPP contract satisfy the requirements established by the PPP Guide, pages 19-21.

D.1.1 Type of asset

The PPP Guide (page 23) requires that the investment must be directed towards a clearly identifiable and specifically designed asset. Additionally, the expenditure incurred by the PPP Partner in constructing a new asset or renovating or refurbishing an existing asset should be substantial in nature.

For a project related to the renovation of an existing asset to be considered a PPP contract, "*the amount of capital expenditure by the Partner under the contract must represent at least 50% of the value of the asset after completion of the works*" (PPP Guide, pages 23-24). The value of the asset after completion of the renovation works can be calculated looking at the capital expenditure that will be incurred by the PPP Partner.

With this contract, 67.82% of the current lighting points in Lentvaris will be renewed. Moreover, the project scope also includes a significant extension of the street-lighting infrastructure, which includes installing lighting in streets where there was either no existing infrastructure at the time of contract signing or only a partial section of the street was illuminated.

The installation works will include:

- Replacement of old and inefficient street lights with new, energy efficient LED street lights;
- Installation of new LED street lights on the streets or sections of streets to be covered;
- Installation of new bollards with foundations;
- Replacement of unusable luminaire brackets with new ones;
- Electrical cabling/layout works;
- Installation of control system and other associated works.

The Contract aligns with the "type of asset" requirements as outlined in the PPP Guide on page 23.

D.1.2 Duration of the Agreement

According to the PPP Guide, the contract must have a minimum duration of ten years and the asset being developed through the PPP should have an economic life that exceeds the contract's duration. At the same time, a PPP contract should cover a meaningful part of the economic life of the asset.

[2] The public procurement report is available at: https://cvpp.eviesiejipirkimai.lt/ReportsOrProtocol/Details/2022-695080?formTypeId=1

This Contract has an operational phase of 14 years, which seems to represent most of the economic life of the new assets. In fact, according to Art. 4.3 of the Contract, when ownership of the renewed lighting infrastructure transfers to the Authority, the infrastructure must meet specific quantitative and qualitative standards. It should also be capable of supporting "for the continued proper operation of the Lighting Infrastructure … for a period of at least two years from the time of handover", considering normal wear and tear.

Assuming that the economic life of the Lighting Infrastructure is at least 14+2=16 years, Eurostat observers that the Contract does cover a meaningful part of the economic life of the PPP assets, as required by the PPP Guide, page 24-25.

D.2 Design and construction of the PPP assets

Responsibility for dismantling the old lighting infrastructure, designing and installing the new energy efficient LED lights lies with the PPP Partner (Art. 7.4-7.6).

The upgrading of the street lighting will be carried out within 12 months from the date of signature of the Contract (Annex 2, Art. 2).

The specific criteria that will be used for determining whether the construction of the asset is complete were missing from the initial Contract, but were introduced with an Amendment signed by the parties on 28 February 2023. This amendment added "Annex 9 - Evaluation and acceptance of Lighting Infrastructure" to the Contract, which specifies how the Authority will assess if the new lighting system has been installed and responds to specific performance requirements. Eurostat assumes this amendment, received separately from the signed Contract, represents an integral part of the analysed Contract.

In the Contract examined, considering the Amendment of 28 February 2023, Eurostat does not detect any of the "Design and construction of the PPP assets" features relevant for the statistical treatment of the contract described by the PPP Guide, Theme 2, pages 35-36.

D.3 Operation and maintenance of the asset

After the installation of the new lighting system, during the operational period, the PPP Partner will be responsible for operating the street lighting system and providing maintenance and repairs (Art.11.3 and 12.2).

Annex 6 outlines the penalties that will be imposed in case of "non-conformity." The list of non-conformity cases includes instances of "lighting failures" and other functionality issues, which must be rectified within a few hours. In such cases, deductions will be made from the defined operational payments, and additional fines will be applied if there are repeated occurrences of non-conformity. The relevant information can be found on pages 64 to 66 of the Contract.

In case of damage to the lighting system caused by "vandalism or other events", the damage risk is borne by the Authority (Art. 11.5). Annex 4, clause 3.2 also specifies that the Authority will take the risk in case the quality of the renewal and maintenance service is not ensured due to intentional or unintentional acts of third parties (vandalism, acts of hooliganism, traffic accidents, theft).

According to the PPP guide, Theme 3, page 39: "*the fact that the Authority takes responsibility for maintaining and/or replacing any component of the asset does influence the statistical treatment and is an issue of HIGH importance for the statistical treatment*".

However, in this Contract "vandalism" is listed in the Relief events (Art. 22.1.11), which makes the above assessment irrelevant based on PPP Guide (see section D.6).

Eurostat observes that the provisions related to the "Operation and maintenance of the asset" fulfil all the main requirements specified by the PPP Guide, Theme 3, pages 38-42.

D.4 The payment mechanism

The typical payments associated to a PPP are the "*Operational payments"*, regular payments that the PPP Partner is entitled to receive after the construction of the PPP asset is completed.

According to the PPP Guide, the payment mechanism must allow for adjustments to the operational payments in case of unavailability or poor service performance.

In the Contract, the payment mechanism is defined in such a way as to cover the costs incurred by the PPP Partner for the initial investment (including financing costs) and for the provision of maintenance and repair services (Art. 18.2 and Annex 5). Deductions and penalties are foreseen for cases of non-compliance.

If, due to the fault of the PPP Partner, the lighting infrastructure is not fully operational, the Partner shall not be paid in full. The remuneration to be paid is proportional to the part of the lighting that is in working conditions (Annex 5, Art. 8).

The Authority must notify the Partner if the lighting infrastructure or any part of it becomes unsuitable, providing supporting documentation of the unavailability (Annex 5, Art. 8.3 and 8.4).

Eurostat notes that the "payment mechanism" in the Contract does satisfy all the main requirements specified by the PPP Guide, Theme 4, pages 45-58.

D.5 Other payment arrangements

According to the PPP Guide, page 64, the PPP Partner should not be entitled to receive operational payments before the construction of the asset is completed.

In the Contract, it is specified that the Partner shall be remunerated in each month of the operating period (Art. 1.1.21).

The Partner shall bear the risks of changes in the prices of the lighting infrastructure during the installation phase (Annex 7.2).

The monthly operational payments/remuneration for maintenance, administration and management services are indexed to the Harmonised Index of Consumer Prices. The index is based in the month of submission of the proposal ($SVKI\_index^0$, Annex 5, Art. 3).

In the Contract, the cost of electricity (during the investment and operational periods) is borne by the PPP Partner and reimbursed by the Authority, invoiced separately from the operational payments (Art. 7.7, and Annex 5 Art.10). The Partner must keep records of the electricity paid, to ensure the Authority is able to pay for these costs separately (Art. 3.1.6).

The WHERAS of the Contract, page 4, specify that the Authority aims "to improve the quality and energy efficiency of the street lighting in the town of Lentvaris".

According to the PPP Guide, paragraph 5.3, page 67, the fact that the Authority takes the price and volume risk related to the energy consumed "on projects whose core objective is to deliver energy efficiency" is an issue of MODERATE importance for the statistical treatment of the project.

D.6 Compensation, relief and force majeure events

According to the PPP Guide (page 75), "*provisions by which the Authority takes or shares the risk of events that affect the delivery of the project do not influence the statistical treatment if all of the following conditions are met: There is a finite number of well-defined events (i.e. the Authority should not be exposed to an indefinite number of risks); The events do not capture changes in macro-economic conditions; The events are not attributable to the acts or omissions of the Partner; and the events, or the consequences of the events, are not reasonably foreseeable or estimable".*

Furthermore, the provisions should "*not compensate or provide relief for anything other than the effects of the event in question*" and "*exclude from any compensation due by the Authority any amounts that the Partner should be able to recover under the required insurances*" (PPP Guide page 81).

Well-defined lists of Relief events (Art. 22.1), Compensation events (Art. 23) and Force majeure circumstances (Art. 24.2) are included in the Contract, none of them attributable to the PPP Partner or related to macro-economic conditions.

The Contract also states that no deductions or penalties shall be imposed on the PPP Partner in case of Relief events (Art. 22.4).

If the Partner fails to provide the maintenance services due to force majeure, the Authority can suspend the payment related to the provision of the services until the force majeure event ceases to exist (Art. 24.7).

In the Contract, Eurostat did not detect any of the "Relief and force Majeure" features relevant for the statistical treatment of the Contract described by the PPP Guide, Theme 6, pages 75-78.

D.7 Changes to the PPP contract

The Contract outlines the circumstances under which both parties can agree to amend the terms (Art. 27 and 28). Among the listed cases: "In accordance with official requests (letters) from the European Union and/or the Lithuanian authorities to ensure that the Contract is not recorded in the government balance sheet" (Art.27.1.4).

In the Contract, the parties have the right to request a modification of the operational payments in three cases: a) if the costs are modified following a material change in legislation, b) if the modification is lower than 10% of the value of the contract (on a cumulative basis) and c) if the modification is due to circumstances which the parties could not have foreseen and if those modifications are below 20% of the value of the contract. The PPP Partner has the right to request a modification in case of changes in its costs (Art. 28.1.2) and the Authority has the obligation to reimburse the additional costs for the provision of maintenance services, but not those related to the initial investment (Art. 28.2.2). The monthly remuneration for maintenance services is already indexed to the HICP (see section D.5 in this note), therefore this further possibility for the Partner to request additional payments in case of changes in its costs shifts the risks from the Partner to the Authority.

According to the PPP Guide, "*an obligation on the Authority to bear the financial consequences of a partner change proposal does influence the statistical treatment and is an issue of HIGH importance*" (PPP Guide, Theme 7, page 82).

D.8 Changes in law

Art. 27.1.1 foresees that the Contract might be amended in case there is a "material change" in the legislation. This amendment requires the agreement of both parties.

Clause 1.1.22 of the Contract explains that "Material Change in Legislation" - means a change or new enactment of Special Legislation **…** affecting the rights and obligations of the Parties under the Contract.

Art. 23.1.1 of this Contract attributes to the Authority the risk deriving from "Material" changes in the legislation introducing additional requirements for the provision of the renewal investment and maintenance services.

Eurostat presumes that, similarly to what happens in other Lithuanian PPP contracts, the Partner shall assume the risks of changes to the law of a general nature (e.g. changes in the regulation on corporate income tax, changes in employment law).

Eurostat observes that the "Changes in law" features included in the Contract do satisfy all the main requirements specified by the PPP Guide, Theme 8.

D.9 Insurance

During the investment and operational periods, the PPP Partner is obliged to conclude insurance contracts at its own expense and risk, for its own benefit (Art. 25.1 and 25.2).

According to the originally signed Contract, the Partner had the possibility not to establish the insurance contracts if the annual cost of the insurance exceeded 5% of the remuneration of the 12 previous months (Art. 25.3).

Eurostat acknowledges that this provision has been removed from the Contract due to the amendment made on 28 February 2023, Art.3. If this had not been the case, the following PPP Guide provision might have been applicable:

According to the PPP Guide, "*Provisions that assess the commercial viability of insurance by reference to any other test (e.g. an increase in insurance costs above a specified level) do influence the statistical treatment if they are likely to apply in a scenario other than disruption in the insurance market. Where this is the case, the issue is of HIGH importance to the statistical treatment*." (PPP Guide, Theme 9, page 90).

Eurostat observes that the "Insurance" features included in the amended version of the Contract do satisfy all the main requirements specified by the PPP Guide, Theme 9, pages 89-90.

D.10 Warranties and indemnities

A section of the Contract covers "Warranties by the parties" (Art 40. and 41), which outlines the respective obligations for both the Authority and the PPP Partner.

The Contract does not include any provision related to the need of the PPP Partner to indemnify the Authority for losses incurred because of the Partner's performance.

However, Art 45.1 foresees that the PPP Partner shall provide a Performance Guarantee (from a credit institution or an insurance company) that shall be valid "until at least the start of the Operational Period" and correspond to at least 5% of the total remuneration over the years. This Guarantee shall be used to cover losses caused by the fault of the Partner (art 45.2). Eurostat considers that this feature does not substantially affect the allocation of risks and rewards described in the different sections of this advice.

In the Contract, Eurostat did not detect any of the "Warranties and indemnities" features relevant for the statistical treatment of the Contract described in the PPP Guide, Theme 10, pages 93-95.

D.11 Early termination of the PPP contract

In the Contract, the cases of early termination due to the fault of the Authority are listed under Art. 29.1 and do not include cases of the Authority taking risks related to the PPP Partner's performance.

Art. 32.1 defines the cases when the Authority has the right to terminate the Contract unilaterally due to the fault of the Partner.

In the Contract, Eurostat did not detect any of the "Early termination of the PPP contract" features relevant for the statistical treatment of the contract described in the PPP Guide, Theme 11, page 98.

D.12 Compensation on early termination of the PPP contract

The cases of Compensation on Early termination of the Contract are covered by Articles 32-33. The compensation that the Authority will have to pay to the PPP Partner in case of early termination due to the fault of the Partner is defined by Art. 33.1, as follows:

a. Real value of the remuneration over the term of the Contract which has not yet been paid;
b. Minus the amount of deductions and penalties already applied;
c. Minus the direct losses incurred by the Authority because of the termination of the Contract, including the costs of rectifying deficiencies in the lighting infrastructure and the additional costs of managing and maintaining the infrastructure;
d. Minus eventual Partner's claims;
e. If the compensation calculated under clause 33.1 is negative the Partner will have to compensate the Authority;
f. The value of the compensation determined with the above clause may not exceed the market value of the Lighting Infrastructure, as determined at the date of termination of the contract.

This method for determining the compensation on early termination due to the Partner's fault (a. minus b, c and d) is assimilable to the market value approach, as presented in the PPP Guide, section 12.1.3/Approach 3 (see pages 103-106). At the same time, the introduction of a cap component (f.) seems to approximate the book value approach, presented in clause 12.1.4/Approach 4 (pages 106-107).

In relation to the market value approach, the PPP Guide (page 104) requires that *"The methodology for estimating the market value of the contract (where the re-tendering process is not followed) is designed to reflect the approach that the market would take in valuing the PPP contract and not to ensure the recovery of the Partner's incurred costs or outstanding debt. The methodology needs to take into account any remediation costs resulting from the Partner's under-performance (i.e., the forecast cash flows should take into account costs to complete/rectify the asset as well as additional operation, maintenance and financing costs)."*

Art. 33.1/c explicitly considers the direct losses incurred by the Authority because of the termination of the contract, including, but not limited to, the costs of rectifying deficiencies in the lighting infrastructure and the additional costs of managing and maintaining the infrastructure.

Eurostat notes that, in the Contract examined, the provisions for determining the compensation the Authority will have to pay in case of early termination due to Partner's fault based on the market value of the contract seem to be in line with the requirements of the PPP Guide, pages 103-106.

Art. 33.1/f introduces a cap on the compensation that the Authority will have to pay, which cannot be higher than the market value of the Lighting Infrastructure, as determined at the date of termination of the contract by an independent appraisal made in accordance with the Lithuanian laws.

As the Lithuanian Central Projects Management Agency explained, in the context of the analysis of another PPP contract, "According to the Rules, the valuation could be carried by comparative method or cost method or income method or mix of these methods". However, in case of this type of assets "Comparative method isn‘t possible because there aren‘t analogous or similar assets to compare with; Income method isn‘t possible because PPP projects assets do not generate income; only the cost method can be used"… "The value of the asset is determined in two stages using the cost method:

a. the costs of creation (construction, etc.) of the assessed asset are determined.
b. the depreciation of the assessed asset is determined.

Thus, according to national law, for asset of this type, the market value of the asset would be equal to the book asset value".

Eurostat notes that the cap, based on the book value of the assets, does not foresee any deduction for the remediation costs (costs to complete/rectify the assets, additional operation, maintenance and financing costs) that will therefore fall on the Authority.

According to the PPP Guide, Theme 12, clause 12.1.4 Approach 4, page 107 *"Provisions that calculate the compensation payable on Partner default on the basis of the book value of the asset but do not take into account the Authority's remediation costs do influence the statistical treatment and automatically lead to the PPP being ON BALANCE SHEET for government.*"

However, Eurostat notes that the book value method will be applicable only if the alternative method, which would classify the contract as off-government balance sheet, leads to greater compensation for the private partner. When the cap is applicable, it indicates that the Authority assumes fewer risks. In this scenario, making a payment to the Partner that doesn't account for remediation costs, but is still lower than another payment that does, should not impact the statistical treatment of the contract.

In the Contract, Eurostat did not detect any of the "Compensation on early termination of the PPP contract" features relevant for the statistical treatment of the contract described in the PPP Guide, Theme 12, pages 103-107.

D.13 Expiry of the PPP contract

Art. 38 of the Contract deals with the return of the Lighting Infrastructure to the Authority at the end of the contract. At the time of return, the Lighting Infrastructure units shall be in working order, considering normal wear and tear (Art. 38.5).

In the Contract, Eurostat did not detect any of the "Expiry of the PPP contract" features relevant for the statistical treatment of the contract "on balance sheet" described in the PPP Guide, Theme 13, pages 115-116.

D.14 Financing arrangements

In the Contract, the PPP Partner is responsible for obtaining the totality of the financing required for the project. Financing is provided in the form of equity (20%) and a loan by a commercial bank (80%). Government does not participate in financing and does not provide guarantees.

The payment mechanism is not demand based and the contract does not include any clause relate to refinancing.

In the Contract, Eurostat did not detect any of the "Financing arrangements" features relevant for the statistical treatment of the contract described in the PPP Guide, Theme 14, pages 119-129.

D.15 Government influence

Under the terms of the Contract, the Authority does not hold any ownership stake in the Partner's business and has no right to claim any portion of the Partner's profits or revenue.

In the Contract, Eurostat did not detect any of the "Government influence" features relevant for the statistical treatment of the contract described in the PPP Guide, Theme 15, pages 130-134.

E. Conclusions and Eurostat's view

Eurostat supports the view of Statistics Lithuania that the Contract does not include combinations of provisions that would indicate the recording of the PPP assets on the balance sheet of government.

Notwithstanding the above, Eurostat has identified one issue of moderate importance (see section D.5) and one issue of high importance (see section D.7) that the Lithuanian Statistical Authorities should closely monitor.

F. Procedure

This view of Eurostat is based on the information provided by the Lithuanian statistical authorities. If this information turns out to be incomplete, or the implementation of the operation differs in some way from the information presented, Eurostat reserves the right to reconsider its view.

We would like to remind you that Eurostat is committed to adopt a fully transparent framework for its decisions on debt and deficit matters in line with Council Regulation 479/2009, as amended, and the note on ex-post advice, which has been presented to the CMFB and cleared by the Commission and the EFC. Eurostat is therefore publishing all official methodological advice (ex-ante and ex-post) given to Member States on its website.

Yours sincerely,

(e-signed)
Luca Ascoli
Director