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Unit C-3: Public finance



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- FINAL FINDINGS -

EDP Mission to Hungary

10-11 July 2008

Executive summary

An EDP dialogue visit to Hungary took place on 10-11 July 2008.

Eurostat carried out this EDP dialogue visit with the aim to analyse the April 2008 EDP notification, to review the sectorisation of some units, to ensure that the provisions from the ESA95 Manual on government deficit and debt (MGDD) and the recent Eurostat decisions are implemented and that specific government transactions are appropriately recorded in the Hungarian EDP notifications and national accounts.

First, Eurostat enquired about the institutional arrangements and division of responsibilities with respect to the reporting of data under EDP. EDP tables are officially reported to Eurostat by the Central Statistical Office (KSH). The statistical office compiles EDP tables 2A-D actual data, and EDP table 1 deficit actual data, while the MoF compiles forecast data for EDP tables 2A-D and EDP table 1 for deficit. The MNB compiles EDP tables 3 and EDP table 1 debt data. Non-financial government ESA tables (ESA table 2, 9 and 25) are compiled by the statistical office, while ESA table 11 is compiled in cooperation with the MoF. ESA tables 6, 7 and 28 are compiled by the Central Bank. Eurostat took note of the current organisation involving the statistical office (KSH), the Ministry of Finance and the Central Bank (MNB) and encouraged their further cooperation.

Second, the data sources for the main sub-sectors were discussed. Eurostat took note of the reasonably good level of source data availability for GFS compilation in Hungary, with access of the statistical authorities to detailed cash flow reporting of budgetary units (and profit and loss accounts for their entrepreneurial activities) and to balance sheets. Eurostat was informed by the Hungarian statistical authorities that profit and loss reporting on an accrual basis seems to have been disrupted approximately fifteen years ago. This seems to be contrary to current trends in public accounting in Member States, and Eurostat strongly encouraged efforts to re-establish accrual based reporting.

Concerning the EDP tables, a few questions, mostly of presentational nature, were discussed. Regarding EDP table 3B, the question of capital injections into the Central Bank and the recording of repos was discussed. Eurostat took note of the reasons why the Hungarian statistical authorities record short-term repurchase agreements (repos) invested within the banking system as loans instead as deposits. Eurostat took note of the explanations and promised to address the question on capital injections into central banks at the MGDD Editorial Committee, in the context of the finalisation of the capital injection chapter.

Sectoral delimitation issues were also discussed. Eurostat welcomed the description of the Hungarian authorities of their approach and the financial statements provided.

The issue of the sectorisation of the transportation companies was examined. Concerning the new split of the railway company into a freight company and a passenger company, Eurostat was informed of the current status of the companies. Financial statements and business plans of these newly created entities and financing arrangements may be subject to further changes. Noting that one could not wait for the October 2009 notification (time when the first annual financial statement will be available), Eurostat invited the Hungarian statistical authorities to make a decision on the classification of the passenger company (MÁV-Start) without delay and in any case before the next EDP notification of October 2008. Concerning the freight company, which just had been privatised, Eurostat enquired about the recording of transactions. As far as the privatisation proceeds obtained in

the context of the disposal of equity of MAV-Cargo is concerned, Eurostat indicated that the rules concerning indirect sale of financial assets must be applied.

Eurostat also took note of the situation of the Budapest transportation company, BKV ZRt, and invited the Hungarian authorities to regularly check the 50% rule for this company, as it seemed to be very close to the 50% threshold.

Eurostat took note that the vignette for the use of roads is considered as a sale of service in Hungary, in application of Eurostat's guidance note released on 7 March 2008. Eurostat also noted that the vignette also covers motorways under PPP contracts where the motorway assets are recorded off the government balance sheet.

Eurostat welcomed the detailed description provided by the statistical authorities to Eurostat (before the mission) on the criteria used in Hungary for risk transfer assessment. Eurostat will reflect on the proposition of the statistical authorities to update the PPP chapter, notably in order to take stock of new developments in PPPs not included in the existing chapter. Given the high number of PPP projects already classified off government balance sheet (2.5 billion € of total value under contract), the Hungarian statistical authorities were invited to consult Eurostat in writing (for advice), in particular for contentious or doubtful cases.

The Hungarian authorities explained to Eurostat their method for recording EU grants, which in principle is in line with Eurostat's decision on the neutralisation of these flows. Eurostat found a good situation with respect to the source data, which allows Hungary to adhere strictly or very strictly to the Eurostat decision. However, Eurostat underlined that the current method overestimated the deficit due to the fact that receipts received from the EU, and entering the working balance, are adjusted downwards when they are higher than the expenditure in a single year, but are never adjusted upwards in the opposite case. Eurostat found this situation highly anomalous and suggested that the Hungarian statistical authorities assume, in the absence of any other detailed information, that the excess of revenue over expenditure in a single year originated from the year before – and correct the data accordingly. Eurostat also provided clarification on more difficult cases where (1) the project is not definitively agreed with the EU, (2) the co-financing rate is set in advance but the actual value can vary, or when it can be modified later, (3) the last part of the expenditure must be advanced by the Member State, and (4) irregularities lead to deductions.

On the issue of capital injections, the Hungarian authorities informed Eurostat that tables Va and Vb of the EDP related questionnaire are not fully consistent and will be corrected in the next EDP notification. Concerning the capital injections into VOLÁN companies, the statistical authorities explained that the capital injection test is applied appropriately, first by the owners (local governments that decide to record a subsidy or a capital operation) and later on, is checked as well by the Central Bank, unit by unit (and not as a group). As far as the capital injections into forestry companies are concerned (currently recorded as transactions in equity), Eurostat considered that these should be most likely recorded as capital transfers, given the pattern of repetitive payments and also given the fact that these seem to have the nature of investment grants. This would imply an increase in the notified deficit.

The meeting was constructive and Eurostat appreciated the explanations provided by the Hungarian authorities during the dialogue visit and the documentation provided prior to the visit.

Final findings

Introduction

In accordance with article 8d of Council Regulation (EC) No 2103/2005 of 12 December 2005, amending Council Regulation (EC) No 3605/93 as regards the quality of statistical data in the context of the excessive deficit procedure, Eurostat carried out an EDP dialogue visit in Hungary on 10-11 July 2008.

Eurostat was represented by Ms Maria-Helena Figueira, acting director of Directorate C – National Accounts, Mr. Luca Ascoli, head of unit C.3, Mr. Philippe de Rougemont (Unit C.3), and Miss Ágota Krénusz (Unit C.3). The Directorate General for Economic and Financial Affairs (DG ECFIN) also participated in the meeting as observer.

Representatives of the Hungarian statistical office (KSH), the Ministry of Finance, and the National Bank (MNB) were present.

Eurostat carried out this EDP dialogue visit with the aim to assess the existing statistical capacity, to review the division of responsibilities concerning the compilation of EDP statistics and government accounts, to discuss the quality and exhaustiveness of primary data sources, to clarify the issues relating to EDP tables raised in the context of previous notifications, to review the progress achieved in implementing ESA 1995 methodology (sectorisation of units, accrual principles), to assure that the provisions from the ESA 1995 Manual on Debt and Deficit and recent Eurostat decisions are duly implemented, and that specific government transactions are properly recorded in the Hungarian EDP tables and national accounts.

In relation to procedural arrangements, Eurostat explained the new procedure, in accordance with article 8 of Regulation 3605/1993 as amended, indicating that the *Main conclusions and action points* would be sent within days to the Hungarian statistical authorities, who may provide comments. Within weeks, the *Provisional findings* would be sent to the Hungarian statistical authorities in draft form for their review. After adjustments, *Final Findings* will be sent to the Economic and Financial Committee (EFC) and published on the website of Eurostat.

1. Statistical capacity issues

1.1. Institutional responsibilities in the framework of the reporting of data under EDP and government finance statistics compilation

Introduction

EDP tables are officially reported to Eurostat by KSH. The statistical office compiles EDP tables 2A-D actual data, and EDP table 1 deficit actual data, while the MoF compiles forecast data for EDP tables 2A-D and EDP table 1 for deficit. The MNB compiles EDP tables 3 and EDP table 1 debt data. Non-financial government ESA tables (ESA table 2, 9 and 25) are compiled by the statistical office, while ESA table 11 is compiled in cooperation with the MoF. ESA tables 6, 7 and 28 are compiled by the Central Bank.

Discussion and methodological analysis

Eurostat took note and complimented the Hungarian authorities for the formalisation of cooperation between the three institutions involved. There are regular meetings at a high level. In addition, a formal permanent working group was set up in 2004, which meets particularly actively at time of notification. Since 2004, a working agreement between institutions has existed, which was complemented in 2006 with a more detailed annex. The Hungarian authorities will provide Eurostat the latest version of the agreement.

In addition, Eurostat took note that reporting obligations to the statistical authorities present in the room as well as to other statistical authorities are foreseen annually in a government decree (after agreement of a statistical committee), in application of the Government Act on Statistics. Finally, Central Bank decrees regulating reporting obligations by various entities to the Central Bank are also relevant for the compilation of government finance statistics (GFS).

Findings and conclusions

Eurostat took note of the current organisation involving the statistical office (KSH), the Ministry of Finance and the Central Bank (MNB) and encouraged their further cooperation.

1.2. EDP Inventory and data sources

Introduction

The data sources used for the main sub-sectors, as described in the EDP inventory, were discussed.

Discussion and methodological analysis

Eurostat took note of the reasonably good level of source data availability for GFS compilation in Hungary, with access of the statistical authorities to detailed cash flow reporting of budgetary units (and profit and loss accounts for their entrepreneurial activities) and to balance sheets. Local governments report data to the regional treasuries, in the form of quarterly reporting, on a cash basis, which is then posted on the Treasury website. Central budgetary units maintain their accounts at the Treasury, so for such units monthly data are available, posted on the Treasury website. Owing to the late availability of aggregated final data (starting from April), the first notification uses the Treasury accounts information for central government and social security and flash estimates for local government, which are considered by the Hungarian statistical authorities as reliable information for estimating the final results. Interest and subsidies are managed centrally. Eurostat was informed by the Hungarian statistical authorities that profit and loss reporting on an accrual basis seems to have been disrupted approximately fifteen years ago. This seems to be contrary to current trends in public accounting in Member States, and Eurostat strongly encouraged efforts to re-establish accrual based reporting.

The Hungarian statistical authorities informed Eurostat that EDP Tables 3 and ESA tables 6 and 27 reporting the financial accounts of government are compiled by the Central Bank, using in large measure counterpart information (e.g. money and banking data, securities data), instead of direct government source data, although cash flow information seems to be available. Eurostat noted that

the use of counterpart information may be appropriate only in the absence of direct source data or when a good reason exists for departing from direct information. In this case, this choice must be appropriately documented and justified, and any difference in data should not lead to entries into the statistical discrepancy but should generally be reported elsewhere in the financial accounts. Eurostat noted that the use of counterpart information might explain the discrepancy in EDP tables 3 in Hungary – which is systematically positive for local government, a cause of concern. The Hungarian statistical authorities expressed their agreement with Eurostat's position, and indicated their plan to compile, on a test basis, the financial accounts of government using direct source data, with the view to decide the most appropriate action. This was strongly encouraged by Eurostat.

Concerning revision policy, the Hungarian authorities explained that the Audit Office examines data at the end of June and its report is submitted to the Parliament at the end of August each year. If the Parliament accepts the appropriation accounts, then data are considered to be final by the next May.

Findings and conclusions

Eurostat took note of the explanations provided and of the relatively good level of source data availability in Hungary. Eurostat further expressed the importance of accrual data, and encouraged the Central Bank to use direct information, instead of counterpart information, to compile financial accounts for government.

2. Actual data – EDP reporting

2.1. Examination of the EDP tables: April 2008 notification

Introduction

Eurostat welcomed the timeliness and consistency of the EDP tables sent by the Hungarian authorities in each notification. Some (mostly presentational) issues were discussed.

Eurostat recalled that the *Questionnaire related to EDP tables* is in the process of being updated. The Hungarian authorities expressed their intention to try to compile the pilot questionnaire related to EDP tables, and to send it to Eurostat either at the time of the notification or in the following weeks.

During the meeting, the EDP notification tables from April 2008 notification were analysed.

EDP table 2A

Discussion and methodological analysis

The working balance of EDP table 2A is taken from the appropriation accounts approved by the Parliament and also published on the Ministry of Finance website. B.9 of central government is constructed from the working balance downwards in the April EDP notification, however in the October EDP notification there is a reconciliation between the working balance and B.9 as taken from national accounts sources.

The Hungarian authorities agreed that the correction lines in EDP table 2A for the prepayments to government for oil royalties (MOL) and for UMTS licences should more appropriately be included under the line "other accounts payable" (in the next EDP notification); this is in concept more

appropriate and has the further advantage of avoiding split of adjustment lines (in the case of MOL) which can be confusing to users.

Concerning the claim cancellation against social security funds, the Hungarian authorities explained that the deficit of the social security fund is covered by a loan from central government, which is cancelled the following year but not included in the working balance, therefore a separate adjustment line is included in EDP table 2A.

Eurostat enquired about the adjustment for claim cancellation against Russia, as in the April 2008 EDP notification the Hungarian authorities provided only preliminary figures and promised to inform Eurostat if the information were available. Because of new developments, the Hungarian authorities will provide new information on this in the October 2008 EDP notification.

EDP table 2C

Discussion and methodological analysis

The local government working balance is cash based and is taken from the flash estimate of cash-flow in April and from the Treasury accounts in October. According to the statistical authorities, the April estimate is a good proxy, and does not change considerably in the October notification.

Concerning local government, the Hungarian authorities promised to provide more information to Eurostat on the considerable decrease in equities in 2007.

Regarding the "Imputed loans related to dwelling privatisation", listed under "Other adjustments" in EDP table 2C, the Hungarian authorities explained that these relate to the subsidized purchase by households of flats previously owned by local governments. The Hungarian authorities presented an excel table, which showed the calculation of this adjustment line, and Eurostat accepted the recording of this item.

Findings and conclusions

Eurostat took note of the explanations and the Hungarian authorities will provide an explanation of the considerable decrease in equities in 2007.

EDP table 2D

Discussion and methodological analysis

The working balance of social security fund is taken from the Treasury accounts, and similarly to central government and extra-budgetary funds, is published and commonly available on the Treasury website.

Eurostat took note of the purpose of the "Debt cancellation by the Central Budget" line among other adjustments, which has the matching entry in EDP table 2A and shows the annual debt cancellation of social security debt by the central government.

Findings and conclusions

Eurostat took note of these explanations.

EDP Table 3B

Discussion and methodological analysis

There were two issues discussed in detail concerning EDP table 3B.

First, the question of the capital injections into the central banks was discussed. The Hungarian authorities expressed their need for an appropriate clarification of the question on the recording of capital injections by government into central banks, in the context of central banks' capital losses. The Hungarian authorities argued against the asymmetrical treatment of holding gains and losses, and asked Eurostat to provide a detailed rationale on the treatment. Eurostat proposed to discuss this issue in the context of the MGDD Editorial Committee in the framework of the finalisation of the chapter on capital injections. Such a clarification would also allow agreeing on an appropriate recording for the case of a large capital injection undertaken by the Hungarian government in the Central Bank in 2002.

Second, Eurostat took note of the reasons why the Hungarian statistical authorities record short-term repurchase agreements (repos) invested within the banking system as loans instead as deposits, as explicitly foreseen by ESA 1995. The national bank indicated that it seems artificial to classify repos according to counterpart sector and that it classifies all of them as loans when drawing up the financial accounts. Eurostat noted that, compared to deposits, which are a means to place liquidities, loans (AF.4) imply an intention by the lender to provide financing to the borrower and are generally at the initiative of the latter. Eurostat recalled a similar case in another Member State. It also underlined that the Hungarian recording is making the monitoring of the loan assets transactions by government, an important aspect of the EDP monitoring, more complex.

Findings and conclusions

Eurostat took note of the explanations and suggested to address the question on capital injections into central banks in the MGDD Editorial Committee in the context of the finalisation of the capital injection chapter.

3. Methodological issues and recording of specific government transactions

3.1. Delimitation of general government sector: classification of institutional units according to ESA95 – application of 50% rule in national accounts

Introduction

Eurostat enquired about the institutional arrangements as well as procedures for methodological decisions on sector classification of units. The sector classification of individual units/groups, such as public infrastructure companies, public hospitals, public TV and Radio were discussed during the meeting.

Discussion and methodological analysis

The statistical office is responsible for the classification of units and the delimitation of general government. Eurostat welcomed the description of the Hungarian authorities of their method and the financial statements provided. Eurostat noted that the Hungarian statistical authorities, via access to financial statements of enterprises contained in the database of the tax authorities, can identify the list of public units (versus private units) and routinely monitor compliance with the 50% rule. This has resulted in the reclassification of some central government controlled enterprises inside government (when non-market), but this has not led yet to any reclassification at the local government level, as the units potentially concerned are very small. Eurostat encouraged the statistical authority to continue to perform regularly the 50% test.

Findings and conclusions

Eurostat encouraged the Hungarian authorities to check the sector classification of units of all general government sub-sectors regularly.

3.1.1. Public infrastructure companies (railway, motorway, transportation companies, airports)

Introduction

Eurostat enquired about the classification of public infrastructure companies, notably about the rail company, in the light of the current privatisation of the freight part, about the motorways and other public transportation companies.

Discussion and methodological analysis

Concerning the *railways*, Eurostat enquired about the details of the railway company restructuring, which was separated in various parts (MÁV Start Zrt is the passenger rail company and MÁV CARGO Zrt is the freight rail company). Eurostat was informed of the current status of these companies. There are difficulties in the availability of financial statements and business plans of these newly created entities and in the fact that the financing arrangement may be subject to further changes. Noting that one could not wait for the October 2009 notification (when a first annual financial statement will be available), Eurostat invited the Hungarian statistical authorities to make a decision on the classification of the passenger company (MÁV-Start) without delay and in any case

before the next EDP notification of October 2008. In order to do so, Eurostat suggested examining, in the absence of a financial statement covering a complete year, any existing business plan if available, and proposed assistance for the analysis. Answering a question raised by the Hungarian statistical authorities, Eurostat indicated that the classification of payments for public service obligations must be analysed in detail according to national accounts rules, and that they cannot be subject to a classification based solely on compliance with European legislation. The Hungarian authorities (MoF) repeated the need for Eurostat guidance on classification of one specific public service obligation, which is regulated by Regulation 1370/2007 of the European Parliament and the Council of 23 October 2007 on public passenger transport services by rail and by road and repealing Council regulations 1191/69 and 1107/70 and formerly by Council regulation 1191/69 of 26 June 1969 on action by Member States concerning the obligations inherent in the concept of a public service in transport by rail, road and inland waterway.

Concerning the freight company, which was just privatised, Eurostat enquired about the recording of transactions. As far as the privatisation proceeds obtained in the context of the disposal of equity of MÁV Cargo is concerned, Eurostat indicated that the rules concerning indirect sale of financial assets must be applied. This entails recording a disposal of equity in government accounts and a subsequent reinvestment into the mother company of MÁV Cargo, and then applying the capital injection test for the latter. In this context, the Hungarian statistical authorities will have to consider any past losses not already covered by recapitalisation actions as well as the existence of genuine expectations of a future sufficient rate of return on investment.

As regards ÁAK, the national *motorway* management company (currently classified in general government) the planned sale of around 25% of its capital was discussed. Eurostat underlined that given that this partial privatisation did not entail forfeiting control of the company by government, it will be without effect on the sector classification of the entity. Because ÁAK is inside government, the Hungarian statistical authorities enquired on how the equity sale proceeds would be recorded. Eurostat recalled that the FAWP has agreed in 2006 on the possibility of equity liabilities of government – admittedly applicable in a few cases only – based on the notion that equity involves being exposed to the risks and rewards arising from the company's performance and provides access to its residual value in case of liquidation, and is not univocally related to the notion of control. This point was also discussed in a draft guidance note on *Classification of holding companies and their subsidiaries in national accounts*. In this context, the proceeds are to be recorded as a disposal of equity assets when drawing the non-consolidated financial accounts, and as an incurrence of an equity liability by government when drawing the consolidated financial accounts.

Concerning the *payments for the use of roads*, Eurostat took note that the vignette for the use of roads is considered as a sale of service in Hungary in application of Eurostat's guidance note released on 7 March 2008. Eurostat also noted that the vignette also covers motorways under PPP contracts where the motorway assets are off government balance sheet. The Hungarian statistical authorities consider that this does not constitute a problem in itself because government is deemed to be purchasing the availability of those "private" motorways (under PPP contracts), instead of having economic ownership of those motorways and of being direct producers of motorway services, and be reselling motorway services to the public at large by way of the vignette. Eurostat took note of the view of the Hungarian statistical authorities and considered that the issue merited some further reflection.

Regarding the *public bus* companies (VOLÁN), Eurostat examined the profit and loss accounts and balance sheets of the companies sent by the Hungarian authorities before the mission. These

companies, even though some of them are loss-making, comply with the 50% test. Eurostat asked the statistical authorities to check their classification regularly. Eurostat also took note of the situation of **Budapest transportation** company, BKV ZRt, and invited the Hungarian authorities to regularly check the 50% rule for this company, as it seemed to be very close to the 50% threshold.

Findings and conclusions

Eurostat found the practice of the Hungarian authorities concerning the classification of public infrastructure units satisfactory and encouraged them to keep on checking these units regularly.

3.1.2. Public utility companies

Introduction

Eurostat enquired about the classification of public utility companies.

Discussion and methodological analysis

Concerning public utility companies, the Hungarian statistical authorities explained that these belong to local governments and their reclassification would have a low impact on the deficit (B.9) in case they were found to be non-market. The Hungarian authorities promised to review these and send more information to Eurostat.

Findings and conclusions

The Hungarian authorities will provide more information on the classification of public utility companies.

3.2. Implementation of accrual principle

3.2.1. Accrual taxes and social contributions

Introduction

Some aspects related to the recording of taxes described in the Hungarian EDP Consolidated inventory of sources and methods were clarified.

Discussion and methodological analysis

Eurostat welcomed the comprehensive information provided in table 1 of the Questionnaire related to EDP tables. However, Eurostat observed that figures in table 1 of the Questionnaire related to EDP do not exactly correspond to figures in EDP tables. The Hungarian authorities confirmed their statement made previously in the clarification of the April 2008 EDP notification that these figures do not correspond because some social security contributions are paid into extra-budgetary funds, to: Labour Market Fund (D.611, D.29), the Research and Technological Innovation Fund (D.214) and the Cultural Fund (D.214).

Findings and conclusions

Eurostat took note of the explanations provided.

3.2.2. Accrual of expenditure – accrual of the 13th month salary

Introduction

The recording of the 13th month salary had been extensively discussed with the Hungarian statistical authorities in the context of previous dialogue visits and the April 2007, October 2007 and April 2008 notifications.

Discussion and methodological analysis

Eurostat took note of the explanation pertaining to the recording of 13th month salaries. Changes in the moment in which the 13th month salary is paid out (delayed to the next year for the 2004 13th month and then brought back to the current year in two steps in 2007 and 2008), have been appropriately corrected so as to enforce the accrual principle. These corrections avoid underestimating the deficit in 2004 and overestimating it in 2007 and 2008. This issue was resolved for the April 2008 notification and Eurostat had no further questions on the recording.

Findings and conclusions

Eurostat accepted the adjustments made for the recording of the 13th month salary.

3.2.3. Calculation of accrual interest

Due to time constraints this issue was not discussed.

3.2.4. Recording of the church compensation

Introduction

The recording of church compensation was briefly discussed during the meeting.

Discussion and methodological analysis

Eurostat thanked the Hungarian authorities for the note describing the church compensation in Hungary. Even though the issue had been extensively discussed with the Hungarian statistical authorities in the context of previous dialogue visits and the April 2007, October 2007 and April 2008 EDP notifications, Eurostat did not completely understand the acceleration process and the related financial arrangements. Therefore, it was agreed that there was room for further discussion on this issue.

Findings and conclusions

Taking into account the complexity of the acceleration process, the national authorities and Eurostat need to further reflect on the issue.

3.3. Recording of specific government transactions

3.3.1. Public Private Partnerships

Introduction

Both methodological and practical issues were discussed concerning the Public Private Partnerships in Hungary. The Hungarian authorities provided to Eurostat before the mission some documentation on how they assess the risks involved in PPPs and the list of ongoing projects.

Discussion and methodological analysis

Eurostat welcomed the detailed description provided on the criteria used in Hungary for risk transfer assessment. During the session, following a first discussion of these criteria used in order to classify PPP contracts on or off government balance sheets, Eurostat indicated its intention to further examine in the coming weeks such criteria, and come back to the Hungarian statistical authorities with questions and remarks. Eurostat underlined that no guaranteed minimum cap on the availability fee can be consistent with a transfer of risks to the private partner, because the latter implies that the non availability of the asset must result in a zero or negative availability fee, a point that was agreed upon by the Hungarian statistical authorities. The statistical authorities welcomed the attempt by Eurostat to clarify certain accounting rules for PPP in the form of a draft guidance note *Assessment of risk transfer in PPP: guarantees, grantor financing and termination clauses*, but felt that the PPP chapter of the MGDD Manual generally needed further clarification. Eurostat will reflect on the proposition of the Hungarian statistical authorities to update the PPP chapter, notably in order to take stock of new developments in PPPs not included in the existing chapter.

A discussion also took place about the criteria relating to early termination of contracts, by analogy with the criteria for availability fees and with the majority financing of a PPP. The Hungarian statistical authorities and Eurostat will further enquire and reflect on the issue.

The Hungarian authorities also explained the procedure relating to PPPs. There is an intra-governmental PPP committee that decides whether a project can be deemed a PPP or not. Afterwards the statistical office receives the contract and provides its opinion on whether the project is on or off balance sheet of the government (and prepares the list to be sent to Eurostat).

As far as PPP projects are concerned, a list of PPP provided to Eurostat was examined. The Hungarian authorities explained that this list (which is also provided in the EDP related questionnaire each notification) shows only those PPPs which are of high value and which are off government balance sheet. Eurostat requested the statistical authorities to provide to Eurostat a copy of the contracts relating to projects no. 26 (ELTE Trefort kerti campus), 39 (Börtön Projekt Szombathely), 40 (M5-ös autópálya Kiskunfélegyháza-Szeged) and 43 (Egységes digitális rádiótávközlési rendszer). Given the high number of PPP projects already classified off government balance sheet (2.5 billion € of total value under contract), the Hungarian statistical authorities were invited to consult Eurostat in writing (for advice), in particularly for contentious or doubtful cases.

Findings and conclusions

Eurostat welcomed the practice of risk assessment applied in case of PPP projects in Hungary. Eurostat might further reflect on the existing practical rules of Hungary. The Hungarian authorities will send the contracts of the four above mentioned PPP projects to Eurostat in the coming weeks.

3.3.2. Capital injections into public corporations, dividends and privatisations

Introduction

The issue of capital injections was discussed briefly during the meeting due to time constraints. The Hungarian authorities provided an updated list of capital injections before the mission.

Discussion and methodological analysis

The Hungarian authorities informed Eurostat that tables Va and Vb of the EDP related questionnaire are not fully consistent and will be corrected in the next EDP notification. According to their explanation, so far in table Vb of the EDP related questionnaire, not only payments to public corporations were recorded but also payments to private ones. However, this was corrected for Eurostat's dialogue visit and will also be corrected for the next notification.

Concerning the capital injections into VOLÁN companies, Eurostat had doubts about the correct recording of capital injections, as it seemed that these companies are loss-making. The statistical authorities explained that the capital injection test is applied appropriately, first by the owners, (local governments that decide to record a subsidy or a capital operation) and later on, is checked as well by the Central Bank, unit by unit (and not as a group). Eurostat accepts this treatment, however it reminded the statistical authorities that if a capital injection is given for a specific investment purpose then it has to be recorded as investment grant (D.92).

As far as the capital injections into forestry companies are concerned (currently recorded as transactions in equity), Eurostat considered that these should be most likely recorded as capital transfers, given the pattern of repetitive payments and also given the fact that these seem to have the nature of investment grants.

Findings and conclusions

The Hungarian authorities will reclassify capital injections in forestry companies and continue to check the capital injection test.

3.3.3. EU flows

Introduction

The Hungarian authorities sent to Eurostat information about the recording of EU flows before the dialogue visit. Eurostat's aim was to clarify whether the Hungarian authorities neutralize the funds received from the EU appropriately.

Discussion and methodological analysis

The Hungarian authorities explained to Eurostat their method for recording EU grants, which in principle is in line with Eurostat's decision on the neutralisation of these flows. Eurostat found a good situation with respect to the source data, which allows Hungary to adhere strictly or very strictly to the Eurostat decision.

The Hungarian authorities explained that the working balance includes both expenditures made on behalf of the EU and money received from the EU for those flows that come from the EU for co-financing national projects (such as the Structural funds and Cohesion Fund (utilized within the framework of national development plans), Schengen Facility, European Agricultural and Rural

Development Fund (utilized within the framework of national rural development plans), Transition Facility, Solidarity and Migration Funds and some minor items where the final beneficiary is a central budgetary organ (e.g. TEN-T)). EU funds distributed on a normative basis (agricultural direct payments and market-related subsidies) and subsidies, which are directly received from the European Commission, are not part of the national budget. The Hungarian authorities also explained that EU advances are not entered into the budget (working balance), but are recorded in a separate Treasury account.

Eurostat took note that the cash flows related to the EU transit via a suspense account and do not immediately enter the working balance. The Hungarian statistical authorities clarified that the transfer from the suspense account to the working balance was made quasi-automatically upon realisation of expenditure (working balance outflow), and that one could not talk of an imputation of revenue. The Hungarian statistical authorities recognized that a delay in transfer could occur, although rare, and particularly when spending is in excess of the EU advance.

In case the transfers coming from the separate account match expenditures of the given period, this leads to a situation where in practice most expenditures are neutralized. There might be occasions, where the account is not credited enough, which leads to an imbalance, which is not corrected, whereas cases of reverse imbalance (excess revenue over expenditures) are neutralized.

Thus, Eurostat underlined that the current method overestimated the deficit due to the fact that receipts received from the EU and entering the working balance, are adjusted downwards when they are higher than the expenditure in a single year, but are never adjusted upwards in the opposite case. Eurostat found this situation highly anomalous and suggested the Hungarian statistical authorities to consider, in the absence of any other detailed information, that the excess of revenue over expenditure in a single year originated from the year before – and to correct the data accordingly. The Hungarian statistical authorities agreed with Eurostat and data from 2004 to 2007 will be amended in this respect in the next EDP notification in the adjustment line of table 2A, implying a reduction in the reported deficit.

Prior to the mission, the Hungarian statistical authorities requested clarification from Eurostat on more difficult cases where (1) the project is not definitively agreed with the EU, (2) the co-financing rate is set in advance but the actual value can vary, or when it can be modified later, (3) the last part of the expenditure must be advanced by the Member State, and (4) irregularities lead to deductions.

- (1) The Hungarian statistical authorities explained that, in case of uncertainty over whether the amount spent is to be reimbursed by the EU, they thought they may not book a revenue until a decision is taken by the EU Commission. In the case of projects of significant size, a specific approval decision has to be taken by the EU, which may occur only after the expenditure is made. The Hungarian statistical authorities wondered about the appropriate time of recording: at the time of decision or at the time of expenditure, and if the latter, whether the data should be revised at the time of decision or be estimated pending decision. Eurostat thought that the spirit of the decision supposed recording a revenue at the time of expenditure and that it would be inappropriate to revise the data: it recommended to make an estimate, based on the reasonable supposition that Hungary had a claim that would, most likely, be reimbursed. Eurostat stressed that the expenditure must be neutralised by booking a corresponding revenue in the same year, and this should be the case even when there are some uncertainties on whether it will be reimbursed, or for what amount. In this case, an assumption must be made (including on the proportion which will be reimbursed by the EU,

with a prudent estimate), and a correction will be recorded when the exact proportion is known. In the specific case of the money spent by Hungary for the construction of motorways and Budapest M4 metro (48 billion HUF), a government revenue from the EU of 32 billion HUF (EU co-financing) should be recorded in 2007 (instead of zero) and accordingly the government deficit for 2007 will have to be revised downwards by this amount in the next notification.

- (2) When the co-financing rate is set in advance but the actual value can vary, or when it can be modified later, Eurostat agreed with the Hungarian statistical authorities' view, that the estimated co-financing rate should be applied instead of the actual one, but exclusively if the co-financing rate is not expected to vary considerably. When the co-financing rate is rather uncertain, the actual co-financing rate observable year by year is to be used.
- (3) Concerning the last part of the expenditure that must be advanced by the Member State, Eurostat saw no specific difficulty as it felt that the general rules are applicable.
- (4) Deductions resulting from irregularities should be booked in the accounts at the moment in which the irregularity is discovered and the decision to implement the deduction is made.

Eurostat noted that EU flows are adequately reflected in financial accounts (EU monies recorded as F.2 of government with a matching payable F.7), and that the data are consistent with the more detailed figures by EU funds provided by the MoF to Eurostat. Eurostat found this recording fully appropriate and remarked that they implied substantial differences compared to a cash approach (notably in 2007).

Findings and conclusions

The Hungarian authorities introduced their method for the adjustment of EU flows, which in principle is in line with Eurostat's decision on the neutralisation of these flows. However, the current adjustment seems to overestimate the deficit, therefore the Hungarian authorities have to adjust EDP tables according to the discussion. The correction will be applied for the October 2008 EDP notification.

3.3.4. Guarantees

Due to time constraints this issue was not discussed.

3.3.5. Military equipment expenditure

Introduction

Eurostat enquired about the recording of military equipment.

Discussion and methodological analysis

Eurostat noted that the Hungarian statistical authorities follow the rules on military expenditures, as they make an explicit adjustment for large deliveries, in the context of the large contract for Gripens, as well as implicitly for other contracts through standard accrual adjustments to calculate intermediate consumption.

Findings and conclusions

Eurostat took note of the explanations and presentation of the Hungarian authorities.

3.3.6. Debt assumption, debt cancellations and debt write-offs

This question was not discussed in detail.

3.3.7. Swap

Introduction

Eurostat enquired about the recording of swaps.

Discussion and methodological analysis

The Hungarian statistical authorities recalled that government was entering into currency swaps, and perhaps in other instruments, with the Central Bank and more recently in the market, in order to hedge its foreign currency debt. In application of the regulation, the Maastricht debt is valued taking into account the exchange rate observable at time of hedge. The impact of the hedge increases the reported Maastricht debt by 138 billion forint as of end December 2007 (0.5% of GDP).

Findings and conclusions

Eurostat concluded that the valuation of the debt followed the rules, valuing the government debt after swap.

3.3.8. Others: Sale and leaseback operations, securitisation, UMTS, carbon trading rights

This question was not discussed in detail.

Annex me: List of participants

	<i>Name</i>	<i>Institution</i>	
1.	<i>Maria-Helena Figueira</i>	<i>Eurostat</i>	<i>Acting Director – Directorate National and European Accounts</i>
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