



EUROPEAN COMMISSION



EUROSTAT

Directorate C: National and European Accounts

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Mr Lambert Verjus
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Subject: Sector classification of Citeo (ex. STIB Invest) in the context of a PPP operation

Ref.: Your letter: T/C2/2007/005554 dated 27 March 2007
Our letter: ESTAT/C-3/LN/LA/MW/mg D(2007) 30182 dated 25 July 2007
Your letter: T/C2/2007/014624 dated 25 September 2007
Our letter: ESTAT/C-3/LN/LA/MW/mg D(2007) 30369 dated 14 November 2007
Your letter: T/C2/2007/018529 dated 30 November 2007

Dear Mr Verjus,

Following your letter of 30 November 2007, I am in a position to reply to the question you asked on the appropriate statistical treatment for the case you have presented.

The accounting issue for which a clarification is requested

The issue for which an opinion is being sought is the appropriate statistical treatment of the sector classification of Citeo (ex. STIB Invest) and whether the envisaged forthcoming operation can be treated in national accounts as a Public-Private Partnership (PPP).

Documentation provided

Eurostat notes that the Citeo operation was subject to two rounds of an ex-ante methodological consultation by the Belgian statistical authorities in 2007. During these previous ex-ante consultation rounds, the Belgian statistical authorities provided Eurostat with an explanatory note (Memorandum on the ESA95 treatment of the STIB-CITEO project), together with several documents about the envisaged operation:

1. Detailed description of Citeo's prospective activities
2. Updated business plan for Citeo
3. Note summarizing the Citeo-project as approved by STIB's management committee
4. Articles of association of Citeo
5. Overview/calculation regarding Citeo's public transport infrastructure investment program
6. Current draft of the concession agreement (*contrat de concession*)
7. Current (sample) draft of SLA on tramways

8. Brussels-Capital Region's legislation (*Ordonnance*) in relation to the Citeo project
9. Explanatory memorandum (*Exposé des Motifs*) to the Brussels-Capital Region's Citeo legislation (*Ordonnance*)
10. Note by consultancy firm Arthur D. Little on Citeo's fee and invoicing model

Description of the case

To recall, the regional government of the Brussels-Capital Region intends to reorganise the regional public transportation company STIB, a public undertaking currently classified in the state government sub-sector. STIB currently operates metro lines, which heavy infrastructure is owned by the state government (STIB owns tracks, carriers, ...), as well as owns and operates tramways and bus lines in the Brussels region. It is envisaged to transfer some of these tasks to Citeo, a recently created company fully owned by the state government through STIB and SRIB (*Société régionale d'Investissement de Bruxelles*). The members of the statutory management bodies of Citeo will be appointed by the shareholders (i.e. state government).

The current infrastructure department of STIB, its assets and liabilities, including the ownership rights to the regional transport infrastructure that is currently held by STIB will be transferred to Citeo. The main tasks of Citeo will be the management and development of the totality of the transport infrastructure of the Brussels region, which it will fully own subsequently to the envisaged restructuring. Citeo will build and maintain the heavy state government infrastructure that remains in the ownership of the Brussels-Capital Region (metro). STIB will retain the public transport operating activities, and acquire an equity stake in Citeo.

The major part of Citeo's revenues will consist of charges, for the use access charges or for the maintenance of the transport infrastructure, paid by the state government, through the reorganised transport operating company STIB (running buses, tramways and metro), classified inside government, and through the Brussels-Capital Region (owner of the underground stations and tunnels).

The issue for which an opinion is being sought is a classification of Citeo in national accounts, as well as whether the whole operation can be considered as a PPP.

Methodological analysis by Eurostat

After an examination of the documentation provided, Eurostat has reached the following provisional views.

Applicable accounting rules

ESA95 paragraph 2.12 applies in this case. In addition, the Eurostat ESA95 Manual on government deficit and debt (MGDD) Part I, Delimitation of the general government sector, Part IV, Leases, licences and concessions, and Part IV.4.2, Long term contracts between government units and non-government partners (Public-Private-Partnership) are relevant.

Availability of national accounting analysis

The letter of the Belgian statistical authorities and the explanatory note provide the opinion that:

1. Citeo is an institutional unit in the meaning of the ESA95 paragraph 2.12.

2. Citeo shall be considered as a market producer, and is to be classified outside the government sector.
3. The whole arrangement between STIB and Citeo should be considered within the ESA95 meaning of PPP contracts, where Citeo is the operator and STIB is the grantor.
4. This PPP contract should be recorded off-balance sheet of the government sector.

Analysis

Classification of CITEO

Concerning the autonomy of decision of Citeo, Eurostat notes that the entity is wholly owned, directly or indirectly, by the state government, and is instrumental for the government objectives of the provision of public transportation services, and that its activity consists almost exclusively of providing services to government.

It is recalled that, the MGDD chapter on leases, licences and concessions makes a reference to the concept of SNA93 of ancillary entities, that would seem relevant for the described case: *"For instance, having the legal status of a corporation, an ancillary corporation is a subsidiary unit, 'wholly owned by a parent corporation [...] (and) strictly confined to providing services to the parent corporation.' [...] (SNA93, §4.40). (...) According to §4.43, 'the ancillary corporation should be treated as an integral part of the parent and its accounts consolidated with those of the parent.'"* The MGDD concludes that *"The same line of reasoning should be applied to the case of ancillary units created by the government for identical purposes (solely providing services to government). Then, all transactions between government and such units should be consolidated when compiling national accounts."*

From the analysis of the provided documentation, Eurostat observes several elements that reinforce its previous opinion expressed in the letter dated 14 November 2007 advising treating Citeo not as an independent institutional unit, but as ancillary unit to the state government:

- Article 23 of Schedule 4 "Articles of association of Citeo" states: *"Si un commissaire du Gouvernement estime qu'une décision du conseil d'administration va à l'encontre ... de l'intérêt général, il introduit un recours auprès du Gouvernement de la Région de Bruxelles-Capitale dans les quatre jours. (...) Si le Gouvernement n'a pas annulé la décision dans un délai de vingt jours, à partir de l'introduction du recours, cette décision devient définitive. Le Gouvernement notifie sans délai l'annulation à la Société."*

It is thus understood that the government can cancel decisions of Citeo on the basis of the perceived infraction to a broad legal concept of "general interest". In this context, one can wonder whether Citeo could, e.g., freely sell or acquire assets, enter into contracts, decide where to build new infrastructure, or whether it would need to follow some precise instructions of the state government (STIB and Brussels-Capital Region).

- Point 2.2.1 of Schedule 5 "Current draft of the concession agreement" states: *"Chaque projet d'investissement majeur pour lequel une demande formelle de développement et de mise à disposition est adressée par le concédant [STIB] au concessionnaire [Citeo], fait successivement l'objet, en concertation étroite avec le concédant, d'une ou de plusieurs études de faisabilité de la part du concessionnaire, qui soumet celles-ci à l'approbation du concédant et développe les spécifications fonctionnelles et techniques de base, soumises à l'approbation du concédant. Sur la base de ces spécifications, dûment approuvées par le concédant, le concessionnaire développe et soumet au concédant un projet détaillé, accompagné d'une*

proposition spécifiant la structure et le montant complémentaire de redevance périodique liées à ce nouvel investissement, de même que les délais de mise à disposition et autres modalités (hypothèses, organisation et contraintes de réalisation,...) sur lesquelles s'engage le concessionnaire à l'égard du concédant."

Citeo seems thus *de facto* to operate and execute its investments following the detailed specifications and precise needs of state government.

- Schedule 10 "Note by the consultancy firm Arthur D. Little on Citeo's fee and invoicing model" states: *"Le montant de l'investissement prévu doit être approuvé par le concédant [STIB] et tout ajustement est soumis à approbation."*

Eurostat understands in this respect that the investment programme of Citeo is fully dependent on STIB's decisions and agreement.

Eurostat reiterates that Citeo has a nature of an ancillary unit to state government, due to the following facts: i) it is fully owned by the state government (STIB and, indirectly, via SRIB), ii) its activity is in its quasi entirety a provision of services to state government (STIB and the Brussels-Capital Region), iii) government determines the details of the investment activities, and iv) it is specifically created to provide, via a different arrangement, the same service as provided by the infrastructure department of STIB up-to-date.

Citeo as a market / non-market producer

The MGDD part I.2 states that: *"Payments from general government to public institutional units in respect to actual services provided are not to be treated as corresponding to sales in the implementation of 50% rule when prices are not economically significant, e.g. in the following two cases:*

- (...)
- *When, in the absence of private producers in the same kind of activity, a public unit is not placed vis-à-vis the market in a position similar to what could be the position of a private unit, because the general government tends anyway to cover its remaining deficit. Therefore, the global amount of payments from the general government to the public unit remains in fact linked to the costs. In this situation, the general government decides to finance the public units in respect to actual services provided for purely administrative reasons, in order to allocate the financing, to control and to compare the costs and to improve the internal productivity of the public units."*

It is currently doubtful that, according to the above-mentioned rule, Citeo could be indeed considered as a market producer. In this context, Eurostat notes that the Citeo fee system seems to be based also on different costs borne by Citeo during its activity (see: point II of Schedule 10).

Classification of the arrangement as a PPP contract

The MGDD chapter on PPPs (Part IV.4 2.1.2.g) provides for criteria for considering given projects or contracts as PPPs, notably the following: *"This type of contract mentions specifically-designed assets which generally need a significant initial capital expenditure (which is precisely why government uses such arrangements in many instances), and the delivery of agreed services, requiring the use of these assets and according to given quality and volume standards that are specifically defined in the contract. It is in this sense that these contracts differ from leases. The*

contract may refer either to a new asset or to significant refurbishment, modernisation or upgrading of existing assets, including assets already owned and managed by government but provided that the expenditure for renovation, etc., will represent a predominant part of the new value of the asset after renovation."

Eurostat notes that the updated project law and statutes of Citeo specify new transport infrastructure projects to be completed by this entity, and that a specific contract (contrat de concession) between government (grantor) and Citeo (concessionaire) is foreseen to be signed for the provision of defined assets by Citeo against specific payments by STIB for this service.

However, from the information provided on prospective Citeo activities, it would seem that the value of investments on new assets and refurbishments of the existing ones will not represent a major part of the future value of the upgraded total transport infrastructure. The already existing infrastructure has supposedly significantly higher value than the planned extensions and refurbishments.

In addition, Eurostat notes that Citeo is 100% public and has been specially created for the purpose of establishing an arrangement with STIB. The MGDD states: *"However, specific attention should be given to cases where the public corporation is 100% government-owned (or to a level close to 100%), and thus there is an absence of private investors in the public corporation who would exercise a significant influence to ensure commercial profitability and efficiency. In cases where payments by government under this contract are a predominant part of the partner's revenue, such that for this public corporation this contract alone results in a significant change in the size or nature of its activities, this corporation could be reclassified as a government unit, depending on the application of the rules described in part I of this Manual.*

As regards contracts with special units, created on purpose (frequently referred to as special purpose vehicle), the only case to be considered is where such unit is created mainly by government and is fully controlled by it."

It is also our understanding that Citeo will be the owner of the new infrastructure built in the coming years. According to the information provided in the explanatory note, STIB will contribute financially to the cost of new infrastructures built by Citeo. In this context, it is not currently known who will bear the risk of cost overruns, and no complete information is available on penalties and sanctions for not fulfilling the contractual obligations by any party.

The "Current (sample) draft of SLA on tramways" suggests that for most of the eight considered infrastructure availability indicators, permissible tolerance margins of delays or non-provision of services to be performed by Citeo are set on a high level. In this context, taking into account historical values of indicators listed in the sample SLA on tramways, Citeo would not be in practice financially liable for any disruptions of its services. In addition, article 10.3 of the Current draft of the concession agreement (contrat de concession)" seems to cap penalties at 6% of the availability fee, which implies an insufficient transfer of availability risk.

Eurostat considers that it is improper in this case to treat in national accounts the arrangement between government and Citeo as a long-term concession agreement that have features of a PPP contract in the meaning of the MGDD, due to the following general observations:

- (1) It is impossible to analyse the extent of the construction risk transfer, given that the value of investments on new assets will not make a major part of the value of the future upgraded infrastructure.

- (2) The revenues related to the Citeo-STIB arrangement originate from STIB, in its capacity of a user of Citeo assets and/or consumer of Citeo services. We are thus not in the context of a provision of services to users with payments by a third party. When the payer is simultaneously the user, special care must be exercised to recognize, if the contract has the feature of a PPP.
- (3) In this context, the whole arrangement seems to resemble the organization foreseen for national railways in the EU Member States separating infrastructure from operating companies. Eurostat notes that the subsequent rental contracts for the use of the railway infrastructure between the infrastructure companies and transport service operators are not treated in national accounts as PPP contracts, but as provision of services.

Conclusion

Eurostat considers that Citeo has a nature of an ancillary unit to the state government and is to be classified inside the state government sector.

Additionally, the planned contractual arrangements between Citeo and STIB cannot be treated as a PPP-type project in the meaning of the relevant MGDD chapter.

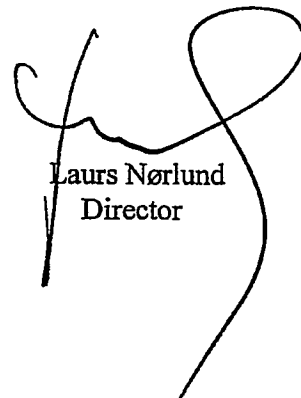
Procedure

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 publishes all official methodological advice (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 10 April 2008.

Yours sincerely,



Lours Nørlund
Director