



EUROPEAN COMMISSION



EUROSTAT

Directorate C: National and European Accounts

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Ms Irena TvariJonavičiūtė
Head of National Accounts Division
Department of Statistics to the
Government of the Republic of Lithuania
Gedimino ave. 29,
LT- 01500 Vilnius

Subject: Recording of transactions related to repayments of unpaid employees compensations and pensions

Dear Ms TvariJonavičiūtė,

Following up on your document submitted to us on 30 January 2007, and discussions during the informal meeting of 17 January 2007 at Eurostat and other previous correspondence, on the cases of uncompensated earning and unpaid pensions, I am in a position to reply to the questions you asked on the appropriate statistical classification for the two cases you have presented.

The issues for which an opinion is being sought are a determination of the correct ESA95 accounting treatment of the reimbursement of some unpaid compensation of employees following a Constitutional Court ruling (*uncompensated earnings case*) as well as the reimbursement of some unpaid pensions following another Constitutional Court ruling (*unpaid pensions case*).

1. Uncompensated earnings case

Description of the case

In 2002, a law amending the Public service law provided for a lower indexation to be applied to the wages of some public and municipality officers. In December 2004, the Constitutional Court ruled that this provision of the Public service law was against the constitution. Following this ruling, the Public service law was immediately adjusted with application from 2005 onwards. A question remained regarding the potential compensation for the lower salary paid during the 2002-2004 period.

In 2006, government decided to repay the salary due for 2002-2004. A Law established an obligation for government to conduct repayments by 1 March 2007. A government decree (*government resolution*) approved the rules for repayment, for an amount of 168 million LTL (0.2 percent of GDP) that was paid in full in 2006. According to these rules, the payments were made by each institution concerned to all the civil servants in question, without exception.

You have asked for our view on the recording in national accounts of transactions related to the repayments described, with regards the classification of the transaction as well as the time of recording.

Methodological analysis

The ESA95 *Manual on Government Deficit and Debt* (section III.4 pages 154-155) indicates that the time of recording, in national accounts, of claims/liabilities in case of Court ruling is at time the decision is taken (assumed to be the time when the obligation is established).

Taking into account the role of the Constitutional Court, which is to ensure that laws and other legal acts are in conformity with the Constitution and not to eliminate these contradictions, we could agree with your line of argumentation that the government had no established obligation to pay arrears at time of Court ruling in 2004, either explicitly as per the Court ruling, or implicitly as per common legal or administrative practices. In particular, we understand that there could have been a genuine uncertainty as to whether government was obliged, based on the Court ruling, to compensations with retroactive effect. Accordingly, Eurostat believes and agrees that a government liability exists only since the recognition of those obligations by the Law of 2006, and not since 2004.

We agree with your proposal to classify this amount as compensation of employees, in view of the nature of these payments, and to avoid underestimating GDP. Although compensation of employees should generally be recorded at time of work in the system, these salary arrears could be considered within the "exceptional payments" foreseen by ESA95 para. 4.15 (a) as well as by the ESA95 *Manual on Government Deficit and Debt* (chapter III.2.2.b).

Conclusion

According to the present understanding of this case by Eurostat, your recommendation of treatment of repayments for uncompensated earnings in national accounts is appropriate, i.e. to treat these repayments as compensation of employees (item D.11 Wages and salaries) in 2006.

2. Unpaid pensions case

Description of the case

Following a former provision of the Law on state social insurance pensions, only a part of mandatory pension was paid to the working pensioners in 1995–2002, for those with earnings above an identified limit. In 2002, the Constitutional Court ruled that this provision was against the Constitution. Following the ruling of the Court, the Law on state social insurance pensions was immediately adjusted with application from 2003 onwards. A question remained regarding the potential compensation for past periods. Government had an intention to carry out some compensatory amounts, although no commitment to do so was formally established and only indicative amounts were known.

A draft Law establishing an obligation for government to repay was under preparation in 2006, and it is likely that the operation would be formalised during the course of 2007.

You have asked for our view on the recording in national accounts of transactions related to the repayments described, with regards the classification of the transaction as well as the time of recording.

Methodological analysis

Under the assumption that the developments in this case will be similar to the previous one, that is, that the obligation for government to pay will be established by law, that the amounts will be estimated with reasonable accuracy, and that payments will be done automatically by government

without prior assessment for specific criteria and with no obligation for the applicant to submit a formal demand foreseen, your suggestion to record a capital transfer payable by government to households in the year when the liability for government is established by the law (assumed to be 2007) could be agreeable.

The classification would plausibly be a capital transfer, the payment resulting from the consequence of a court decision relating to distributive transactions, in application to the ESA95 *Manual on Government Deficit and Debt* (section III.4 page 155).

Conclusion

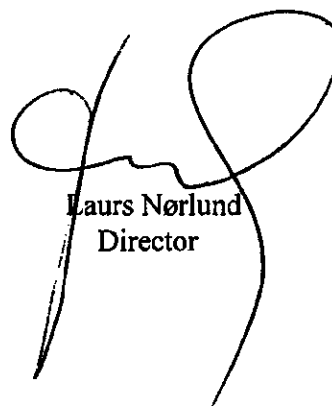
The analysis leads Eurostat to the tentative conclusion, based on available information and actual understanding of the case, that the treatment in national accounts proposed by you is appropriate: to classify the repayments for the unpaid pensions as a capital transfer payable by government (item D.9), in the year when the commitment to pay is established by Law (assumed to be 2007) and not at the time the Constitutional Court found the law unconstitutional (2002).

Procedure

This view of Eurostat is based on the information provided by the Lithuanian 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 addition, 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 the amended Council Regulation 3605/93 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 12 March 2007.

Yours sincerely,



Laurs Nørlund
Director