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EUROSTAT

Directorate D: Government Finance Statistics (GFS)

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Subject: Statistical classification of MyCSP Ltd

Dear Mr Stokoe,

Thank you for your letter dated 13th August 2013 and the following accompanying documents:

- The classification paper by the UK Office for National Statistics (ONS), setting out the statistical classification issues,
- The submission document by the UK Cabinet Office, outlining the background of setting up MyCSP Ltd,
- The contract notice for the participation in the MyCSP mutual joint venture, published in the Official Journal of the European Union, and
- The constitutional documents of MyCSP Ltd (the articles of association and the shareholders' agreement).

I would like to inform you of Eurostat's preliminary view on this case.

Accounting issue

In July 2011 the UK government established a private limited company, MyCSP Ltd, to administer the UK Civil Service Pension scheme. In this task, MyCSP Ltd succeeded My Civil Service Pension, a UK government unit that was an in-house administrator of the Civil Service Pension scheme.

MyCSP Ltd was established as a mutual joint venture, a type of a UK company limited by shares, with the ownership split between government, a private sector partner and the employees of the company. In the case of MyCSP Ltd, 35% of shares are owned by government, 40% by a private partner (Equiniti Group) and 25% by employees (through the Employee Benefit Trust, EBT).

Both the selection of the joint venture partner and the award of the outsourcing contract for the administration of the Civil Service Pension Scheme were subject to a competitive tendering process.

The ONS is satisfied that the general corporate policy of MyCSP Ltd is controlled by the private sector and the employees, but has concerns regarding the restrictions on the sale of shares (in particular, the restrictions applicable to EBT) which might mean that the economic ownership remains with government. The ONS is therefore requesting Eurostat's advice on the statistical classification of MyCSP Ltd.

The ONS has confirmed that the statistical classification of MyCSP Ltd would have no implications for the treatment of the UK Civil Service Pension scheme which would remain classified as an unfunded, general government scheme.

Methodological analysis

Control of MyCSP Ltd

Control is the key concept to distinguish between public sector and private sector bodies. This concept is defined in the European System of Accounts (ESA95)¹ and further explained in the context of general government in the ESA95 Manual on Government Deficit and Debt (MGDD).² It should be noted that the concept of control is substantially extended and elaborated in ESA 2010, but this issue is currently analysed under ESA95.

¹ ESA95, paragraph 2.26:

Control over a corporation is defined as the ability to determine general corporate policy by choosing appropriate directors, if necessary.

A single institutional unit (another corporation, a household or a government unit) secures control over a corporation by owning more than half the voting shares or otherwise controlling more than half the shareholders' voting power. In addition, government secures control over a corporation as a result of special legislation decree or regulation which empowers the government to determine corporate policy or to appoint the directors.

In order to control more than half the shareholders' voting power, an institutional unit needs not own any of the voting shares itself. A corporation C could be a subsidiary of another corporation B in which a third corporation A owns a majority of the voting shares.

Corporation C is said to be subsidiary of corporation B when: either corporation B controls more than half of the shareholders' voting power in corporation C or corporation B is a shareholder in C with the right to appoint or remove a majority of the directors of C.

² MGDD chapter 1.2 (Criteria for classifying units to the general government sector), section 3:

A public producer is a producer that is controlled by general government. All other producers are private producers.

Public producers are found either in the corporations' sectors (if they are market) or in the general government sector (if they are non-market or if they are not institutional units).

Control is defined as the ability to determine the general (corporate) policy or programme of an institutional unit by appointing appropriate directors or managers, if necessary. Control may be exercised by government directly or indirectly (through a public holding corporation for example).

Owning more than half the shares of a corporation is a sufficient, but not a necessary, condition for control. Government can also exercise control over a corporation through special legislation, decree or regulation that empowers the government to determine corporate policy or to appoint the directors.

This definition of control is also applicable to NPIs. But in cases where the criteria set out above are not formally satisfied, or where special legislation is lacking, a more operational definition of control is necessary. The government secures the control of a unit when it influences the management of this specific unit, independently of general supervision exercised on all similar units. Public intervention in the form of general regulations applicable to all units working in the same activity should not be considered as relevant when deciding whether the government holds control over an individual unit.

MyCSP Ltd is majority privately-owned. 40% of its shares are owned by Equiniti Group, a private sector body. 25% of the shares are owned by MyCSP Ltd employees, through the Employee Benefit Trust (EBT). Based on the information provided by the UK authorities, EBT also qualifies as a private sector body: it is run for the benefit of employees by three directors, none of whom have connections with the government and two of whom were appointed directly by employees.

With regard to the appointment of directors of MyCSP Ltd itself, the UK authorities confirmed that, while the current shareholding remains in place, government, the Equiniti Group and EBT each appoint one director, in addition to the senior employees who also act as directors.

Based on the information provided by the UK authorities, government does not exercise control over MyCSP Ltd through special regulation. In addition, the constitutional documents do not give government, through one director out of a maximum of 6, any greater powers in the running of MyCSP Ltd. In particular, government does not have the overriding ability to:

- determine aspects of how the body delivers its outputs;
- have a final say in sale/acquisition of fixed assets;
- be entitled to a share of proceeds of asset disposals that goes beyond the repayment of previous government support for capital formation;
- liquidate the body;
- prevent the body from ending its relationship with the public sector;
- change the constitution of the body;
- decide what sort of financial transactions the body can undertake, or limit them;
- prevent the body from receiving certain types of income from other sources;
- exert numerous minor controls over how the body is run;
- exert financial control as part of a general system of controlling public expenditure;
- control dividend policy;
- set pay rates;
- (for non-regulatory reasons) approve acquisitions.

Therefore Eurostat concurs with the ONS' conclusion that MyCSP Ltd is not controlled by government either by a majority shareholding, through the appointment of directors or through special regulation.

Transfer of ownership in MyCSP Ltd

Initially, when MyCSP Ltd succeeded My Civil Service Pension (a UK government unit), shares were split between government and employees (EBT). In April 2012, government sold a part of its shares to Equiniti Group.

The shareholders' agreement stipulates that none of the shareholders can dispose of their shares within 5 years "*of the vesting of the business in MyCSP Ltd*" (May 2012). In addition, EBT can only dispose of its shares when government ceases to hold any shares.

The ONS concern is that strict application of principles³ set out in the securitisation chapter of the MGDD could lead to a conclusion that government retained economic ownership, and therefore control, of MyCSP Ltd.

From the information provided by the UK authorities, it appears that risks have been transferred, but some benefits (such as a right to capital gains) have not. Other benefits, notably a right to dividends, have been transferred. The UK authorities confirmed that MyCSP Ltd can and intends to pay dividends to shareholders in the first 5 years. According to the shareholders' agreement, if the board cannot agree on the amount of dividends to pay shareholders, the default position is that 50% of distributable profits are paid out. MyCSP Ltd has already paid a dividend to all shareholders following its first full year of trading.

Eurostat is of the opinion that the temporary restrictions stipulated in the shareholders' agreement are in line with the common business practice. It is worth noting that the restriction to dispose of shares within 5 years applies to all shareholders, including government. Therefore the principles set out in the securitisation chapter of the MGDD should not be interpreted to mean that government retains economic ownership of MyCSP Ltd solely by virtue of the temporary restrictions on the disposal of shares.

Statistical classification of MyCSP Ltd

As discussed in the section above, MyCSP Ltd is not controlled by government either by a majority shareholding, through the appointment of directors or through special regulation. In addition, MyCSP Ltd is not subject to various forms of secondary control, such as the overriding ability to liquidate the body or to set pay rates.

Both the selection of the joint venture partner and the award of the outsourcing contract for the administration of the Civil Service Pension Scheme were subject to a competitive tendering process. The UK authorities have also confirmed that MyCSP Ltd can and has already engaged in other activities than the administration of the Civil Service Pension scheme, whilst the fees for the administration of the scheme were negotiated between MyCSP Ltd and government in the framework of a standard outsourcing contract.

Therefore Eurostat believes that MyCSP Ltd, as a profit-seeking institutional unit that is not controlled by government, should be statistically classified in the Non-financial Corporations sector (S.11) under ESA 1995.

³ MGDD chapter V.5 (Securitisation operations undertaken by general government), paragraphs 24, 31 and 45:

24. Assuming that the securitised items are recognised as transferable assets in national accounts, a sale of these can only be recorded in national accounts if there is transfer of economic ownership from government to the securitisation entity. There is transfer of economic ownership of assets when the risks and rewards that are attached to these are completely transferred. If the risks and rewards are not completely transferred from government to the securitisation entity, the securitisation is recorded as government borrowing. [...]

31. The risks and rewards associated with the asset are judged as not fully transferred, leading to a recording as government borrowing, if any of the following applies:

- Restrictions are imposed by government on the securitisation entity's right to subsequently sell the assets. [...]

45. Any restriction to on-selling the acquired assets, or other rights to future cash flows, would provide evidence that economic ownership has not been transferred.

However, a number of features discussed above make MyCSP Ltd a specific case. As a result, Eurostat reserves the right to separately examine the statistical classification of any future mutual joint venture.

Conclusion

Eurostat's preliminary view is that:


- (1) MyCSP Ltd is not controlled by government either by a majority shareholding, through the appointment of directors or through special regulation. Neither is MyCSP Ltd subject to various forms of secondary control.
- (2) The temporary restrictions stipulated in the shareholders' agreement are in line with the common business practice. Therefore principles set out in the securitisation chapter of the MGDD should not be interpreted to mean that government retains economic ownership of MyCSP Ltd solely by virtue of the temporary restrictions on the disposal of shares.
- (3) In consequence, Eurostat believes that MyCSP Ltd, as a profit-seeking institutional unit that is not controlled by government, should be statistically classified in the Non-financial Corporations sector (S.11) under ESA 1995.

Procedure

This preliminary view of Eurostat is based on the information provided by the UK 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 and the note on ex-ante advice.⁴ Eurostat therefore publishes all official methodological advice (ex-ante and ex-post) given to Member States on its website. Eurostat intends to publish this letter, unless you raise any objections by 17.00 CET on 27 September 2013.

Yours sincerely,



François Lequiller
Director

Copy: Iain Bell

⁴ Available on the Eurostat website:
http://epp.eurostat.ec.europa.eu/portal/page/portal/government_finance_statistics/documents/Ex-ante_advice_final_2013-01-18.pdf.