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Directorate D: Government Finance Statistics (GFS)
Unit D-2: Excessive Deficit Procedure I



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FINAL FINDINGS

EDP dialogue visit to Estonia

4 – 5 July 2011

Executive summary

An EDP dialogue visit to Estonia took place on 4-5 July 2011.

Eurostat carried out this EDP dialogue visit with the aim to analyse the April 2011 EDP notification, to review the sector classification procedures, 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 Estonian 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. Eurostat took note of the current organisation framework for EDP purposes involving the NSI, the MoF and the NCB, welcomed the good cooperation between these institutions and recommended the NSI to formalise their co-operation by signing a Memorandum of understanding with the MoF.

Second, Eurostat appreciated that all action points resulting from the June 2009 EDP dialogue visit were completed on time.

Further, Eurostat enquired about the new centralised data source, providing accrual data. This system had been discussed at the previous EDP dialogue visit and started to be operational as of 2010.

Concerning the classification of units, Eurostat concluded that so-called 50 % test is to be undertaken more frequently. Eurostat recommended the Estonian statistical authorities to look at both, the results of the 50% market / nonmarket test, as well as the legal form and the involvement of government, when deciding about the sector classification of a unit.

As regards the time of recording of the VAT in years 2009-2010, in particular with respect to an exceptional event of a strengthened control of the VAT reimbursements, Eurostat recalled that this kind of events should be reflected in the calculations and time series should be adjusted accordingly, in order to get the real picture on the tax receipts. Eurostat asked the Estonian statistical authorities to correct their existing VAT accrual data for 2009 and 2010.

Eurostat took note of the recording of debt cancellations and debt assumptions as well as of the recording of purchases of military equipment and of the EU funds. Eurostat reminded the rules on the recording of capital injections set up by the MGDD. The Estonian statistical authorities acknowledged that the superdividend test has been undertaken on a regular basis. The non existence of securitisation and sale and lease back operations was noted as well. The Estonian statistical authorities will correct swaps for the amounts relating to the students loans, which have been incorrectly included in the figures for swaps. Eurostat was also informed about the treatment of the sale of emission permits which took place in 2010. The Estonian statistical authorities will correct presentational mistakes in the Questionnaire relating to the EDP tables, in particular in Tables relating to accrual interest, military expenditure and debt cancellations.

Eurostat will study the two discussed PPP contracts under preparation: 1) the construction of Tallin prison and 2) the Kose – Mao section of the Tallin – Tartu – Luhamaa highway (E263). The Estonian statistical authorities will keep Eurostat informed about the developments

relating to both projects¹.

Eurostat very much appreciated the openness and transparency demonstrated by the Estonian statistical authorities during the meeting and the documentation provided prior to the visit.

¹ Eurostat and the Estonian statistical authorities finalised the issue in August 2011.

Final Findings

Introduction

In accordance with article 11(1) of Council Regulation (EC) No 479/2009 as regards the quality of statistical data in the context of the Excessive Deficit Procedure, Eurostat carried out an EDP dialogue visit to Estonia 4 – 5 July 2011.

The delegation of Eurostat was headed by Mr. François Lequiller, Director of Eurostat Directorate C – National accounts. The Directorate General for Economic and Financial Affairs (DG ECFIN) and the European Central Bank (ECB) also participated in the meeting as observers. The Estonian authorities were represented by the Statistical Office (NSI), the Ministry of Finance (MoF) and the National Central Bank (NCB). In addition representatives from other institutions were present for particular issues.

Eurostat carried out this EDP dialogue visit in order to review the implementation of ESA95 methodology and to assure that provisions of the ESA95 Eurostat Manual on Government Deficit and Debt and Eurostat decisions are duly implemented in the Estonian EDP and Government Finance Statistics (GFS) data.

In detail, the main aims of the dialogue visit were: to discuss the new centralised system of data collection based on accrual accounting, to review the existing practices in general government sectorisation and recording of specific government operations, to discuss issues concerning the recording of taxes and social contributions and to analyse two PPP projects under preparation.

In relation to procedural arrangements, Eurostat explained the procedure, in accordance with article 13 of Regulation No 479/2009, indicating that within days the Main conclusions and action points would be sent to the Estonian statistical authorities, who may provide comments. Within weeks, the Provisional findings would be sent to the Estonian statistical authorities in draft form for their review. After amendments, Final findings will be sent to the Economic and Financial Committee (EFC) and published on the website of Eurostat.

Eurostat very much appreciated the openness and transparency demonstrated by the Estonian authorities during the meeting and the documentation provided prior to the visit.

The following are the main conclusions and action points resulting from the meeting:

0. Eurostat thanked the Estonian statistical authorities for the cooperation demonstrated during the meeting and for the information provided prior to and during the EDP visit.

1. Statistical capacity issues

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

Introduction

The NSI is responsible for the compilation of EDP tables for years T-4, T-3, T-2 and T-1; the MoF is in charge of the planned data for year T. The MoF is the owner and provider of the main data source – "Public sector Financial Statements` information system" (PSFSIS).

The co-operation between the institutions is not formalised by any Memorandum of understanding; only a memorandum on transmission of data between the NSI and MoF has been signed. Ad hoc meetings are organised between the MoF and the NSI and more regular meetings are organised between the NSI and the NCB.

Discussion and methodological analysis

The NSI informed Eurostat that a Memorandum of understanding will be signed between the NSI and NCB in a short future. No signature of such a Memorandum is planned between the NSI and MoF. Nevertheless, the NSI representatives consider the co-operation between these two institutions as good.

Findings and conclusions

1. Eurostat welcomed the forthcoming signature of a Memorandum of understanding between the NSI and the NCB and encouraged the MoF to also sign a similar document with the NSI, as the MoF is the main supplier of data to the NSI for EDP purposes. (*Deadline: as soon as possible*)

1.2 Data sources, compilation practices

Introduction

As described in the documentation to this point provided by the NSI prior to this visit, the main data source for the compilation of the EDP tables and other GFS statistics is the PSFSIS. For calculation of accrual taxes, data from the Estonian Tax and Customs Board is the source; for calculation of interest on tax liabilities the State budget revenue report is used.

Discussion and methodological analysis

The PSFSIS had been already partly discussed during the 2009 EDP dialogue visit, but at that time the System was not yet in place.

The Estonian statistical authorities explained that this is an online system, directly accessible to the NSI, providing detailed accrual data for general government on a monthly and on a quarterly basis for the public sector.

Eurostat wanted to know whether it is possible to reconcile the accrual data from the system with the underlying cash data. The Estonian statistical authorities admitted that it is not easy to do so, as the cash data are more aggregated.

Findings and conclusions

2. Eurostat took note that the NSI is now using direct accrual data sources for the compilation of EDP and other government finance statistics. Eurostat invited the NSI to participate in the first meeting of the working group on quality management (November 2011) and to present its experience in using this kind of data source for the compilation of EDP and relating statistics.

2. Methodological issues and recording of specific government transactions

2.1 Delimitation of general government

Introduction

According to the note provided by the NSI prior to the visit, the NSI is responsible for the sector classification of newly established units. There is also a list of government units managed by the MoF and the goal is that these two lists should be identical.

Discussion and methodological analysis

The list of units classified in general government is published on the NSI website. This list is regularly (twice a year) reviewed and consultations on this matter take place with the NCB and the MoF. The NSI representatives explained that a general reclassification of units is undertaken within the process of major revisions of national accounts (every 5 years). If a major revision is necessary during the five years period, then units are reclassified in the framework of that revision.

Eurostat found the period of five years too long and stressed that the 50% test fulfilment should be examined more often. Eurostat also reminded that the subsidies on production should not be included in the calculation of the sales of units.

The Estonian statistical authorities asked Eurostat about its opinion on the classification of some units (the list of units had been provided prior to the visit). In general these units were local government enterprises providing services "of common interest" (water management, waste collection and similar). The NSI explained that, in the past, these enterprises were classified as a group, by default, outside general government (the result of the 50% test was not taken into account).

Eurostat recalled that, when deciding on the classification of a unit, both "quantitative" (the results of the 50% test) as "qualitative" (type of activity, legal form, and involvement of government) criteria have to be taken into account.

Findings and conclusions

3. The NSI will undertake the market / nonmarket test on a regular basis, not exceeding 3 years, and on an annual basis for large units. *Deadline: Continuous*

4. The NSI will re-run the market / nonmarket test according to ESA 95 rules on a unit by unit basis, subtracting subsidies on production from market sales and excluding net interest from both sales and costs. A table with the actual results of the test, showing also the level of the debt for individual entities, will be sent to Eurostat. *Deadline: 31 August 2011²*

5. As far as the issue of classification of units according to ESA2010 is concerned, the NSI will perform also in future the market / nonmarket test for all individual units and not on the basis of NACE groups, for those companies which are owned by government and have been classified in S.11. The results of the first of such tests in terms of ESA 2010 will be sent to Eurostat. *Deadline: Continuous (for the results of the test: 31 August 2011)*

2.2 Compilation practices

2.2.1 Accrual taxes and social contributions

Introduction

The Estonian statistical authorities reported, in the Questionnaire on the recording taxes and social contributions, that they use time adjusted cash (adjusted by 1 month).

The issue of possible misreporting of receivables from taxes (VAT) for 2009 and 2010 had come to the attention of Eurostat early in 2011. First views were exchanged between Eurostat and the Estonian statistical authorities by letters before the April 2011 EDP notification. The discussion continued during the April 2011 EDP notification assessment and during the EDP dialogue visit.

Discussion and methodological analysis

With respect to the abovementioned risks, Eurostat enquired in particular about the following three issues:

- 1) the time of recording of returns by government of overpaid VAT to taxpayers
- 2) the time of recording of the amounts to be returned by government to taxpayers for wrongly collected interest and overdue charges for delayed tax payments
- 3) the recording of revenue relating to the change in the VAT rate

After the explanations provided by the NSI, it seemed that the issues 2) and 3) would not be a possible cause of misreporting. The issue 1) (time of recording of returns of overpaid VAT by government to taxpayers), on the contrary, needed a more detailed examination.

The NSI confirmed that Estonia uses the time adjusted cash method with a time lag of one month for the recording of the VAT receipts. Due to reinforced control of the VAT

² The Action point was completed on 31 August 2011.

declarations in January 2010, VAT reimbursements relating to the 2009 VAT collection had been delayed and paid only in February 2010, which lowered the amount of government expenditure in 2009 in connection to VAT reimbursements. At the request of Eurostat, the NSI provided monthly data on VAT collection and reimbursements for the years 2008-2010 (both in EEK and euro). Eurostat stressed that an exceptional event (such as reinforced VAT control and consequent postponement of the reimbursements) should have been reflected in the calculations of the tax receipts in order to get the real figures of accrual receipts in the concerned years (in this case 2009 and 2010).

Findings and conclusions

6. The strengthened control of requests for the VAT reimbursements for the month of January 2010, led to a postponement of these reimbursements into the month of February 2010. As the VAT tax receipts are calculated on a time adjusted cash basis (with a lag of one month), consequently, the ESA95 government revenue for 2009 was inappropriately inflated. The NSI will provide to Eurostat the figures on VAT gross receipts and reimbursements, as well as on VAT controls, on a monthly basis, for the period from 2006 onwards. The NSI will provide an explanatory note on this issue to Eurostat. *Deadline: 31 August 2011*³

2.2.2 Calculation of accrual interest, consolidated interest

Introduction

The Estonian statistical authorities had sent a short note on the calculation of accrued interest prior to the visit. The data source already used accrued data.

Discussion and methodological analysis

The NSI confirmed that the data source for reporting of interest is on an accrual basis. Eurostat enquired about the content of the line "Difference between interest paid and accrued" in EDP Table 2A. The Estonian statistical authorities explained that the line contains only interest on swaps, while data on accrued interest are reported in the line "Other adjustments" (Accrual adjustments and adjustments in intra-sector transactions), which is not correct. The same misinterpretation of this line applied also for EDP Table 2C. Although this mistake had no impact on the level of the deficit, Eurostat asked nevertheless the Estonian statistical authorities to correct it and to report accrual interest in the appropriate line.

The mistake in EDP table 2C was of a different nature, as the line "Other financial transactions" contained information on holding gains as well as on accrual interest. This should be corrected and only holding gains should be shown under "Other financial transactions".

Findings and conclusions

7. The NSI will correct the line "Difference between interest paid and accrued" in EDP tables 2A and 2C. This line, until now, has been used only in order to account for

³ The Action point was completed on 31 August 2011. The accrual figures on VAT for 2009 and 2010 were changed for the October 2011 EDP notification.

interest from swap transactions, while it should report on interest in general. *Deadline: October 2011 EDP notification*

8. The NSI will only correct the effects of revaluation of social security financial assets in EDP table 2D and will not include any correction of interest. *Deadline: October 2011 EDP notification*⁴

2.3 Recording of specific government transactions

2.3.1 EU flows

Introduction

The previous Eurostat EDP dialogue visit concluded that the rules on the recording EU flows seemed to be followed by the Estonian statistical authorities.

Discussion

The Estonian statistical authorities explained that the EU funds flow from the European Commission through the Ministry of Finance and implementation agencies to the final beneficiary. All the agencies (except one) are classified in general government sector. The receipts of these funds are recorded at the time of their expenditure, which is in line with the national accounts rules. The Estonian statistical authorities excluded the possibility of any double counting. They explained that all the money received are well tracked, also thanks to the PSFSIS.

Findings and conclusions

9. Eurostat took note of these arrangements.

2.3.2 Military equipment expenditures

Introduction

According to the qualitative information provided in the Questionnaire related to EDP notification tables, accrual data is used for the recording of military equipment in national accounts. Sometimes military equipment contracts include late payments or prepayments (with cash payments within one year). No financial lease exists and no equipment is built over a period of several years.

Discussion

When comparing data reported in the EDP tables and in the EDP Questionnaire, Eurostat spotted an inconsistency in the tables of the Questionnaire as compared to the EDP reporting, where other accounts receivable were reported instead of other accounts payable (other accounts payable were correctly reported in the EDP notifications).

Findings and conclusions

⁴ The Action point was completed for the October 2011 EDP notification.

10. The NSI will correct tables 7.1⁵ and 4⁶ of the EDP relating questionnaire, as amounts reported for military expenditures under other accounts receivables are, in reality, other accounts payable. *Deadline: October 2011 EDP notification*⁷

2.3.3 Guarantees

Introduction

No guarantees have been called in the period of 2006-2010. According to the note from the NSI provided prior to the visit, all guaranteed debt is repaid according to the contracts.

The issue of export guarantees was also discussed.

Discussion

The Estonian statistical authorities confirmed that no guarantees have been called in recent years. There has been no debt assumption or write-off relating to guarantees provided by general government.

The export insurance system is managed by the KredEx Fund and by the KredEx Credit Insurance. Guarantees represent only a small part of the Fund activities. Both institutions are 100% owned by government; they are both classified outside the government sector.

In 2009 the government provided a loan to the Fund (51,1 mill euro) and a capital injection recorded as equity acquisition to KredEx Insurance. Both operations are reported in the Questionnaire relating to the EDP notification tables. The Estonian statistical authorities informed Eurostat that the activities of both KredEx institutions are monitored on a continuous basis.

Findings and conclusions

11. Eurostat took note of this situation.

2.3.4 Debt assumptions, debt cancellations, debt write-offs and foreign claims

Introduction

The NSI provided a table on government claims for 2006-2010 for all general government, including information on the ten most significant debtors for each year. There have been no debt assumptions, debt cancellations or debt write-offs in 2006-2010.

Discussion

The Estonian statistical authorities confirmed that there have been no debt assumptions, debt cancellations or debt write-offs in recent years. Eurostat analysed the data reported in Table 8 of the Questionnaire relating to the EDP notification tables.

⁵ Military equipment expenditure

⁶ Breakdown of other accounts receivable / payable (F.7) of general government

⁷ The Action point was completed for the October 2011 EDP notification.

The figures provided in the table slightly differed from the figures reported in the Questionnaire relating to EDP Tables. The NSI promised to investigate these differences. The NSI recalled that the significant increase in the stock of claims in 2009 is due to the loan provided to KredEx (see the section 2.3.3).

The figure reported under foreign claims appeared to be a claim of the Estonian Agricultural Registers and Information board (PRIA) towards the EU, for intervention purchases. Eurostat had doubts on whether this claim should be reported as a foreign claim. The NSI explained that considering the special character of this claim, this might not even be reported as a loan but rather reclassified as F.79. Eurostat would need more details in order to decide on the appropriate classification.

Findings and conclusions

12. The NSI will check why the closing balance of the stock of government claims towards public corporations at the end of 2009, as presented in the table provided prior to the visit, does not correspond to the starting balance of the same stock at the beginning of 2010. The NSI will provide a corrected table. *Deadline: October 2011 EDP notification*⁸

13. The NSI will report in the table 8⁹ of the EDP relating Questionnaire (part on foreign claims) only claims to third countries. The NSI and Eurostat will investigate whether a claim of PRIA towards the EU has more the nature of a loan or of other accounts receivable. The NSI will send a note to Eurostat on the issue. *Deadline: 31 August 2011*

2.3.5 Capital injections in public corporations, dividends, privatization

Capital injections

Introduction

The Estonian statistical authorities provided a document about the assessment and treatment of the capital injections provided to the public corporations by general government and a list of capital injections provided in 2006-2010.

Discussion

As a general rule, capital injections in foundations and non-profit organisations are treated in Estonia as investment grants (D.92). In the case of corporations, the economic results for the last three years are analysed in order to decide about the treatment of a capital injection. If a corporation reported losses in three previous years, then the injection is recorded as an investment grant (D.92). The same would apply if a profit is reported in one year and losses in other years. If profits are reported in all investigated years, then a financial transaction (F.5) is recorded. In the case of newly created companies of small size, capital injections in these are automatically treated as financial transactions and are again examined after three years of existence of a company, taking into account its economic results. In case of new big

⁸ The Action point was completed for the October 2011 EDP notification

⁹ Central government claims, debt cancellation

companies (own funds of at least 1 mio eur), capital injections are examined and their treatment decided already at inception.

Eurostat recalled that the analysis of capital injections provided to corporations by general government has to be more thorough. The treatment of a capital injection should be decided on a case by case basis, following the rules established in the MGDD (chapter III.2).

Eurostat also reviewed the table on the treatment of capital injections provided in 2006-2010. The largest capital injection treated as a financial transaction was provided in 2009 to KredEx (Insurance) and the largest capital injection treated as a non-financial transaction was provided to Estonian Air in 2010.

Findings and conclusions

14. Eurostat recalled that rules on capital injections, as set up by the MGDD, had to be applied. When deciding on whether a capital injection is a financial or non-financial transaction, analysis of past profits and losses of the entity in question, as well as future profitability, should be analysed. *Deadline: On a continuous basis*

Dividends

Introduction

A short note on the treatment of dividends in general was provided prior to the visit. The previous EDP dialogue visit concluded that the superdividend test should be undertaken on a regular basis.

Discussion

Dividends and superdividends are recorded according to the ESA95 rules – as non financial transactions (D.42) in the case of a dividend and as financial transactions (F.51) in case the amount received is considered to be a superdividend. The NSI explained that the superdividend test has been done since 2010 regularly, using operating results of the previous year.

Eurostat also reviewed the table on dividends received in 2006-2010 and their treatment. Superdividends were mainly reported in 2009.

Findings and conclusions

15. Eurostat took note of this treatment.

Privatisation

Introduction

The figures on privatisation receipts reported in the table provided prior to the visit showed that they were rather minor. A significant sale of shares was reported for the year 2009.

Discussion

The NSI confirmed these figures and explained that the significant figure reported for 2009 (223.8 mill eur) relates to the privatisation of Telekom AS.

Findings and conclusion

16. Eurostat took note of this situation.

2.3.6 Public Private Partnerships

Introduction

The Estonian statistical authorities had sent their analysis and their opinion on the treatment in national accounts of two PPP contracts prior to the visit: 1) the construction of Tallin prison and 2) the Kose – Mao section of the Tallin – Tartu – Luhamaa highway (E263). It should be pointed out that both contracts were still under preparation and not signed yet.

Discussion

Eurostat recalled the rules on treatment of PPP contracts set by the MGDD. Eurostat further analysed both projects (not signed yet) in particular with respect to the bearer of the risks: availability, construction and demand risks. All these three risks seemed to be on the side of the private partner in both cases. No guarantee from government was foreseen for any of the two projects.

At that stage Eurostat could only provide a preliminary view and needed further information in particular with respect to the risk bearing as well as with respect to termination clauses and other aspects.

Findings and conclusions

17. The Estonian statistical authorities will send to Eurostat the amended versions of the PPP contracts concerning the Tallinn prison and the construction of road E263, taking into account the various comments and requests for further information of Eurostat, pointed out during the meeting. Eurostat will then provide its view on these amended versions of the contracts. *Deadline: As soon as possible*¹⁰

2.3.7 Derivatives: swap cancellations, off-market swaps, options

Introduction

Interest rate swaps are used by central government and local government, while social security funds use forward rate agreements. The NSI provided a short note containing a table with figures for 2007-2010. The debt of government is mostly in euro.

No swap cancellations, off-market swaps or options exist.

Discussion

¹⁰ The Action point was completed in August 2011.

Eurostat discussed interest rate swaps used by central government in order to cover the risks related to the student loans. There is no swap agreement in case of these low interest rate loans, therefore they are not real swaps and should not be treated as such.

Eurostat also spotted a presentational mistake in the reporting of swaps in EDP Table 3D. This will be corrected for the October 2011 EDP notification.

Findings and conclusions

18. The NSI will exclude from swaps in EDP tables, amounts provided to banks to subsidise student loans. Data for years 2007 and 2008 will be corrected by those amounts. Data for years 2009 and 2010 will also be checked and corrected if necessary. *Deadline: October 2011 EDP notification*¹¹

19. Eurostat took note that there are no off market swaps and swap cancellations in Estonia, undertaken by government. The NSI will correct the sign of the amounts of interest under swaps in EDP table 3D. *Deadline: October 2011 EDP notification*¹²

2.3.8 Other: Carbon trading rights

Introduction

A sale of Assigned Amount Units took place in 2010. This was recorded as a sale of non produced assets.

Discussion

Eurostat reminded that the receipts from such a sale should be recorded as a separate operation and not when they are used as expenditure for environmental projects. These are two separated events and there should not be, as for the treatment, any similarity with the recording of the EU flows. The Estonian statistical authorities confirmed that they followed the recommendations of Eurostat. The receipts from the sale of emission permits are recorded as a sale of nonproduced assets.

Findings and conclusions

20. Eurostat took note of the treatment.

¹¹ The Action point was completed for the October 2011 EDP notification.

¹² The Action point was completed for the October 2011 EDP notification.

Annex: List of participants

Eurostat:

Mr François Lequiller, Director of Eurostat Directorate C – National accounts
Mr Luca Ascoli, Head of Unit C3 – Statistics for Excessive deficit procedure
Mr Denis Besnard, Unit C3
Ms Ivana Jablonska, Unit C3 – Desk officer for Estonia

DG ECFIN:

Ms Ingrid Tomming – Desk officer for Estonia

ECB:

Ms Linda Kezber - Economist

Statistics Estonia:

Ms Agnes Naarits, Head of National, Financial and Environmental Accounts Department (NFEAD)
Ms Elo Parveots, Leading Statistician, NFEAD
Mr Mikk Medijainen, Leading Statistician, NFEAD
Ms Anastassia Toming, Statistician, NFEAD
Ms Anu Lill, Leading Statistician, NFEAD

Ministry of Finance:

Mr Sven Kirsipuu, Councillor, Public Finance and Strategies Department
Ms Juta Maar, State Accountant General, State Accounting Department

Bank of Estonia:

Ms Reet Kirt, Deputy Head, Balance of Payments and Economic Statistics Department
Ms Sünne Korasteljov, Economist, Balance of Payments and Economic Statistics Department

Tax and Customs Board:

Ms Monika Jõesaar, Deputy Head, Department of Control

Representatives for the PPP-projects (Observers):

Ms Piia Kallas, Finance Director, State Real Estate Company Ltd
Mr Teet Tender, PriceWaterhouseCoopers Advisors Ltd
Mr Olavi Grünvald, PricewaterhouseCoopers Advisors