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Unit C-4: Statistics for Excessive Deficit Procedure II

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**- FINAL FINDINGS -**

**EDP dialogue visit to Cyprus**

**13 December 2010**

## Executive summary

*Eurostat conducted an EDP dialogue visit to Cyprus on 13 December 2010 with the aim to review all the relevant statistical organisation issues, analyse the EDP tables reported in the context of the October 2010 notification and examine methodological issues relating to the recording of specific government transactions.*

*Regarding the statistical organisation issues, the Cypriot statistical authorities informed Eurostat that there have been no changes in the responsibilities of the institutions involved in EDP reporting. Furthermore, the Cyprus authorities agreed to send to Eurostat an updated EDP inventory with a new list of public corporations by the April 2011 EDP notification.*

*There was an agreement to further improve the coordination between annual and quarterly financial accounts and resolving the remaining inconsistencies regarding the timing of the production of information from different data sources.*

*The EDP tables of the October 2010 notification were thoroughly examined and a series of issues were clarified. The Cyprus authorities provided explanations for the reclassification of government bills to the financial corporations sector (S.12) and informed Eurostat on developments regarding the issue of penalties imposed on Petroleum companies by the court.*

*Eurostat welcomed the changes to EDP tables 2C and 2D introduced by the Cyprus authorities which provide more information on financial transactions included in the working balance and other accounts receivable relating to social contributions.*

*For EDP tables 3, the Cyprus authorities confirmed the figures for the appreciation/depreciation of debt due to foreign currency movements as well as the entries for other accounts receivable relating to social contribution in Table 3E.*

*Regarding the questionnaire related to the EDP tables, the Cyprus statistical authorities agreed to complete Table 8.1 with information on government claims recorded in the Financial Report and to provide a short note explaining the underlying factors in the evolution of military equipment data by end February 2011.*

*During the discussions on methodological issues and the recording of specific government accounts, it was agreed that a new analysis of public units with respect to the 50% criterion will be carried out by the Cyprus authorities and will be reported to Eurostat by June 2011. In this context, a series of issues relating to public entities were clarified.*

*Concerning government guarantees, the Cyprus authorities confirmed that there were no guarantee calls during the reporting period. Likewise, it was confirmed that the superdividend test was carried out for dividends paid to government, while there have been no privatisation receipts in the period 2009-2010.*

*Eurostat found that the existing arrangements for the recording of the EU flows continue to meet the requirements of the relevant Eurostat Decision, no revenue and payments relating to transactions with the EU budget transit government accounts. Eurostat was also informed that there has as yet been no decision of the European Commission on the issue of disallowances identified by the European Court of Auditors.*

*Regarding PPP projects, securitisation and sale and leaseback operations, it was agreed that the Cyprus authorities will review the contract of the Moni Mobile Desalination plant and*

*report the results to Eurostat by end-February 2011, as well as the statistical treatment of the transfer of Cyprus airport to a private partner.*

## **Introduction**

In accordance with the Council Regulation (EC) No 479/2009 as amended by Council Regulation (EU) No 679/2010 as regards the quality of statistical data in the context of the excessive deficit procedure, Eurostat carried out an EDP dialogue visit with Cyprus on 13 December 2010.

Eurostat was represented by Mr. John Verrinder and Mr. Stelios Pantazidis. A representative of the European Central Bank (ECB) participated in the meeting as an observer. The Cyprus statistical authorities were represented by the National Statistical Institute (NSI), the Ministry of Finance (MoF), and the Central Bank of Cyprus (CBC).

The aim of this visit was the examination of issues relating to statistical organisation, the analysis of the October 2010 EDP notification, as well as the examination of methodological issues relating to the recording of specific government transactions.

Eurostat thanked the Cyprus authorities for their excellent cooperation and provision of very extensive relevant background material. The last EDP dialogue visit was in 2008.

## **1. Statistical organisation issues**

### **1.1 Institutional responsibilities**

#### *Introduction*

The Cyprus Statistical Service (CSS) is responsible for the preparation of the actual deficit data (Tables 2) whereas data on planned deficit and actual and planned debt data (Tables 3) are prepared by the Ministry of Finance. The involvement of the Central Bank of Cyprus (CBC) is restricted to providing only some of the source data.

#### *Discussion*

The Cypriot statistical authorities informed Eurostat that the institutional arrangements for the production of EDP tables in Cyprus have not changed since the last EDP dialogue visit. EDP tables 2 are compiled by the Cyprus Statistical Service, whilst EDP tables 3 are compiled by the Ministry of Finance. The Central Bank of Cyprus provides some complementary data.

#### *Findings and conclusions*

There has been no change in the institutional responsibilities. The tasks for EDP reporting are shared by the National Statistical Institute (NSI) and the Ministry of Finance (MoF), while the Central Bank of Cyprus (CBC) provides some of the source data.

## 1.2 EDP Inventory

### *Introduction*

The consolidated EDP inventory of sources and methods of Cyprus (September 2007) is published on Eurostat's website. The inventory provides information on data availability and data sources for all subsectors of the general government sector.

### *Discussion*

Eurostat was informed that the NSI intends to publish a more simplified (less technical) version of the EDP inventory on its website. Eurostat was also informed that the updating of the existing inventory will be completed by October 2011 along with a new list of public corporations

### *Findings and conclusions*

The updating of parts of EDP inventory will be completed by the October 2011 EDP notification. A new list of public corporations will be added to the existing inventory. *[Action point 1]*

## 1.3 Data sources

### *Introduction*

The State budget is the main data source for compiling the accounts of the **State**. The data reported in the Budget are on a cash basis. All information regarding the transactions of the State is obtained from the National Treasury. The Statistical Service has on-line access to the National Treasury accounts, having thus the ability to monitor all transactions on a daily basis. Budget reporting is also the main data source for the compilation of the accounts of the extra-budgetary funds. Information on the net lending/net borrowing of the **Local Government** is obtained directly from the municipalities and community boards. Information on the accounts of the sub-sector **Social Security Funds** is obtained from the audited accounts of the Ministry of Labour and Social Insurance.

### *Discussion*

Eurostat mentioned the need for further improving the coordination between annual and quarterly financial accounts, as well as the need for a better coordination of the transmission of annual financial accounts with other accounts.

### *Findings and conclusions*

Eurostat took note of the explanations of the NSI that only some inconsistencies remain to be resolved, relating mainly to the timing of the production of information from different data sources.

## **2. EDP reporting – analysis of the October 2010 EDP notification**

### **2.1 EDP Tables**

#### *Introduction*

The EDP tables provided by the Cyprus Statistical Service are quite complete. During the October 2010 notification round no major problems were encountered regarding the recording of government transactions and the required adjustments to the reported working balance. The accruals adjustments are quite limited (four such adjustments are being made: for some categories of income taxes, VAT revenues, military equipment trade credits, and revenue from deposits) as most of the data are reported on an accrual basis.

#### *Discussion*

The EDP tables of the October 2010 notification were thoroughly reviewed and the discussion focused on the following issues: (a) the reclassification for of government bills to the sector S.12 in 2009, (b) developments regarding the penalty imposed to Petroleum companies by the court, (c) the changes in EDP Table 2C providing more information on financial transaction included in the working balance, (d) the change in the EDP Table 2D providing information on other accounts receivable relating to social contributions.

Regarding EDP Table 3, a series of issues were clarified relating to the calculation of changes in debt due to currency movements, the recording of receivables in Table 3E, as well as the adjustments that might possibly be needed for pension benefits payments.

#### **a) EDP Table 1**

##### *Findings and conclusion*

Eurostat took note of the explanation of the Cyprus authorities regarding the reclassification for 2009 of government Treasury bills to the sector S.12 as a one-off problem of the system in identifying the counterparty of the transaction, which would not be expected to re-occur.

#### **b) EDP Tables 2A**

##### *Findings and conclusions*

The Cyprus authorities confirmed that there have been no developments regarding the court decision on the penalty imposed on Petroleum companies.

#### **c) EDP Table 2C**

##### *Findings and conclusions*

Eurostat welcomed the changes introduced in this table which provide information on financial transactions included in the working balance.

## EDP Table 2D

### *Findings and conclusions*

Eurostat took note of the explanations of the Cyprus authorities regarding the change introduced to this table. The table now contains information on other accounts receivable relating to social contributions which are calculated using the method of time adjusted cash with a time lag of one month.

## EDP Tables 3B-3E

### *Findings and conclusions*

- The Cyprus authorities confirmed that the entry for appreciation/depreciation of debt due to foreign currency movements was correctly calculated.
- The Cyprus authorities confirmed that entries for other accounts receivable relating to social contributions to EDP table 3E were added.
- Eurostat took note of the explanations of the NSI that no adjustments are needed for pension benefits payments and that lump sum payments for government officials are made from the State Budget at the time of the retirement of those officials.

## EDP Table 4

### *Findings and conclusions*

Eurostat took note of the clarification of the NSI that trade credits and advances reported in this table cover the whole of general government, and do not relate only to military equipment purchases.

## 2.2 Questionnaire related to the EDP tables

### *Findings and conclusions*

- **Table 8.1** of the Questionnaire will be completed in the April 2011 notification exercise with data on government claims recorded in the Financial Report. *[Action point 2]*
- **Table 7.1** Eurostat took note of the explanations of the Cyprus authorities on the high cash payments compared to deliveries of military equipment. The Cyprus authorities noted that orders for military equipment have been reduced significantly and that in 2010 the recent trend of higher cash payments compared to deliveries is expected to reverse. The Cyprus authorities will provide a short note setting out the main underlying factors in the evolution of military equipment expenditure data by end-February 2011. *[Action point 3]*

### 3. Methodological issues and recording of specific government accounts

#### 3.1 Delimitation of general government, application of the 50% rule in national accounts

##### *Introduction*

The NSI has the responsibility for classification of units, based on ESA 95 and the Manual on general government deficit and debt. According to the EDP Consolidated Inventory of Sources and Methods, each unit is examined to conclude whether it enjoys autonomy of decision, whether it is a private or public unit, and finally whether it is a market or non-market producer, according to the 50% criterion.

##### *Discussion*

During the discussion, Eurostat asked the Cyprus authorities to provide information on the common list of public units which was to be created by all institutions involved in the EDP reporting as well as whether a new analysis of public units was carried out. The discussion also covered the statistical treatment of a series of entities such as the Sewage disposal Boards, the Cyprus Land Development Corporation (non financial institution) – Housing Finance Corporation (financial institution), the Cyprus Broadcasting Corporation, the Cyprus Agricultural Payments Organisation and the newly created Investment Fund.

##### *Findings and conclusions*

- The Cyprus authorities informed Eurostat that the discussions among the institutions involved in the EDP reporting on the creation of a common list of units have been completed with the Central Bank.
- Eurostat took note that a new analysis of public units with respect to the 50% criterion is planned by the NSI for the coming months and the results will be reported to Eurostat by June 2011. [*Action point 4*]
- The Cyprus authorities confirmed that Sewage disposal Boards are profitable and their revenue comes from sales of services paid for by direct users.
- Eurostat took note of the explanation of the Cyprus authorities on the nature of the activities of Cyprus Land Corporation. It is a financial institution providing low interest rate loans for projects relating to land development. An analysis of this entity will be provided to Eurostat by June 2011. [*Action point 5*]
- The Cyprus authorities confirmed that the Cyprus radio-television authority continues to derive its revenues mainly from advertising.
- Eurostat took note of the explanation of the Cyprus authorities that the Agricultural Insurance Organisation is an independent legal entity which handles subsidies to farmers. This Organisation is classified within general government

- Eurostat took note that a new unit (Investment Fund) was created in 2010, and that it will be classified inside the general government sector and therefore its activities will have an impact on government accounts from that year onwards.
- The Cyprus authorities explained the nature of activities of the Investment Fund, which has the aim to undertake exchange-of-asset operations with banks. It was confirmed that the government bonds subject to exchange under the scheme are not counted as part of government debt, in line with the Eurostat decision on liquidity schemes created in the context of financial turmoil.
- Eurostat observed that Sinking Fund continues its activities, however for smaller amounts. The Cyprus authorities confirmed that Sinking Fund has no impact on the calculation of accrued interest.

## **3.2 Recording of specific government accounts**

### **3.2.1 Taxes and Social Contributions**

#### *Introduction*

The Cyprus statistical authorities use a time adjusted cash method to adjust VAT and income tax receipts onto an accruals basis. A time-adjusted cash method of 2 months is used for some income taxes, VAT and one month for social contributions, corresponding to the administrative delay in each case. It is noted that there are no tax rebates, while tax credits were abolished in 2003.

Eurostat had requested that the questionnaire on taxes and social contributions be clearer as in several entries taxes marked "accrual" are actually measured with cash receipts, which are thought by the Cyprus authorities to correspond to an accrual-basis.

#### *Findings and conclusions*

It was confirmed that now the explanation regarding the basis of recording of some taxes and social contributions is clearer in the new questionnaire.

### **3.2.2 Government guarantees**

#### *Introduction*

There is a relatively high level of government guarantees in Cyprus. The majority of these guarantees have been provided to local government and public corporations. There is no system of export credit guarantees in Cyprus.

#### *Findings and conclusions*

The Cyprus authorities confirmed that there were no guarantee calls in 2009-2010. Lines 19 and 20 of the Questionnaire Table 9.1 will be filled in with zeros indicating no transactions at the time of the April EDP notification [*Action point 5*]. The Cyprus authorities noted that all



payments for guarantee calls are recorded in the budget as expenditure – in the case of the call for the Cyprus Development Bank, this was netted off the relevant privatisation proceeds in the budget, but an adjustment was made in the EDP reporting tables.

### **3.2.3 Capital injections, superdividends, privatisations**

#### *Introduction*

General government undertook capital injections in each year during the period 2004-2009. Disposals of equity were reported for 2008 in the October 2010 notification. Significant amounts of distributions to government (around 0.5% of GDP) were reported for the years 2006, 2008 and 2009. No privatisation receipts have been reported in the last years.

#### *Discussion*

The Cyprus authorities were asked whether the superdividend test was carried out for dividends paid to government and whether there have been any privatisation receipts during the reporting period.

#### *Findings and conclusions*

- The Cyprus authorities confirmed that for dividends paid to government, the superdividend test was carried out.
- The Cyprus authorities confirmed that there have been no privatisation receipts during the period 2009-2010. No privatisations are expected in near future.

### **3.2.4 Debt assumptions/debt cancellations/write-offs**

#### *Introduction*

In the October 2010 notification, no debt assumptions or cancellations and write-offs have been reported for the 2006-2009 period.

#### *Discussion*

Eurostat asked the Cyprus statistical authorities to provide any further information on the debt cancellation programme relating to the Public Loans Fund, which was planned for 2008 and would be recorded in the 2008 accounts.

#### *Findings and conclusions*

- The Cyprus authorities informed Eurostat that the debt cancellation programme relating to the Public Loans Fund, which was planned by the government to take place in 2008, did not in fact take place.
- The Cyprus authorities confirmed that no debt assumptions, debt cancellations and write-offs have been carried out in the 2006-2009 period.

### **3.2.5 Recording of EU flows**

#### *Introduction*

The recording of the transactions with the EU budget must comply with Eurostat decision published on 15 February 2005 requiring that those transactions have no impact on net lending/net borrowing of general government.

In the 2008 visit, Eurostat found that the arrangements regarding the statistical treatment of the transactions with the EU budget continue to meet the requirements of the relevant Eurostat Decision.

#### *Discussion*

Eurostat asked the Cyprus statistical authorities to confirm that there has been no change in the arrangements regarding the transactions with the EU budget. Eurostat enquired about the developments on the issue of disallowances identified by the European Court of Auditors.

#### *Findings and conclusions*

- It was confirmed that no revenue and payments (and cash movements) relating to transactions with the EU budget transit government accounts, as they are made through a separate account.
- The Cyprus authorities informed Eurostat that on the issue of disallowances identified by the European Court of Auditors there has been no decision yet of the European Commission. Eurostat confirmed that any impact on the budget should be recorded in the year of the decision

### **3.2.6 PPP contracts, securitisation and sale and leaseback operations**

#### *Introduction*

In the October 2010 notification seven PPP projects were reported. In the request for clarification, it was indicated that all these projects' assets are classified outside general government (S.13). No securitisations and sales and lease back operations were reported.

#### *Findings and conclusions*

- Eurostat took note that no significant expansion of PPPs is expected in the near future.
- The Cyprus authorities will review the contract of the Moni Mobile Desalination plant and report the results to Eurostat by end-February 2011 [*Action point 6*].

- The Cyprus authorities will examine the need for entries in government accounts for the transfer of the Cyprus airport assets to the private partner by end-February 2011 [*Action point 7*].

### **3.3 Financial turmoil**

#### *Introduction*

In the 2008 visit, the Cyprus authorities explained that there have been no particular difficulties in Cyprus banks relating to the financial turmoil. It was not then envisaged that government would guarantee bank borrowing or undertake recapitalisation operations.

Eurostat was informed that there was a deposit guarantee agency, compulsorily funded by private banks, offering a deposit guarantee of up to EUR 40,000 (this limit was raised to EUR 100,000 on 24 July 2009). This agency was classified to the financial corporations sector in national accounts.

#### *Findings and conclusions*

- Eurostat took note that there have been no other government programmes for assisting banks (no capital injections, no direct lending, no guarantees) except for the Investment Fund activities mentioned earlier.
- The Cyprus authorities confirmed that the Deposit Guarantee Agency is classified outside the general government sector.

## **4. Other issues**

### **4.1 ESA95 transmission programme**

#### *Introduction*

Eurostat reviewed the situation regarding the tables of the ESA95 transmission programme.

#### *Findings and conclusions*

- Technical issues relating to the transmission of Tables 6 and 7 will be clarified with Eurostat experts.

### **4.2 Any other issues**

The Cyprus authorities confirmed that purchases of government bonds by social security funds have taken place and recorded, in accordance with the relevant accounting rules, as claims of the social security funds against central government without any impact on general government debt.