



EUROPEAN COMMISSION



EUROSTAT

Directorate C: National and European Accounts

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Subject: Formal consultation on the classification of the assets in the Public-private partnership (Autovía del Salnés, Tramo enlace con la PO-531-SANXENXO)

Ref.: Your letter of 13 February 2008 and 5 March 2008

Dear Mr Gómez del Moral,

Following your letters of 13 February 2008 and 5 March 2008, I am in a position to reply to the consultation on the appropriate statistical classification 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 a determination of the correct EDP accounting treatment of the classification of the assets in the Public-Private partnership (PPP) contract for the construction, maintenance and exploitation of the *Autovía del Salnés, Tramo enlace con la PO-531-SANXENXO*.

Documentation provided

The following background documents were provided to Eurostat:

- Consultation request by the Comunidad Autónoma de Galicia;
- Report from the Working Group on General Government issues (INE (National Institute for statistics), IGAE (Government Audit Office) and Banco de España) on the classification of the PPP assets;
- Two notes prepared by the Comunidad Autónoma de Galicia on the analysis of the PPP contract for the construction, maintenance and exploitation of the *Autovía del Salnés, Tramo enlace con la PO-531-SANXENXO*;

- Particular Conditions and Technical Specifications for the call for tender of the concession for the construction and exploitation of the *Autovía del Salnés, Tramo enlace con la PO-531-SANXENXO*;
- The PPP contract for the construction, maintenance and exploitation of the *Autovía del Salnés, Tramo enlace con la PO-531-SANXENXO*.

Description of the case

The issue for which an opinion is being sought is a determination of the correct classification of the PPP assets "*Autovía del Salnés, Tramo enlace con la PO-531-SANXENXO*".

The Spanish statistical Working Group on General Government issues (comprising INE, IGAE and Banco de España staff) examined all the documentation related to the above mentioned PPP contract in order to determine the classification sector of the PPP asset. As a result of this analysis, the Working Group considered that the assets should be classified on the balance sheet of government (S.13), with impact on government deficit and debt.

In line with the Article 8c of the *Council Regulation 2103/2005 of 12 December 2005* and following a request of the Comunidad Autónoma de Galicia to INE, INE asked Eurostat for a formal consultation on the classification of the PPP assets in question.

Methodological analysis and clarification by Eurostat

Applicable accounting rules

The Eurostat ESA95 Manual on government deficit and debt (MGDD) chapter (*Part IV.4*) on *Long term contract between government units and non-government partners (Public-private partnerships)* is relevant.

Availability of national accounting analysis

The Working Group on General Government issues mentioned above considers that the PPP assets should be classified on the balance sheet of general government (S.13), with impact on government deficit and debt.

The opinion of the Working Group is that clause 6 of the contract's *Particular Conditions and Technical Specifications* related to the duration of the PPP has a decisive influence on the sector classification of the PPP asset. The limits imposed with this clause attenuate significantly the deductions and rewards mechanism, and therefore the transfer of risks and rewards to the private partner does not comply with the required terms in the manual on government deficit and debt.

Analysis

After an examination of the background documentation provided by the Spanish statistical authorities, Eurostat has reached the following views.

It is recalled that, according to national accounts rules, in order for the asset to be classified on the balance sheet of the private partner, both of the following conditions should be met:

- The private partner bears the construction risk, and

- The private partner bears at least one of either availability or demand risk.

The MGDD provides a list of criteria (non-exhaustive) that are typically applicable to assess the extent of the risk transfer for each of the construction, availability and demand risks. On observation of the contract, Eurostat observes the following three fundamental features.

1. Firstly, Eurostat observes that, whereas the contract is designed to provide government payments as a function of traffic (thus of a demand fee nature), these are structured in a manner that provides, for a given traffic, a relatively high floor in case of availability deficiency. A key point to be taken into account here is clause 83 of the *Particular Conditions and Technical Specifications*, which establishes the maximum limit of the penalties for inadequate performance of the private partner, as follows: "... *The maximum limit of the penalties to be imposed on the toll company will not be more than the 10 % of the work total budget during the construction stage, or the 20 % of the income obtained by the exploitation of the dividend highway during the previous year, during the exploitation stage ...*"

The manual on government deficit and debt indicates in the Part IV.2.3.2 – Assessment of the risk (availability risk) that "*Furthermore, the existence of a maximum amount or percentage of penalties that could be applicable in the event of defaulting performance would also suggest that this risk has not been significantly transferred to the partner.*"

It would thus seem that the availability risk is insufficiently transferred, by a wide margin, if at all.

2. Secondly, stipulation 4 of the contract as well as clause 6 of the *Particular Conditions and Technical Specifications* seem to put a total limit to the fees collectible by the operator and to indirectly regulate the total return on its investment, in a manner that puts a question mark on the reality of demand risk transfer.

Stipulation 4 of the contract puts a maximum annual fee payable to the operator, by setting a "top limits of traffic payment": ... *the maximum limits of traffic payment, expressed in vehicles-kilometre per year, as limit point from which the Ministry of Territorial Politics, Public Works and Transport should not pay fares (demand canon) to the Salnés Motorway, concessionary society of the Xunta de Galicia will be the following ones:*

Light vehicles: 171.925.042

Heavy vehicles: 12.937.808."

In addition, clause 6 on the duration of the concession of the *Particular Conditions and Technical Specifications* states that "*The concession duration will be 30 years starting from the date the contract is signed. However, the concession will end after 20 years have passed from this date, if the Economic and Financial Plan offered by the granted tenderer is fulfilled. For these purposes, the Economic and Financial Plan offered by the granted tenderer is understood to be fulfilled if the current net value of the payments of the granting Administration, discounted at a rate of 5.0 % and in nominal Euros on 31 December 2004, exceeds the maximum value established by the granted tenderer's financial proposal. The updating of payments will be done monthly, taking the last day of the month when the corresponding payment is due as a reference.*

In the case that, by the end of the concession period, payable obligation from the concession holder are still pending derived from its financial plan, this will not imply any obligation on the part of the granting Administration.

In any case, once the concession has ended and having complied with the provision established in Clause 66 of these bidding conditions, all the concession road works and sites will be returned to the Public Administration."

Both clauses put *de facto* a limit to the overall payments that government will pay to the private partner, and consequently the revenues that the private partner obtains, over the life of the contract. In addition, clause 6 *de facto* creates a mechanism that aims at stabilizing the total return on funds invested – and at a rather low level (5%). In the case of a high demand and/or good management of the private partner, the contract would be terminated already in the year 21, if the agreed return is reached, earlier than the nominal 30-year duration of the contract.

Consequently, the private partner would not be able to reap the benefit of better performance or demand, which indicates a limitation on the transfer of rewards to the private partner.

It can also be noted that the rate of return of 5% seems low, potentially suggesting limited risks faced by the partner, which may be due to the fact that the potential duration of the contract (30 years) serves to provide a satisfactory cushion to the investors.

3. Finally, it is noted that government has the possibility to change the contract, if justified by "public interest", as stated in the clause 77 of the *Particular Conditions and Technical Specifications* (Prerogatives of the Administration) under items b, c and e as follows: "*The awarding Administration, in the terms established in the changed legislation of Administration contracts (TRLCAP), in the valid legislation and in the present folder, will have the following prerogatives and rights:*

- b) modifying the contract because of reasons of public interest properly justified;*
- c) Re-establishing the economical balance of the concession in favour of the public interest, in the way and the extension provided in the present folder and in the article 248 of the TRLCAP;*
- e) Establishing, if it is the case, the maximum tariffs for the application of the demand canon. ..."*

Thus, government has the possibility to amend or change the contract for public interest purposes, i.e. changes the maximum tariffs of royalties paid to the private partner so to re-establish the economical balance of the concession. The argument that the awarding Public Administration has to guarantee the viability and sustainability of projects for public interest reasons cannot be a justification for avoiding the accounting consequence of such limitations.

On the basis of the four above-mentioned clauses, Eurostat considers that government remains most of the risks and rewards of the contract, given that it has not substantially transferred availability or demand risks. Therefore, the assets built should be on the balance sheet of government.

Conclusion

On the basis of the above considerations, Eurostat agrees with the opinion of the Working Group on General Government that the PPP assets of *Autovía del Salnés, Tramo enlace con la PO-531-SANXENXO* should be classified on the balance sheet of the government (S.13), with impact on government deficit and debt.

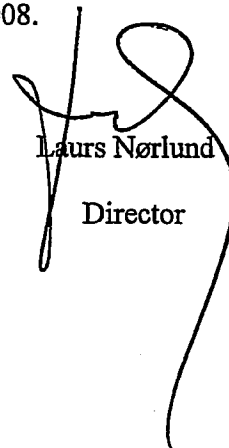
Procedure

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 web-site.

This preliminary view of Eurostat is based on the information provided by the country 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 would 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 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 21 June 2008.

Yours sincerely,



Lours Nørlund
Director