



EUROPEAN COMMISSION  
EUROSTAT

Directorate D: Government Finance Statistics (GFS) and quality

Luxembourg  
ESTAT/D1/EBC/LA/MS/ltd(2014)

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**Subject: Ex-ante consultation on registration in GFS and in national accounts of the transactions connected with the pension reform (according to ESA95 and ESA2010 methodologies).**

**Ref.: Your letter RN-5-0713-01/56/2014**

Dear Ms Jeznach,

Following your letter of 28 April 2014, Eurostat is now in position to provide its preliminary opinion on the appropriate statistical recording in government finance statistics (GFS) and in national accounts of the transactions connected with the pension reform (according to ESA95 and ESA2010 methodologies).

### ***Accounting issue***

In December 2013, the Polish parliament adopted a law *on amendment of certain acts in relation to the definition of principles for pension payments from funds collected in open pension funds*. Due to the complexity and importance of the issue, the Polish authorities have decided to consult Eurostat on the appropriate statistical recording of the transactions involved.

The first ex-ante consultation took place in December 2013 and concerned the statistical recording of existing accounts in the Polish pension system on which information about contributions paid (to Social Insurance Institution - ZUS) and assets accumulated (in open pension funds - OFE ) are registered. In its letter of 10<sup>th</sup> of February 2014, Eurostat re-confirmed its view, already expressed in 2011<sup>1</sup>, that the sub-accounts should be treated as a

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<sup>1</sup> Eurostat ex-ante advice on the changes in the Polish pension system 2011: [http://epp.eurostat.ec.europa.eu/portal/page/portal/government\\_finance\\_statistics/documents/570653\\_Let\\_F\\_L\\_Ms%20Jeznach\\_%20Polish%20pension%20funds.pdf](http://epp.eurostat.ec.europa.eu/portal/page/portal/government_finance_statistics/documents/570653_Let_F_L_Ms%20Jeznach_%20Polish%20pension%20funds.pdf)

part of unfunded pension scheme. As a result, they should be classified in the general government sector with no associated liabilities recorded for the pension entitlements (no AF.63 liability in ESA2010).

This request for an ex-ante consultation seeks advice on other statistical aspects of the pension reform. It mainly concerns recording of transactions linked to the transfer of assets and redemption of the State Treasury bonds). In addition, the Polish authorities are asking Eurostat to confirm the eligibility of the Polish pension reform of 1999 for the treatment as a systemic pension reform under the Single Growth Pact provisions. They are also raising a question on ESA2010 methodology concerning the calculation of the output of open pension funds.

#### Documentation provided

With their letter, the Polish Central Statistical Office (CSO) provided Eurostat with a description of the transactions linked to the pension reform together with proposals for the recording in: (i) national accounts according to ESA95 and ESA2010 and in ii) ESA2010 EDP tables. The documents were prepared in co-operation with the Ministry of Finance and National Bank of Poland.

#### Description of the case

##### *Transfer of assets*

In result of the adopted reform, on the 3<sup>rd</sup> of February 2014, each open pension fund transferred to the ZUS 51.5% of its assets as of the 31<sup>st</sup> of January 2014 (the market value of PLN 153.2bn). At the same time, 51.5% of the units recorded in the individual accounts of each member in OFE were cancelled.

The following categories of assets were transferred to ZUS:

- bonds and bills issued by the State Treasury (face value of PLN 130.2bn, market value of PLN 134.1bn);
- bonds issued by Bank Gospodarstwa Krajowego (BGK) on behalf of National Road Fund, guaranteed by the State Treasury (face value of PLN 15.6bn, market value of PLN 16.9bn subject to redemption in October 2014);
- other securities guaranteed by the State Treasury (corporate bonds issued by Polish State Railways, face value and market value of PLN 0.3bn, subject to redemption in September 2014);
- cash (PLN 1.9bn).

### *Redemption of the State Treasury bonds*

ZUS immediately presented the Treasury securities for acquisition by the State Treasury. The remaining assets were transferred to the Demographic Reserve Fund (FRD).

- The State Treasury acquired assets from ZUS in return for a guarantee of future payments from the Social Insurance Fund (FUS) of pension benefits corresponding to the values recorded on sub-accounts kept by ZUS. Assets acquired from ZUS were immediately redeemed (cancelled).
- The Demographic Reserve Fund is obliged to transfer to FUS within 30 days the cash transferred by OFE and cash received from the redemption of assets (or interest due) mentioned above.

### *“Security slider”*

The reform foresees also a gradual transfer of members’ assets accumulated in OFE to FUS, starting 10 years of less before retirement (on monthly basis, in cash only) – the so called ‘security slider’. Transferred amounts are to be recorded on the sub-accounts in ZUS. The ‘security slider’ mechanism is to be launched at end October 2014.

### ***Methodological analysis by Eurostat***

#### *Applicable accounting rules*

The following accounting rules are relevant for the analysis.

- ESA 95, Annex III, social security schemes of government;
- The Eurostat Manual on government deficit and debt (MGDD) Part III General Government and public corporations

From September 2014:

- ESA 2010, Chapter 17: Social Insurance including pensions and Chapter 20: The government accounts
- The Eurostat Manual on government deficit and debt (MGDD), Implementation of ESA10, Part III General Government and corporations controlled by government.

#### *Availability of national accounting analysis*

In their letter, the Polish authorities presented two proposals for recording of transactions with regard to ESA95. The difference between two options concerns the presentation of redemption (cancellation) of the State Treasury bonds. It is proposed to be conducted either through a capital transfer D.9 in capital accounts or securities other than shares F.3 other changes in volume.

With regard to ESA2010, three recording proposals are presented. The first one assumes that as a result of the transfer of assets no general government (S.13) liabilities should be created, which results in the unbalanced accounts.

On the contrary, the second and third proposals both envisage recording of assets received from OFEs as the financial advance in S.13. They differ in the accounting approach

undertaken for recording of transactions in the accounts. The second option proposes to record the transactions in the financial accounts whereas the third option recommends recording of the entire reform in the other changes in volume account, so without impact on transactions.

### *Analysis*

Eurostat has carefully analysed the proposals for statistical recording of transactions linked to the pension reform. We have noted that all scenarios assume a balanced transfer of the assets from the open pension funds to the general government i.e. the ‘lump sum’ paid to the government matches or will match the pension obligations taken on by government (MGDD, III.6.2.12).

As this aspect of the Polish pension reform is not described in your request for an ex-ante consultation, we would like to ask you to re-confirm the correctness of this assumption and provide us with documentary evidence.

Assuming the transaction is balanced, we can provide a following advice on the statistical recording of the transactions linked to the Polish pension reform.

With regard to ESA95, Eurostat supports the general approach to record the transactions linked to the transfer of assets in the financial account. Concerning the issue of redemption of the State Treasury bonds, Eurostat regards it more as an S.13 internal movement of assets rather than a transaction of acquisition/disposal of assets. In this context, we support the recording of other changes in volume in securities other than shares (AF3) rather than capital transfers in capital accounts. This recommendation is valid for both ESA95 and ESA2010 methodologies.

With regard to ESA2010, the transfer of assets from open pension funds to the general government sector should follow the provisions of paragraph 20.275. The transfer of assets (in the form of a lump sum) should be viewed as a pre-payment of social contributions and recorded as a financial advance (AF8). In the future, a pre-payment of miscellaneous current transfers (D.75) should be recorded in proportion to the related payments of pensions. As a result, the lump sum payment will have no impact on the net lending/net borrowing of the general government in the year of transfer of obligations.

The same approach should be followed in case of the asset transfer (in cash) resulting from the ‘security-slider’ mechanism i.e. a gradual transfer of members’ assets accumulated in OFE to FUS.

It is worth emphasising that, as a result of the transfer of assets, no liabilities for pension entitlements (no AF63 liability in ESA10) should be recorded (as indicated in our letter of the 10<sup>th</sup> of February 2013).

Concerning the technical aspect of statistical recording in national accounts and EDP tables, we are strongly in favour of showing the transfer of assets to government through transactions in the financial account. In our view this is appropriate for transparency and accounting precision reasons. Nevertheless, as stated above, the redemption of bonds should be presented through the securities other than shares (F3) other changes in volume, for arguments already mentioned.

### *Other issues*

Regarding eligibility of the Polish pension reform of 1999 as amended for a treatment as a systemic pension reform, Eurostat has noted that the recent reform introduced a major change concerning participation in the second pillar. It was modified from a mandatory to a voluntary scheme. In order to express its view on the eligibility of the reform as amended, additional information on the post-reform population coverage (i.e. percentage) of the second-pillar is requested. Upon the receipt of the relevant information from the Polish authorities, Eurostat will revisit the issue and express its opinion.

Concerning the calculation of output of open pension funds, Eurostat notes that the applicable rules have not changed between ESA95 and ESA 2010. ESA 2010 does not explicitly mention the case of open pension funds; however Eurostat feels that a recording by analogy with multi-employer pension schemes could be made. In the case of such schemes, ESA 2010 paragraph 3.74 (d) (4) says that the value of output is measured as for life insurance policies, that is “investment income received by the schemes less the amount added to reserves”. ESA 2010 paragraph 3.74 (b) provides a more detailed specification of this calculation.

### *Conclusions*

On the basis of the above considerations and the provisions of ESA95 and ESA2010, Eurostat’s advice is as follows:

- with regard to ESA95, to record the redemption of the State Treasury bonds in securities other than shares (AF3) as other changes in volume.
- with regard to ESA2010, to register the transfer of assets through transactions in the financial account and the redemption of the State Treasury bonds in securities other than shares (AF3) as other changes in volume.

Furthermore, Eurostat would like to ask the Polish authorities to provide information about the mechanism to be used for revenue imputation (D.75) in proportion to the expenditure, alongside with a reduction in AF8. This could potentially be conducted either through the monitoring of accounts for actual payments of pensions or (in the absence of actual payment information) the expected cash flows resulting from the actuarial calculations.

### *Procedure*

This preliminary view of Eurostat is based on the information provided by the country 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. To this end Eurostat would request to be informed of the final details of the operation (contract and accompanying papers where relevant) when they are available, or (should this be the case) information that the planned operation has been abandoned.

In this context, we would like to remind you that Eurostat is committed to adopting 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-ante advice, which has been presented to the CMFB and cleared by the Commission and the EFC. Eurostat intends, therefore, to

publish all future official methodological advice (ex-ante and ex-post) given to Member States, on the Eurostat web site. In case you have objections concerning this specific case, we would appreciate if you let us know. In any case (regardless of whether you have objections or not) we would like to receive an answer from you on the issue no later than **4 July 2014**.

Yours sincerely,

Eduardo Barredo Capelot

*(e-Signed)*  
Acting Director