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Directorate C: National and European Accounts

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Istituto Nazionale di Statistica
Ms. Alfonsina Caricchia
Head of Nacional Accounts
Via Cesare Balbo 16
IT - 00184 Roma

<u>Subject</u>: Operations concerning the trade debts of the Local Health Units
Your letter dated 13 July 2006

Dear Ms. Caricchia,

Eurostat acknowledges the receipt of your request for opinion concerning the recording of restructuring operations related to trade credits of the Local Health Units (ASL) of the Lazio Region in national accounts

The issue

According to the explanations provided and in the context of debt restructuring for the health sector, the *Region (Lazio)* authorized the ASL to negotiate bilaterally with health suppliers the repayment of their debts. This event occurs due to the fact that payments are being significantly delayed from ASL to suppliers. It should also be noted that ASL are reimbursed by the *Region* for the acquisition of this health services. Both the ASL and the *Region* are classified inside general government.

This debt restructuring might be broken down into two steps. The first step involves an actual renegotiation of the debt between ASL and suppliers aiming among other issues to certify the amount of the nominal debt to suppliers and to agree for the reimbursement of the debt to be spread for a longer period than the original maturity (up to three to five years and in some cases up to ten years). The second step provides an option to suppliers to securitize their credits transferring them to a Special Purpose Vehicle or to a factoring corporation. Although no guarantee is given by the *Region* itself in this process, the *Region* accepts to pay directly to health suppliers the instalments that were due to be paid to ASL.

Your note raises the question of whether such events should lead to a re-qualification of government payable into government debt, and lists pros and cons to this effect.

The analysis

Eurostat recalls that SNA 11.23 indicates that the changing of the terms of the loan contract enters the financial accounts, reflecting the fact that an interaction by mutual agreement takes place between two institutional units. This indicates that the original contract is assumed to be redeemed and a new contract is issued. Thus, to the extent that the first step of the debt restructuring in question changes the underlying financial instrument, it must be seen as a redemption in the original payable against an incurrence of a new liability.

The original liability of ASL towards health suppliers is a trade credit (financial instrument AF.7) because this financial claim related to the time lag between cash payments and the delivery of goods and services. Such claims are understood to be usually of a short-term nature, which was the direct reason why there was no opposition for excluding this category of liabilities from the definition of the government debt (Maastricht debt): even though the SNA seems to explicitly envisage the possibility of long-term payables, this would not seem the interpretation of the ESA1995.

Moreover, the renegotiation means a redemption of the initial financial instrument and a creation of a new one that arguably is no longer related with the goods and services themselves. In that later case, the suppliers enter into a financing arrangement that intends to provide long-term finance to another unit. Such long-term financing facility to refinance is to be classified as a loan (ESA95, par. 5.81-h)).

The criteria of ESA 5.74 to which your note refers to, related on who is the party that initiates the borrowing, generally seems not to contradict this recording, to the extent that the ASL might be considered as willing to engage in debt restructuring, and in any case is mostly relevant in the deposit/loan delineation.

In addition, the possible securitisation of the trade credits through a SPV or a factoring corporation offered by the second step in the context of this debt restructuring process would seem to reinforce this reading. It would seem anomalous that the mere direct lending by a banker to the Region for repaying the suppliers would be included in the government debt, while a combination of two separate events to the same effect would leave the government liability as a payable.

Eurostat notes that the *Region* seems to be accepting by a formal act a liability towards suppliers when accepting to pay them directly, and it is unclear whether in this case the ASL have redeemed completely their liability. Finally, one issue might be the appropriate sectorization of the SPV.

Conclusion

Eurostat considers at this stage that the debt restructuring involving payables leads to creation of a new instrument, most likely to be a loan (AF4). The securization arrangements foreseen reinforce the loan recording.

Yours Sincerely,

On behalf of
the Director

Laurs Nørlund
Director