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Subject: Ex-post advice
Accounting treatment of the sale of emergency oil stock reserves from the State Material Reserves of the Slovak Republic to EOSA (Emergency Oil Stock Agency)

Your ref.: Your letter 700-0023/2014 of 07/03/2014

Dear Mr Bernadič,

Thanks for your letter dated 7 March 2014 where you request some clarifications on the proposed accounting treatment of the sale of emergency oil¹ stock reserves between the State Material Reserves of the Slovak Republic (SMR) and Emergency Oil Stocks Agency (EOSA) that took place in December 2013. Eurostat has recommended, as part of the conclusions and action points of the standard dialogue visit that took place on 28-29 November 2013, not to record the sale as government revenue in national accounts.

1. The accounting issue for which a clarification is requested

In 2013, the Slovak government decided to change the system in place to comply with the international requirements of emergency oil stocks. EOSA was established by the legal Act 218/2013 Coll. and became responsible for the storage of oil stocks in Slovakia, an obligation that was previously the responsibility of SMR. EOSA has the legal form of an association of legal persons and it is controlled by government, which has a fixed 70% of the voting rights. Every oil operator in Slovakia can be a member of EOSA. The 30% voting rights reserved for private oil operators is distributed based on the volume of their

¹ For the purposes of this note oil includes also gasoline, diesel and kerosene products.

sales. Private operators participate to some extent in the management process but government effectively controls EOSA. Therefore EOSA is considered a public unit.

According to Act 218/2013 Coll., all oil operators in Slovakia should comply with the requirement of holding some oil reserves by paying a fee to EOSA. The amount of the fee is based on the volume of the sales of the operator. The fees paid are calculated using a formula that ensures that the total costs of EOSA are covered.

In December 2013, SMR sold to EOSA its stocks of oil reserves. EOSA paid EUR 465.207.738,19² to SMR. The valuation of the oil stocks was done by an independent expert. EOSA bought the stocks in order to be prepared to fulfil its duties as the Slovak Central Stockholding Entity, as defined by Council Directive 2009/119/EC. The sale and its conditions were decided by government in the same legal act as the one that created EOSA (Act 218/2013 Coll.). The sale was financed by a commercial loan of EUR 520 million granted by a consortium of private banks.

2. Methodological analysis and clarification by Eurostat

The Slovak statistical office has classified EOSA as a non-financial corporation, following ESA 95 2.23 d)

“Non-profit institutions or associations serving non-financial corporations, which are recognised as independent legal entities and which are market producers principally engaged in the production of goods and non-financial services”⁷ “

⁷ *Including institutions financed by voluntary contributions of a quasi-fiscal nature, levied on producers by units whose principal activity is to provide services in exchange. These contributions are considered as purchases of market services.*

Eurostat has some doubts on the applicability of this ESA 95 paragraph to EOSA. It would seem that EOSA is not serving non-financial corporations (oil operators) but government, which has to comply with the requirements of the European Union and the International Energy Agency of keeping a specified level of emergency oil reserves. Additionally, the contributions paid to EOSA are not voluntary. Every oil operator is obliged by law to comply with its obligation by paying a fee to EOSA. The fee is set by government. Oil operators do not have the possibility to comply with the obligation using its own oil stocks and storage facilities.

However, in order to ensure homogeneity of treatment between countries³ and awaiting explicit guidance on this issue, Eurostat can agree that, under ESA 95, the Slovak Statistical Office provisionally classifies EOSA outside the government sector.

Eurostat considers that the sale of oil from SMR to EOSA cannot be recorded as a sale in national accounts, even if EOSA is classified in the sector non-financial corporations.

² <http://crz.gov.sk/index.php?ID=1156965&l=sk>

³ Eurostat has investigated the sector classification of similar units in other Member States and found out that, in some cases, they are classified outside government. In a specific case, the agency was directly financed by taxes and it has been agreed to reclassify it to the government sector already in the April 2014 notification. Based on the survey carried out by Eurostat in recent months, Eurostat is planning to discuss the issue at the next Financial Accounts Working Group in June 2014 for taking a final decision in the context of ESA 2010. Eurostat will review with countries in the coming months the sector classification of such units.

Eurostat has investigated if the same transaction, sale of emergency oil stocks from a government unit to a newly created unit classified outside government, has taken place in some other Member State. The result of the investigation was that no such transaction has taken place in any other Member State. Therefore, Eurostat can only make reference to similar cases involving the sale of assets from government to publicly controlled corporations where government, through specific legislation, kept some rights on the assets. In all these cases, Eurostat did not allow to record as government revenue the proceeds of the sale and considered them as financial transactions, not affecting government net lending/net borrowing. EOSA is obliged by law to keep the emergency oil reserves at the disposal of government. The emergency oil stocks cannot be sold or subject to bankruptcy procedures. The members of EOSA do not hold any ownership rights on the emergency oil stocks. All these facts are a clear indication that government still holds an indirect control of the emergency oil stocks.

Eurostat therefore considers that the sale of the emergency oil stocks did not involve a disposal of non-financial assets from government and that only a financial transaction should be recorded with no impact on government revenue. A future sale back from EOSA to government of the emergency oil stocks should also have no impact on government expenditure. In the Slovak national accounts, a loan, equal to the payment in cash received by government, should be re-routed from EOSA to government accounts and treated as government debt. Moreover, an appropriate rate of interest will have to be imputed on the loan and be treated as government expenditure until the loan will be repaid. Future sales of the oil stocks by EOSA to private companies will be considered as disposal of non-financial assets and will decrease the amount of the government loan.

3. Conclusion

Eurostat agrees with the Slovak Statistical Office that, awaiting further clarifications, EOSA is classified under ESA 95 in the sector public non-financial corporations to ensure a comparable treatment with other countries. Nevertheless, Eurostat will discuss the sector classification of such units with Member States in the new FAWG and provide more explicit guidance.

Eurostat confirms its view that the sale of emergency oil stocks must not be recorded as government revenue. This view is consistent with past Eurostat's opinions for similar transactions. The sale should be recorded as a financial transaction, a loan increasing government debt.

4. Procedure

This preliminary view of Eurostat is based on the information provided by the Slovak 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.

In this context, 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-ante advice, which has been presented to the CMFB and cleared by the Commission and the EFC. Eurostat therefore publishes all official methodological advice (ex-ante and ex-post) given to Member States on the Eurostat website. In case you have objections concerning the publication of this specific case, we would appreciate if you would let us know *before 14 April 2014*.

Yours sincerely,

(e-Signed)

Laurs Nørlund
Director