



MARIANO GÓMEZ DEL MORAL
Director General of Statistical Products

Mr. Laurs Norlund
Director
Direction C
EUROSTAT

Subject: Methodological treatment of the capital injections into ADIF

Madrid, 13 August 2007

Dear Mr. Norlund,

In reference to the above mentioned subject and in reply to your letter of 26-07-2007 last, in which EUROSTAT considers that the capital injections into ADIF should be classified as non-financial transactions, as *capital transfers (D.9)* in the form of *investment grants (D.92)*, with the subsequent impact on government deficit, I would like to make the following comments:

The new treatment proposed by EUROSTAT amends what the Spanish statistical authorities have considered appropriate until now: to record these capital injections into ADIF as financial transactions, under the heading of *shares and other equity (F.5)*, without any impact on government deficit. This treatment is the one that has been applied since 1997, has been approved by EUROSTAT in its News Release no. 24, of 26 March 1997, and has been discussed at different EDP Missions in Spain (in particular in 2004 and 2007).

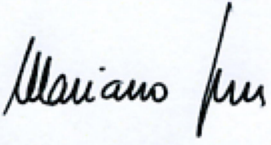
The Spanish statistical authorities appreciate the EUROSTAT position in relation to this case, although, as it is explained in the adjoining Note, they do not share the criteria which are set out in that document and serve as a justification for the EUROSTAT decision. They also consider that Spanish opinion would be reinforced if consideration had been given to the efforts made by the Spanish government in the financial re-organization of the railway companies (infrastructure manager and operator), which had the corresponding impact on the deficit and debt of the General government sector and which have enabled ADIF to achieve the excellent asset situation it now holds. However, this situation, which strengthens this company's ability to generate future profits, has not been the subject of comparative analysis with similar cases examined by EUROSTAT in other Member States.

Even though the Spanish statistical authorities do not share the arguments set forth by EUROSTAT in its methodological analysis of the subject, they **accept** the

treatment proposed by this body and inform that in the next EDP notification to be submitted at the end of September 2007, the capital injections made into ADIF will be included as State government expenditure, in the form of *investment grants (D.92)*.

Lastly and regarding the procedure that EUROSTAT is obliged to follow in relation to the publication of methodological advices given to Member States, I would like to inform you that Spain has no objection whatsoever to the treatment proposed being publicized on the EUROSTAT website. In this respect, I would tell you that, alongside the EUROSTAT position, the Spanish statistical authorities wish that the Spanish opinion on the matter should also be stated, as explained in the Note adjoining this letter.

Yours sincerely,



e



Comments on the methodological analysis by EUROSTAT about the ESA95 accounting treatment of the capital injections into ADIF

1. Insofar as the sources of financing foreseen for ADIF are concerned, we have to specify a point. Page 2, paragraph four, of the EUROSTAT document refers to the sales of lands as one of the sources of ADIF financing, for an amount of four million euros. However, according to ADIF Business Plan, this amount is obtained from the following items: self-financing generated by ADIF through its profits and amortizations, and financing through other accounts receivable.

2. EUROSTAT has added new requirements with regard to the conclusions reached in the 2004 EDP mission in Spain, where it was concluded that the nature of the capital injections would be classified as capital transfers if, after future analysis, ADIF (at that time GIF) turned out not to be profitable.

EUROSTAT now states, furthermore, that it is not enough to be profitable but that profitability should be similar to what would be required of a private investor, a condition that is apparently not met by ADIF, whose projected long-term rate of profitability in the Business Plan until 2025 will still be very low, between 1 and 2%.

It should be pointed out, however, that the required profitability depends on the features of each specific project and that in the case of investments with long-term maturity periods (as may be the case of toll highways undertaken by the private sector or even built-to-let properties), profitability is only achieved after a good many years and their intended rate of return is not usually very high.

In this respect, we should indicate that the ADIF forecasts in its Business Plan for the years 2006-2025 have been calculated on the principle of accounting caution, so that their treatment cannot be prejudged on the basis of the concept of low profitability, let alone when the EUROSTAT ESA-95 Manual on government deficit and debt (MGDD), for treating capital injections made by the government in a public corporation as financial transaction, only requires that there should be expected profitability and an increase of the government equity, either through a higher value of its property rights in the company or also through a potential distribution of profits (dividends).

The foregoing comments show that the treatment of these transactions is not clear enough. For this reason and since the MGDD is to be reviewed in the near future, the Spanish statistical authorities propose that the matter should be examined both in the *financial accounts* and in the *national accounts working groups*, and the specific conditions laid down in which general government acts as private investor. In this way, the criteria to be applied by Member States in the handling of these operations will be finally clarified.

3. EUROSTAT says that ADIF investments are co-funded by the European Union (EU) and that it does not seem justified to give a different treatment to the EU financing (expenditure) from that of the Spanish State (shares and other equity). We should not overlook, however, the fact that capital injections of both agents are made in quite different conditions: the Community contribution is non-returnable, while the contribution of the Spanish State is in its status as owner of ADIF, so that it may expect a return on its contribution.

4. EUROSTAT argues that capital injections into ADIF are linked to investment in high-speed rail infrastructure and that, in accordance with the MGDD, injections made into public companies linked to the acquisition of fixed assets should be recorded as an investment grants.

The opinion of Spanish experts in this respect is that EUROSTAT is applying this section of the MGDD having previously decided that capital injection should be treated as a capital transfer (D.9) due to the expected lack of profitability. In other words, this argument only makes reference to the precise consideration of the type of capital transfer in question, namely either an investment grant (D.92), or else other capital transfers (D.99)

If capital injection is made to finance a profitable investment and the Public Administration wishes to obtain an increase of its equity in the future, the MGDD also expressly states that capital injection should be treated as a financial transaction, without entering into considerations regarding the end use of the funds in the receiving unit.

Madrid, 13 August 2007

e