



EUROPEAN COMMISSION



EUROSTAT

Directorate C: National and European Accounts

Luxembourg, 14 MARS 2008
ESTAT/C-3/LN/MW/mg D(2008) 30044

Mr Lambert Verjus
President
Institut des Comptes Nationaux
City Atrium C, Rue du Progrès, 50
B-1210 Bruxelles

Subject: Methodological treatment of the renovation of the Residence Palace

Ref.: Your letter: T/III/2005/013451 of 14 June 2005
Our letter: ESTAT/C-3/GH/LA/fk D(2005) 30202 of 18 July 2006
Your letter: T/C2/2006/DC8781 of 18 April 2006
Our letter: ESTAT/C0/LN/EBC/lc D(2006) 50027 of 23 May 2006
Your letter: ST/2006/05/081/ra of 24 May 2006
Our letter: ESTAT/C-3/LN/MW/mg D(2006) 30222 of 4 September 2006
Your letter: T/C2/2007/012401 of 24 July 2007
Our letter: ESTAT/C-3/LN/LA/MW/ji/ D(2007) 30371 of 15 November 2007
Your letter: T/C2/2007/018502 of 28 November 2007
Letter of the Belgian Treasury of 21 December 2007 (no reference)

Dear Mr Verjus,

Following your letter of 24 July 2007 and letter of the Belgian Treasury of 21 December 2007, I am in a position to reply to the question you asked on the appropriate statistical treatment for the case you have presented on the renovation by the Belgian State of a building in Brussels (Résidence Palace) and a possible subsequent long-term renting contract with a buy option with the European Community (the Council of the European Union).

The accounting issue for which a clarification is requested

Documentation provided

Eurostat notes that the same question was a subject of three rounds of ex-ante methodological consultations by the Belgian statistical authorities in 2005, 2006 and 2007. The issue was also discussed during the EDP dialogue visit to Belgium in April 2006 and in the meeting with the representatives of the Belgian government and the Council in January 2008.

During that consultation process, a preliminary agreement (memorandum of understanding) between the Belgian State and the Council was received on 24 May 2006.

Subsequently, a project of the final agreement between the Belgian government and the Council dated 20 December 2007 was received in January 2008.

Description of the case

The question for which a reply is being sought is a determination of the correct ESA95 accounting treatment of the expenses for the renovation by the Belgian State of Résidence Palace and a subsequent sale of the building to the Council, with the price paid in deferred payments.

The Belgian government is currently the sole legal owner of Résidence Palace and will bear the costs for the renovation of this building, currently estimated at approx. 240 million euro (constant prices). On 25 November 2005 the parties signed a memorandum of understanding outlining the main features of the project. A further agreement, the final convention, will be signed in order to define rights and obligations of both parties, as well as to specify the financial matters.

To recall from the previous correspondence, the initial contract's main features were as follows:

- After the renovation works conducted by the Belgian authorities, the Belgian government and the Council will conclude a 27-year rental contract. Under this contract, the total amount of monthly rents paid during the contract by the Council will be equivalent to the total expenditures incurred by the Belgian government for the renovation of the building.
- At any time during the rental (except for the last six months) the Council was entitled to exercise the call option concerning the acquisition of the building. The price was calculated as the remainder of the total monthly rents to be paid until the end of the rental contract plus 1 euro (price of the buy option).
- There was no obligation for the Council, either at present, or in the future, to purchase the renovated Résidence Palace.
- The Belgian government was supposed to be the sole legal owner of Résidence Palace until the moment in which the Council might decide to purchase the renovated building.

The project of the final convention of 20 December 2007 includes the following amendments:

- After the completion of the renovation works, the Belgian authorities and the Council will proceed to the signing of the sale agreement; the payments of the purchase price, that will be equal to the renovation costs but not higher than 240 million, will be spread over maximum 27 years.
- The Council made available in 2007 an amount of 72 million € for the reconstruction of the building, and the amount of 15 million € is foreseen for this purpose in the 2008 budget.

Methodological analysis by Eurostat

After an examination of the provided project of the final convention, Eurostat has reached the following provisional views.

Applicable accounting rules

Council Regulation (EC) No 2223/96, as amended, incorporates the national accounts concepts and definitions of the European System of Accounts (ESA95) on Community legislation. The ESA95 Manual on government deficit and debt (MGDD) published by Eurostat provides further elements for interpreting the accounting rules of ESA95. In the case submitted, are of particular relevance Annex II of ESA95 and MGDD Part IV on Leases, licences and concessions.

Availability of national accounting analysis

The Belgian Treasury, in their letter of 21 December 2007, consider that the expenditures incurred by the Belgian government during the renovation period should be accounted in the Belgian national accounts as undertaken on behalf of the EU (without an impact on net lending / net borrowing) and not as general government expenditure.

Analysis

The accounting question in the present case is, whether the Council will be an economic owner of the building already during the renovation phase, i.e. before signing the sale agreement with the Belgian government.

Eurostat observes that the project of the final convention does not change substantially the relations between parties during the renovation phase, i.e. the Belgian government (a) remains the legal owner of the building, (b) bears the responsibility for construction, as well as (c) costs of renovation during the execution of works.

However, under the draft of the final convention, the Council decided to make available 87 million euro for the pre-financing of the renovation works in its budget of 2007 and 2008.

An important change of the draft final convention in comparison to the initial memorandum of understanding is that both parties foresee now a sale transaction after the completion of the renovation works. Previously a long-term rental contract with a sale option was only considered.

In order to assess whether the expenses of the Belgian government for the renovation of the building can be recorded in national accounts as undertaken on behalf of the Council, it should be established whether the Council can be considered as the economic owner of the building already before the renovation process. In particular, it would need to be considered whether the draft final convention introduces an obligation for the Council to buy the building already before the start of the renovation works.

In this context, Eurostat notes that Article 15 of the draft final convention contains provisions on the preliminary approval of the building by the Council. In this context, the Council has the obligation to proceed with the approval, or justify its decision not to do so, thereby initiating a conciliation procedure. The automatic consequence of the preliminary approval is a possible occupation of the building by the Council, the start of the 24-month warranty period, and the implementation of specific provisions concerning the sale and price payments. Apart from the procedure concerning the preliminary approval of the building, no further conditions for the sale of the building are specified that might indicate that the Council would have the right to withdraw from the sale.

It would thus seem that the economic ownership of the building will be transferred to the Council with the signature of the draft final convention and that the expenses on fixed capital formation could be reflected in the Belgian government accounts as on behalf of the EU.

Conclusion

On the basis of the above considerations, Eurostat concludes that the gross fixed capital formation expenditure during the renovation phase could be recorded by the Belgian government on behalf of third parties without a negative impact on the net lending / net borrowing, after the signing of the final convention.

Procedure

There is no explicit Community legislation which governs a procedure by which Eurostat gives its views on operations which have not yet been enforced. Nevertheless, Eurostat is prepared to give a preliminary view on the statistical classification of such operations provided that it is in possession of all of the necessary background information. The preliminary view is given in accordance with the guidelines for ex-ante advice published on the Eurostat website.

This preliminary view of Eurostat is based on the information provided by the Belgian 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. To this end Eurostat could request to be informed of the final details of the operation (contract and accompanying papers where relevant) when they are available, or (should this be the case) information that the planned operation has been abandoned.

In this context, 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, therefore, publishes all official methodological advices (ex-ante and ex-post) given to Member States, on the Eurostat website. 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 11 April 2008.

Yours sincerely,



Laurs Nørlund
Director