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Directorate D: Government Finance Statistics (GFS) and quality
**Unit D-2: Excessive deficit procedure (EDP) 1**

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# FINAL FINDINGS

# <u>EDP dialogue visit to Estonia</u>

## 7-8 September 2017

# Executive Summary

Eurostat carried out an EDP dialogue visit to Estonia on 7 and 8 September 2017. The purpose of the visit was to review institutional responsibilities in the field of government finance statistics (GFS) including EDP reporting and data sources for the EDP data compilation. In addition, Eurostat also reviewed the implementation of the ESA2010 methodology, in particular for the delimitation of general government as well as in the recording of specific government transactions and the application of the accrual principle.

First, the institutional arrangements currently in place were reviewed. There have been no substantial changes and inter-institutional cooperation has not been further formalised with the exception of the cooperation with the Bank of Estonia. Eurostat was informed that in the future, rather than memorandum of understanding, service level agreements may be used to formalise existing cooperation practices. Besides institutional cooperation, the risks associated with the relatively small size of the EDP dedicated team were discussed.

Following the discussion of technical matters, Eurostat invited SE to update the current EDP inventory in view of the changes observed in Estonia and the impact of some ex-ante technical advice provided by Eurostat. A major point discussed was the adoption of an accrual working balance by the government from 2017. Eurostat encouraged SE to study the practical implications and to share this assessment with Eurostat before the first submission of 2017 EDP data in the April 2018 notification period.

Following the 2015 dialogue visit, Eurostat and SE discussed the sector classification of some units. Particular attention was paid to the classification of public units in liquidation, inactive and start-up companies. For Estonian Air, Eurostat enquired about the classification of the company outside general government despite being in liquidation since 2015. SE confirmed that the company will be reclassified to S.13 in the next report to Eurostat. The sector classification of Nordic Aviation Group AS (Nordica) and OÜ Transpordi Varahaldus was also addressed. Eurostat invited SE to analyse the sector classification of an insurance company, in view of the advice given in the past as regards the classification of its parent entity, KredEx Fund.

Standard items of EDP dialogue visits were also discussed. Among these, the participants discussed the statistical impact of the new taxes the government aims to adopt. The participants found that the road tax was particularly challenging as it was too early to know how the tax will be implemented and therefore which should be its statistical treatment.

Eurostat thanked the Estonian statistical authorities for the co-operation prior and during the mission.

# 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 (EDP), Eurostat carried out an EDP dialogue visit to Estonia on 7 and 8 September 2017.

The delegation of Eurostat was headed by Ms. Lena Frej Ohlsson, Head of the Excessive Deficit Procedure I Unit. Eurostat was also represented by Mr Luca Ascoli, Ms Camelia Jüttner and Mr Francisco de Miguel. The Estonian authorities were represented by Statistics Estonia (SE), the Shared Service Centre (SSSC) and the National Central Bank (Eesti Pank). Representatives of the DG ECFIN and the European Central Bank (ECB) also participated in the meeting as observers.

The previous Eurostat EDP dialogue visit to Estonia took place on 20 and 21 January 2015.

Eurostat carried out this EDP dialogue visit in order to review institutional responsibilities in the field of government finance statistics (GFS) including EDP reporting and data sources for the EDP data compilation. In addition, Eurostat also reviewed the implementation of the ESA2010 methodology, in particular for the delimitation of general government as well as for the recording of specific government transactions and the application of the accrual principle.

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 for comments to SE. Within months, the provisional findings would be sent in draft form for review. After amendments, the final findings will be sent to the Economic and Financial Committee (EFC) and published on the website of Eurostat.

Eurostat appreciated the information provided by the Estonian statistical authorities prior to the EDP dialogue visit. Eurostat also thanked the Estonian statistical authorities for the co-operation shown during the mission and consider that the discussions were transparent and constructive.

## 1. Statistical capacity issues

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

*Introduction*

The EDP tables are reported by Statistics Estonia (SE), which compiles government financial statistics (GFS) according to the rules of European System of Accounts (ESA). SE compiles non-financial and financial accounts, Maastricht debt and the corresponding ESA2010 transmission tables. The Ministry of Finance (MoF) only provides forecast data (planned data for year T). Bank of Estonia (BE) does not currently provide any data.

GFS is compiled by four leading statisticians and one leading statistician-methodologist; the group reports to the Deputy Head of Department on macroeconomic statistics. Two experts in the group are specialised on EDP issues and are also compiling both the annual and quarterly general government financial and non-financial accounts, using in part input from other statisticians.

There are two main data sources used for the compilation of the government sector accounts:

- Accrual accounting information collected by the State Shared Services Centre (SSSC), which is the government agency in the governing area of MoF (until year 2013 the information was collected directly by MoF).
- The tax revenue report prepared by the tax authority.

*Discussion and methodological analysis*

Statistics Estonia made the presentation on the recent developments. SE explained the interest of the government to develop the use of service level agreements as the preferred mechanism of interinstitutional cooperation and discussed staff allocation. SE noted that even if more funding is obtained in 2018 for SE, the increase will also entail new activities and therefore a possible staff increase in the GFS team (in the government finance and EDP statistics team) would depend on the reallocation of current staff rather than in obtaining new resources.

Eurostat expressed its concern about the relatively small size of the GFS team. SE confirmed that there are no immediate plans to recruit more staff and that the priority is currently the training of the two new staff that joined the team in 2016[1]. SE also confirmed that it does not expect any other staff departure from the GFS team.

Eurostat insisted that the GFS team is objectively small and reminded SE of the possibility of using the courses offered in the European Statistical Training System programme to train newcomers into EDP issues. Eurostat also noted that the small team size encompasses continuity risks and that the situation may not be sustainable in the long run. Thus, it recommended SE to review the staff allocation to GFS statistics in any future workload assessment.

Eurostat also asked about cooperation with the SSSC/MoF and with BE. SE confirmed that there is effective cooperation with these bodies. Cooperation is mostly based on personal contacts between specialists. Complicated methodological cases are thoroughly discussed

[1] Two out of four leading statisticians from the GFS team left in June 2016. One of them was specialised on EDP issues, namely the debt statistics, the other was compiling taxes and transfers.

with the Head of State Accounting Department and ad-hoc meetings are organised when needed.

SE confirmed that it signed a Memorandum of Understanding with BE on 1 February 2017 (action point 1 of the 2015 EDP dialogue visit). The purpose of this agreement was to change the workflow for the compilation of annual financial accounts (AFA). According to it, from 2018 onwards the main data compiler will be BE (BE was compiling the quarterly data and under the agreement it will also compile the annual data). This memorandum will be applicable from September 2017. A joint team BE/SE will validate the national accounts and should also address methodological differences (minutes of validation meetings are available). The new working arrangements require enhanced coordination and that both entities respect the deadlines. SE holds annual meetings with BE, usually in late autumn, to discuss common issues in the statistical domains like balance of payments, foreign trade, financial and national accounts.

Given the government's policy to develop the use of service level agreements, SE considers that it is not feasible to formalise the cooperation with the SSSC and with the MoF through memoranda of understanding. Instead, SE considers that it should be ready to negotiate and sign service level agreements with these bodies once the practice is generalised.

Eurostat enquired about cooperation with other bodies such as the Estonian Court of Audit or the Fiscal Council. SE confirmed that there is exchange of information with the Estonian Court of Audit, notably through annual meetings, to discuss issues of common interest, although there is not a formal agreement between the two to do so. As regards the Fiscal Council, SE does not cooperate with it in a regular manner. SE does not consider it necessary to establish a formal and regular cooperation with it at this moment.

*Findings and conclusions*

*Action Point 1: SE will send Eurostat the recently signed memorandum of understanding on statistics between SE and the Bank of Estonia. Deadline: September 2017*[2].

### 1.2. Data sources and revision policy, EDP inventory

*Introduction*

The Estonian public sector follows accounting principles which are fully accrual based and consistent with International Public Sector Accounting Standards (IPSAS). The MoF has the authority to establish the accounting principles applicable to all institutions of the Estonian public sector.

The MoF uses the Public Sector Financial Statements (PSFS) for recording all transactions of S.13 accounts, except for the majority of taxes and interest on tax liabilities.

Prior to the visit, SE had provided a note on the consolidation process (in particular on the impact of the preference given to amounts declared by S.1314). There have been small differences detected during the consolidation and the effect of the priority given to S.1314 was negligible (annual differences between S.1314 and counterpart information about stocks for last five years are well below 0.3 million euros).

[2] Action Point completed on 29 September 2017

*Discussion and methodological analysis*

Eurostat invited SE to update the current inventory which was published in 2015 after adapting the previous version to ESA 2010. Eurostat noted that some of the references included in the 2015 version are no longer applicable. Notably, the current text has not been adapted to reflect Eurostat's advice as regards the accounting of euro coins, it does not make reference to the consolidated cash flow management (see centralised treasury subsection), it refers to the ongoing implementation of PSFS (which should be finished by now) and omits the reclassification of some units following the bankruptcy of Estonian Air, among others[3].

As a follow-up of the 2015 EDP dialogue visit, SE confirmed that its systems are now fully adapted to exploit the potential of PSFS as a source of data and that, at the moment, no further developments are deemed to be necessary.

As regards quarterly financial accounts, SE described the validation process and confirmed that there are automated controls for the validation of quarterly data produced by the BE. However, the controls for the annual financial accounts have not yet been formalised. SE and BE meet after each compilation of quarterly reports. In addition, Statistics Estonia explained that there are some changes in the compilation of financial accounts due to the fact that the BE is more involved in the production of financial quarterly accounts as well as annual financial accounts starting with September 2017.

Eurostat enquired about the timing of the audit of the Consolidated Annual Report of the State. SE confirmed that the audited version of the report is available on time for the October notification (this year the audited version was available by the end of May), even though in the inventory it is stated that the October notification is prepared with the version presented to be audited. SE agreed to update the reference to the timing of the audit in the next version of the EDP inventory.

In addition, SE and Eurostat discussed the implications of the adoption of an accrual based budget by the State from 1 January 2017. This would have an impact on the April 2018 notification, as data for the period 2014-2016 will be based on a cash working balance, while data for 2017 will be based on an accrual based working balance. SE has already identified three main concerns: taxes (currently reported using time-adjusted cash), EU grants and other units (e.g. foundations). In addition some adjustments will not be necessary anymore, for example for military expenditure.

SE announced that it was analysing all implications and that it will share with Eurostat its assessment before the April 2018 notification.

As regards the local sector, SE confirmed that the current process of reducing the number of municipalities in Estonia is not expected to have any impact on the quality of data, as all municipalities already follow the same accounting principles. In particular, SE indicated that this would not change their accounting and therefore no changes in reporting, affecting debt and deficit figures, are foreseen. There is a possible effect on the COFOG statistics[4], as the level of detail by government functions might be affected by larger reporting units.

Eurostat enquired on why the EDP Table 2C indicates that the working balance used for the local government sub-sector is drawn from the mixed-based aggregated local government

[3] The subsection on EU structural funds can also be updated to the MFF 2014-2020 terminology.
[4] COFOG is the acronym of Classification of the Functions of Government.

budget execution reports if all municipalities follow same accounting principles. SE explained that the reason is that this aggregated report is compiled by the MoF based on the budgetary reports presented by local governments and that these reports are mixed, as some are cash based while others are accrual based. SE explained that this situation is considered to be temporary, as the national law requires all municipalities to adopt accrual based budget within two years of the State doing so. SE will closely monitor the adoption of accrual based budget by local government.

As regards compliance with the reporting requirements of Council Directive 2011/85, Eurostat noted that the nationally published data are very detailed and transparent. Nevertheless, there are differences between the data published at national and European level, which could raise questions from users. SE agreed to make further steps to converge the two sets of data using a methodology at national level similar to the one applied by Eurostat. Therefore, the MoF will change the reporting of guarantees based on the methodology agreed by Eurostat with the Member States. In addition, Eurostat also highlighted that the amounts of liabilities for public corporations published at national level is very different from what Eurostat is publishing. This is due to the fact that the data at national level include all the liabilities included in the financial report of the corporation while Eurostat is publishing only the Maastricht liabilities. Differences for the treatment of PPPs will remain and thus, Eurostat encouraged SE to convey to the MoF the common interest in clearly disclosing the methodological differences between the two sets of data when doing the national publication.

*Findings and conclusions*

*Action Point 2: SE will update the current EDP Inventory in line with the discussions held during the meeting. Deadline: January 2018.*

*Action Point 3: SE will analyse the changes to the working balance for the central government and the consequences for the reporting in EDP Table 2A and provide a note to Eurostat with its conclusions. Deadline: January 2018.*

*Action Point 4: SE should assess together with the Ministry of Finance the consistency of the information provided at national and European level (as required by Council Directive 2011/85) and any existing difference between the two sets of data should be properly explained. Deadline: January 2018.*

## 2. Follow-up of the EDP dialogue visit of 20-21 January 2015

*Introduction*

The 2015 EDP dialogue visit held on 20 and 21 January 2015 led to a list of 21 action points. As a result of these action points, several units were reclassified inside general government, notably the Financial Supervisory Authority (action point 10), the Deposit Guarantee Fund (action point 12), the Estonian Development Fund (action point 13), ES Smart Cap (action point 15) and the Oil Stockholding Agency (action point 16).

In addition, a debt cancellation from government was recorded (a loan provided by government to Estonian Air in 2013 (action point 17)). Furthermore, the recording of emission trading permits was also revised according to the treatment set in the Manual of Government Deficit and Debt (MGDD).

*Discussion and methodological analysis*

Eurostat enquired about the status of the 2015 action point 13 regarding companies owned/managed by the Estonian Development Fund (EDF). During the 2015 visit, Eurostat was of the opinion that these should be considered as public companies controlled by government, independently of the share of ownership by EDF, given the extended veto rights of EDF in such companies.

SE explained that the application of the market/non-market test to these companies was not adequate, as most of them were innovative companies (start-ups). Indeed, SE explained that it should not be expected that such companies could be profitable while they are at inception and development stages. Furthermore, EDF does not expect to receive distributed profits from these companies, instead it aims to obtain a profit by selling its shares at a higher market price. Overall, this means, according to SE, that the application of the market/non-market test should not be done mechanically.

Eurostat and SE discussed the issue at length. Eurostat and SE concluded that innovative companies owned by EDF do not need to pass the market/non-market test over a period of 3 years but rather over a period which is consistent with the business plan of each company. Also, Eurostat and SE agreed that if the market/non-market test is not passed, other evidence might be relevant and used so that these companies could be maintained outside general government (for example an observable share market price which demonstrates that EDF's investment proposition -earning a profit by selling its shares at a higher price- continues to make sense).

However, Eurostat emphasised that the nature of these companies require a very close monitoring. These are start-up companies and it is reasonable to expect that the majority of these innovative companies will not succeed and that the investment will not be recovered. This has already been observed in the past with a number of companies entering into liquidation. Eurostat noted that SE should reclassify into general government any company owned by EDF entering into liquidation or being inactive.

In relation to the status of action point 21, Eurostat also enquired about the present situation of the Rail Baltic project. SE confirmed that an agreement between the Government of the Republic of Estonia, the Government of the Republic of Latvia and the Government of the Republic of Lithuania on the development of the Rail Baltic/Rail Baltica Railway connection was signed by all parties on 31 January 2017 in Tallinn. SE also explained that while the agreement was ratified by the Estonian Parliament on 19 June 2017 and by Latvian Parliament on 22 June 2017, the Lithuanian Parliament had not yet done so at the time of the visit.

Even though the ratification of the agreement by all parties was still pending, SE was in a position to confirm that all related transactions will be recorded in the government sector accounts. This means that the recipient of EU grants will be the government sector and investment expenditures and corresponding assets will also be recorded in the government accounts. Eurostat enquired about the practicalities of this decision. SE explained that a 'head office' company based in Riga may issue debt; SE considered that, in that case, each country would record a portion of this debt. Eurostat enquired whether the debt would be guaranteed in full by all three countries or by each country separately for their respective share in the project. Eurostat also enquired about the possible need to re-route activities carried out by the umbrella company on behalf of the Estonian government and about the implications of recording in national accounts actions taken by the umbrella company based in Latvia. SE explained that it is too early to know the specific financing details but that nevertheless, the decision to record all related transactions through general government has been taken and that re-routing of some transactions is probable.

Eurostat reiterated the importance of monitoring the project closely and stated that the recording should be consistent in the three countries. SE explained that the need for consistency had already been raised by the Baltic States' statistics cooperation group and that this forum will continue to be used to harmonise the statistical recording.

*Findings and conclusions*

*Action Point 5: SE should continue to monitor the status of companies which are subsidiaries of the Estonian Development Fund (EDF) in order to ensure that MGDD rules concerning classification are promptly applied. Deadline: Ongoing.*

*Action Point 6: SE should monitor public units which are inactive or in the process of being liquidated in order to make sure that present MGDD rules are applied. Deadline: Ongoing progress, first progress note by End of January 2018.*

*Action Point 7: SE should follow the development of the Rail Baltic project in order to analyse and decide on the possible statistical recording consequences. Deadline: When available.*

## 3. Analysis of EDP tables - follow-up of the April 2017 EDP reporting

*Introduction*

During the April 2017 notification, Eurostat noticed that amounts for currency and deposits and receivables for 2016 were significantly different compared to the previous years. The lower amount of deposits was explained by SE as possibly due to different timing of inflows and outflows. The higher amount of receivables was partly explained by higher amounts of social security contributions cashed by the Estonian Tax and Customs Board but not transferred to the Social Security.

During the April 2017 notification Eurostat had noticed a slight increase in trade credits in 2016 compared with 2015 data. SE clarified that the increase in trade credits is associated with various fixed assets. Prior to the visit, Eurostat required further information on the nature of these trade credits. SE provided the following updated detailed information:

| Trade credits, assets | MEUR |
|---|---|
| Prepayments for fixed assets and inventories | 23.4 |
| Other prepayments | 23.1 |
| Claims associated with sale of goods and services | 44.4 |
| Claims associated with sale of fixed assets | 0.8 |
| | |
| ***Total Assets*** | ***91.7*** |

| Trade credits, liabilities | MEUR |
|---|---|
| Prepayments received for fixed assets to be sold | 0.3 |
| Other prepayments received | 10.4 |
| Liabilities associated with the acquisition of fixed assets | 43.4 |
| Liabilities associated with goods and services | 143.5 |
| Other liabilities | 5.7 |
| ***Total Liabilities*** | ***203.3*** |

During the 2015 EDP dialogue visit (action point 4) there were discussions about the counterpart of trade credits. After the visit, SE informed that there were no cases of factoring or trade credits with a bank as counterpart.

*Discussion and methodological analysis*

a) *Trade credits.*

SE confirmed that the observed differences in cash were due to different timing of inflows and outflows and that the economic recovery has contributed to increase the receivables. For example, receivables associated to social contributions, which are collected by the Estonian Tax and Customs Board and then transferred to the Social Security Funds, increased 1.3 million euro.

As regards the trade credits, liabilities associated with goods and services (143.5 million euro in the table above), SE confirmed that data is consolidated. Regarding possible cases of factoring, SE explained that it only had found one case of a factoring operation which was recorded as loans (F4) in 2015. Eurostat enquired about the possibility of finding factoring operations among the trade credits reported for local government. SE agreed that it could be possible that some municipalities do so. Eurostat and SE discussed how to quickly identify whether the risk is significant and agreed to carry out an enquiry of the amounts reported by the municipality of Tallinn, which represents about 50% of the total amount reported by the local sector (the local sector reported about 52 million out the 143 million euro, the rest being central government for 74 million and social security funds for 17 million euro).

For central government, SSSC explained that there is a special account label to indicate whether a transaction was recorded as a loan and, in such cases, it could be further investigated whether the operation could be related to factoring. SSSC and SE agreed to do some research to verify whether factoring operations are actually recorded as such. The participants discussed the possibility of verifying invoice payments to bank accounts not associated to the vendor as a possible indication of payments to banks and not to vendors.

b) *Questionnaire 10.2.*

Eurostat also enquired with SE about some remaining issues as regards EDP questionnaire table 10.2. In particular, during the April 2017 notification, Eurostat had asked about a capital injection of 32 million euro in one company (Elering) which was considered as a financial transaction and about an equity injection in the unit State Forest Management Centre (RMK).

SE explained that in the case of Elering, the capital injection has been justified by an expansion of its activities and that the company is profitable. Elering's total capital expenditure in 2012-2015 amounted to 469 million euro, with the majority of spending occurring in 2013 and 2014. In 2015, the company acquired a 100% stake in the Estonian gas transmission system operator (TSO) for 53.7 million.

As regards the capital injections for the unit RMK in the years 2015 and 2016, Eurostat noted that these transactions were recorded as a capital transfer. In addition, Eurostat mentioned that the company was also paying significant dividends in 2016 despite the fact that the company incurred losses in 2015. SE confirmed the payments of dividends by the company to government in 2016 but assured that this was not a super-dividend payment. SE explained that the losses recorded by the company in 2015 and 2016 were due to re-evaluation of biological assets. Eurostat further enquired about the equity injection recorded as a capital transfer. SE explained that this capital transfer was done to counterbalance the recording of the transfer of land from State to this company. The transfer of land to the company in exchange of shares was recorded by the state as P5 (imputed) and capital expenditure. Overall, this recording had no impact on government's accounts (in other words, EDP data was not affected) although for GFS purposes the recording was not neutral. Although SE agreed with Eurostat that the land transfer should in fact have been recorded as K6 (other changes in volumes) SE explained that they were not aware at the beginning about the nature of this transaction and at first they only noticed the increase in shares with a code of non-financial transactions.

Eurostat enquired and SE confirmed that the transfer of land did not lead to the recognition of a profit by RMK (in the financial statements of RMK, the increase in the value of land is compensated by the same increase in own resources, therefore the transaction did not have impact on the profit and loss account of the company although it increased assets and equity).

Eurostat enquired why RMK paid dividends while it incurred in significant losses in 2015 and 2016 (48.3 million and 232.9 million euro respectively). SE explained that the losses for both years were due to the impact of the revaluation of biological assets (originated by lower world market prices for timber). This explains why the dividends were not considered super-dividends as the losses due to the revaluation of assets are not considered when doing the super-dividend test.

*Findings and conclusions*

*Action Point 8: SE should take steps in order to ensure that information on factoring operations is properly reported for the central and local government. For the local government, this investigation can be done for the Tallinn municipality before deciding whether a full review of other local units is necessary. Deadline: January 2018.*

## **4. Methodological issues and recording of specific government transactions**

### 4.1. Delimitation of general government, application of the market/non-market rule in national accounts

#### 4.1.1. Implementation of the new MGDD (2016 edition). State of play

*Introduction*

Eurostat published a new MGDD (2016 edition) on 4 March 2016. Several chapters were significantly affected. During the 2017 April Notification, Eurostat had asked SE about the implementation of the provisions of the new MGDD (2016). SE confirmed that no further changes were necessary in order to implement the new MGDD.

*Discussion and methodological analysis*

a) *The treatment of public units in liquidation*

The treatment of public units in liquidation had been discussed with SE during the 2015 EDP dialogue visit. At that time, SE had noted that it was informed on time of the liquidation of public companies.

Eurostat enquired whether public companies in liquidation are reclassified to the general government. SE answered that so far there have been few cases, all affecting small companies and that, as a result of its analysis, none has been reclassified yet.

Eurostat stated that the reclassification to general government should be automatic for public companies in liquidation regardless of their size. SE noted that the decision to enter into liquidation and the actual closure are normally close in time and therefore the reclassification may not be necessary in some cases. Eurostat accepted that in some occasions this may be the case (both acts taking place in the calendar year) but emphasised the principle of reclassification of public companies in liquidation. In any case, SE noted that when a company has entered into liquidation but SE has decided to maintain its classification, SE adds the reference "(in liquidation)" to the name of the company in the report submitted to Eurostat.

Eurostat and SE agreed that the follow-up of inactive companies is also necessary. SE noted that inactive companies should fail the market-test. Eurostat argued that waiting for 3 years of non-compliance with the market test would delay the reclassification and thus it is not an adequate approach.

SE agreed with Eurostat on the need to investigate inactive and large public companies.

*b) The case of Estonian Air*

Estonia's national airline Estonian Air declared itself bankrupt in November 2015 after the European Commission decided that the state funding that the company had received was illegal and should be repaid. At that moment, Estonian Air was classified in S11 and its liabilities amounted to 84 million euro (half of these towards government).

SE considered that, according to the MGDD chapter, units in liquidation may still be market producers and should only be reclassified into the government sector if they fail the market/non-market test. Therefore, SE maintained the classification of Estonian Air as a market producer in 2015.

SE explained that the loan provided by the government was reported as a debt cancellation in 2014. Eurostat enquired how it was possible that SE decided to record a debt cancellation in 2014 while at the same time not questioning the classification of Estonian Air outside general government. SE noted that the decision to record the debt cancellation was a prudent decision based on the difficulties faced by the airline at the time. However, it decided to keep its classification as Estonian Air was still able to pass the market/non-market test.

SE explained that, as from 2016, Estonian Air is classified inside general government and it will be included in the questionnaire to be sent to Eurostat by December 2017. Eurostat also enquired about the current status of the liquidation. SE explained that, at the time of the visit, Estonian Air had not yet presented the closing reports to the Business Register. SE noted that, as there is no official data source, the actual figures for assets and liabilities have not been imputed into GFS.

*Findings and conclusions*

*Eurostat and SE agreed on the importance of analysing the situation of inactive companies. SE stated that it will continue to analyse each case individually to decide whether a sector reclassification is needed. As regards Estonian Air, SE announced that the company should be reclassified into S.13 in the next questionnaire to be sent to Eurostat by December 2017.*

### 4.1.2. Application of the market/non-market test in the context of ESA 2010 (i.e. Hospitals)

*Introduction*

Eurostat is currently doing a review of the classification of hospitals across the EU. Taking advantage of the visit, Eurostat decided to clarify with SE a few aspects regarding public hospitals. Currently, public hospitals in Estonia are classified into the government sector.

In Estonia, hospitals, as all health care providers, operate under private law and can belong to public or private ownership. The Estonian Health Insurance Fund (EHIF, part of S.1314) is the largest buyer of health care in the country (67% in 2013) followed by the households (22%) and government (10%).

There are currently about 65 public and private hospitals in Estonia, including 35 nursing and rehabilitation hospitals.

The EHIF has contracts with the 19 public hospitals that are included in the Hospital Network Development Plan (HNDP). This plan, approved in 2003, lists the investment needs of these hospitals in order to renovate their premises and restructure their services. The HNDP investment needs served as a basis for the implementation of EU structural funds from 2007-2013. The current contract between the EHIF and the HNDP network was signed in 2014 and has a five-year duration.

*Discussion and methodological analysis*

Due to the relevance of the EHIF as the primary buyer of health care in Estonia, Eurostat enquired about the HNDP network. In particular, Eurostat enquired whether there was any private hospital in the network. SE confirmed that all HNDP hospitals are public hospitals and that all are classified inside general government.

Eurostat also enquired about private hospitals and the role of the government in their governance and autonomy of decisions. SE confirmed that the government does not intervene in the running of private hospitals which can set their own tariffs and decide on the working conditions of its staff. When the EHIF needs to complement the services provided by the major public hospitals included in the HNDP network it signs contracts with health care providers to deliver the services. The contract sets the prices for these services. The EHIF only contracts for the services it may need, which means that the contract only covers certain services. Private hospitals and public hospitals compete for these contracts.

*Findings and conclusions*

*On the basis of the information provided, Eurostat agreed with SE that the current classification of hospitals in Estonia is correct.*

### 4.1.3. Changes in sector classification

*Introduction*

Prior to the mission, SE informed Eurostat that there have been no significant changes in the sector classification in the last two years. SE informed that three very small corporations have been classified into government sector due to the consolidation of the units with the parent company.

Starting from year 2014 a number of local hospitals (4 hospitals) have been consolidated with state hospitals and have therefore been reclassified from the local government subsector to the central government subsector. As a result, the financial reports of these hospitals have been consolidated with the new parent unit.

In addition to the hospitals, another four units were consolidated and classified into the central government sub-sector. These units were classified into government sector as ancillary units due to the fact that their services were provided to other units of the government sector (in particular to public hospitals).

*Discussion and methodological analysis*

Eurostat enquired about the consolidation of hospitals. SE confirmed that the local hospitals affected were already classified inside local government and theferore the consolidation did not have any impact on EDP or debt figures.

Eurostat enquired about other type of transactions affecting hospitals. SE explained that two local hospitals were privatised and thus reclassified from S.13 to S.11. These hospitals are currently owned by private sector investors and there is no intervention from government, other than holding a licence and eventually contracts with the EHF as other hospitals in the country.

*Findings and conclusions*

*Eurostat agreed on the adequacy of the reclassification of the ancillary units and reminded SE to monitor possible cases in other sectors.*

### 4.1.4. Questionnaire on government controlled entities classified outside the general government sector and Questionnaire on implementation of ESA 2010 general government delimitation

*Introduction*

SE provided Eurostat with a questionnaire on government controlled entities in December 2016 with 2015 data. During the previous EDP dialogue visit, SE agreed to monitor some of the units. One of the most relevant entities included in this report is Estonian Air, a unit which declared bankruptcy in 2015.

*Discussion and methodological analysis*

Eurostat enquired whether SE checks regularly that all public companies pass the market/non-market test. SE confirmed that it checks all units even if only units above the threshold are included in the report submitted to Eurostat.

SE explained that it does the testing over 5 years, and that unless SE has information from other sources, SE waits for at least three years before reclassifying a company failing to pass the market/non-market test. The data provided in the questionnaire is based on PSFS.

Eurostat and SE reviewed some of the companies included in the December 2016 report.

Estonian Air (10076042) has been classified within subsector S.11 despite being in liquidation, a point addressed in section 4.1.1. However, Eurostat noted that the financial information included in the list for Estonian Air cannot refer to 2015 as the company declared bankruptcy before year-end and the closure reports have not been adopted yet. SE explained that the information refers to the latest financial information available before the company declared bankruptcy.

As regards Nordic Aviation Group AS (Nordica) and OÜ Transpordi Varahaldus, the two companies which were established by the Government to continue Estonian Air's operations, SE explained that the two companies are included in subsector S.11 as there is not sufficient ground to reclassify them into general government.

In this regard, Eurostat noted that, according to the financial statements, the Nordica group incurred in total losses of 14.3 million euro during the first fifteen months of operations (9 October 2015- 31 December 2016). However, SE replied that initial losses were expected and that SE still considered that Nordica would be in a position to pass the market/non-market test over a multi-year period. SE also noted the relevance of recent corporate operations (on 21 February 2017 Regional Jet OÜ was sold to LOT Polish Airlines[5]).

SE also noted that, despite classifying these units into the non-financial corporations sector (S.11), SE decided to record the capital injections made to the companies at their creation as capital transfers (D.9) in GFS.

Prior to the visit, SE had confirmed that these two companies did not assume employment contracts of Estonian Air. Eurostat enquired about an ongoing court case by which 59 former Estonian Air employees have taken Nordica to Court to claim severance pay[6]. SE replied that it is aware of this situation and that it is following up the case.

Eurostat also enquired whether OÜ Transpordi Varahaldus, which is the company providing planes to Nordica, should be considered an ancillary of Nordica. SE replied that it is expected that the company would be involved in other sectors, with other clients and not only with government. Nevertheless Eurostat and SE agreed that the sector classification of OÜ Transpordi Varahaldus will be assessed if there is any change to the sector classification of Nordica. Eurostat furthermore asked SE to monitor the airplane leasing contracts to decide whether these are operational or financial leases.

[5] In December 2015 Nordica created a subsidiary – Regional Jet OÜ. Regional Jet OÜ has air operator certificate, operating licence and other international certificates. Starting from mid-2016 Regional Jet OÜ was providing flight operating services to LOT Polish Airlines.

[6] The plaintiffs seek more than 1.7 million euro in unpaid severance and vacation as well as dismissal benefits. They argue that Estonian Air took on a new form in Nordica and thus, the latter must also take responsibility for the claims.

Eurostat enquired about another company, Ilmarine Engineering OÜ (11329039), which is the only one failing the market/non-market test according to the list prepared by SE. SE explained that this company was a patent holder. As the patent fees were not recorded as revenue from sales, but as other revenues, the market test of the company was zero or close to zero. SE also informed that the company went into liquidation in 2016. SE explained that, as the government has minority share (15%) in the company and no veto rights in the case of liquidation, it decided that the unit would not be reclassified into government sector for such a short duration. SE emphasised that this deviation is not material as reclassifying this small company would have no significant effect on government financial figures.

Eurostat enquired whether SE performs the market/non-market test for the individual entities part of Eesti Energia AS group (10421629). SE confirmed it does so and noted that, although the questionnaire only discloses consolidated data, this is because the consolidated financial report is easily available. SE confirmed that as agreed in January 2015, it does individual tests although less frequently than for other entities in the questionnaire.

Eurostat welcomed this information and invited SE to update this procedure in the next version of the EDP inventory.

Eurostat also enquired about the number of companies with no employees. SE explained that this may be due to different reasons, for example some of the companies could be holding companies, with no employees. SE also stated that it does not have any doubts regarding the reliability of the information.

Eurostat enquired about a small difference in the profits of one company between the questionnaire and the published financial statements. SE explained that the difference may be due to updated data and that it will verify that the questionnaire to be submitted by end 2017 includes the most recent data.

Eurostat asked SE about the characteristics of the company AS KredEx Krediikindlustus. SE explained that it is an insurance subsidiary of KredEx Fund. Eurostat noted that, on the basis of the information received, it recommended SE to analyse the sector classification of AS KredEx Krediikindlustus. In particular, Eurostat recommended SE to analyse whether the criteria used by Eurostat to advice on the reclassification of KredEx Fund into general government was also applicable[7]. Eurostat noted that this assessment should also consider whether AS KredEx Krediikindlustus falls into the category of captive financial institution. SE agreed to carry out this assessment.

*Findings and conclusions*

*Action Point 9: SE will send to Eurostat the English version of the most recent accounts of the Nordic Aviation Group AS. Deadline: September 2017*[8].

*Action Point 10: SE should closely monitor the financial situation of Nordic Aviation Group AS (Nordica) in order to confirm its current classification in S11. Deadline: Ongoing.*

[7] http://ec.europa.eu/eurostat/documents/1015035/2990403/EE-Fund-grants-provided-from-EU-budget-to-KredEx.pdf/12684085-f5ef-4fce-be38-1c986951d51d

[8] This action point could not be completed by September 2017 as no English version was available. SE will send these as soon as an English version becomes available.

*Action Point 11: SE should monitor the financial situation of OU Transpordi Varahaldus in the context of its envisaged expansion in order to assess the statistical reporting consequences. Deadline: March 2018.*

*Action Point 12: SE should analyse the current classification of AS KredEx Krediikindlustus in the light of the 2014 Eurostat advice for the classification of KredEx Foundation. Deadline: January 2018.*

## 4.2. Implementation of the accrual principle

### 4.2.1 Accrual taxes and social contributions

*Introduction*

SE records taxes and social security contributions on an accrual basis using time-adjusted cash data. The data source becomes available in T+1 month from the Tax and Customs Board. This procedure affects two taxes (VAT and Social tax) which are paid in the month following the activity.

*Discussion and methodological analysis*

Eurostat enquired SE whether the recording of taxes and social security contributions includes estimations. The EDP inventory states that the authorities (mainly the Tax and Customs board) make an assumption (based on time-series) that 1/3 of the increase in tax arrears will never be paid. Eurostat asked how this is applied considering that the recording method is time-adjusted cash.

SE confirmed that no estimation is done as regards the recording of taxes and social security contributions.

SE, however, noted that for some small taxes cash figures may not be available on time for the April notification. This is the case for example for land taxes for which the budgetary figure is used for the April notification and the actual cash figure for the October notification. Eurostat and SE discussed whether it was technically possible to use the cash figure for the April notification and SE noted that in view of the limited staff resources available, it did not consider it feasible. SE also noted that experience shows that tax revenues rarely change due to the impact of the correction of small taxes.

Eurostat also enquired about the new taxes being introduced by the government. As regards the sugar tax, it will be recorded as the rest of excises, that is time-adjusted cash. As regards the road tax, Eurostat noted that depending on the characteristics of the tax, it will need to be recorded as tax or a service charge. SE and Eurostat discussed the influence of different elements such as the compulsory nature, whether it was due even when the motor vehicle was temporarily out of circulation, whether it is related to the possible deterioration of the road by each vehicle (for example, charging much more to heavy vehicles), etc.

SE agreed on the importance to assess the nature of the road tax at an early stage. However, SE noted that it was too early to do such assessment as the final characteristics of the tax were not known.

Eurostat and SE also discussed other changes to the tax system, such as changes to personal income taxes (mortgage interest allowances, increase of basic tax-free allowance, increase of additional tax-free allowance of pensions), increases in excise duty on alcohol, tobacco, fuel and natural gas and a new reduced corporate tax rate of 14% of regularly distributed profits.

Eurostat and SE agreed that changes to tax structure will not require adjustments to the recording of taxes as the recording follows a time-adjusted cash method and no assumptions/estimations are done.

SE also confirmed that tax refunds are recorded on a pure cash basis (when the refund is paid, without estimations).

*Findings and conclusions*

*Action Point 13: SE is invited to seek an ex-ante advice request for the recording of the new road tax to be implemented from January 2018. Deadline: When considered necessary.*

### 4.2.2. Accrued interest, consolidation

*Introduction*

The data source used for recording interest expenditure is PSFS (accrual basis) which provides separately recorded information for interest expenditures associated with loans, with securities, with financial leases and with other payables, as well as interest revenues. The EDP Inventory states that interest accrued but not paid on loans, securities and financial leases is recorded in one account. As the major share of liabilities in this category is associated with loans, the predefined amount of interest for known securities is recorded under AF.3 Securities and the rest is allocated under the instrument AF.4 Loans in financial accounts.

According to the Inventory, the working balance presented in EDP tables 2A and 2C originates from cash based budget execution reports, which are more aggregated than the PSFS and it is impossible to draw the full information about interests paid and received from there. Prior to the visit, Eurostat requested a table on interest recording. SE informed Eurostat about the difficulties and workload required to provide the level of information demanded in the table.

*Discussion and methodological analysis*

SE confirmed that it lacks sufficient detail to fill the tables at subsector level and that it relies on the information provided by PSFS and some assumptions.

SE also confirmed that due to the small number of issuers of securities (four issuers at the time of the visit) the impact of the assumptions is not too significant. Eurostat noted that there was an amount declared for central government as coupons accrued/paid whereas the central government does not appear to be an issuer of securities. SE confirmed that there were no issuers of securities classified in central government. SE noted that it was thus probable that the amounts included as coupons accrued/paid for central government referred to interest accrued/paid for loans.

Eurostat acknowledged that given the very low debt of Estonia, the practical consequences of the limitations faced by SE are relatively small. However, Eurostat conveyed the importance of counting with reliable and sufficiently detailed data and encouraged SE to work with the SSSC and MoF to obtain it in the future.

### 4.3 Recording of specific government transactions

#### 4.3.1. Guarantees

*Introduction*

Three major government units provide guarantees: MoF, the Ministry of Education and Research and KredEx Fund (formally a foundation established by the state). MoF provides one-off guarantees for other central government units and also to public sector enterprises. The Ministry of Education and Research provides standardised guarantees for student loans. KredEx (S.1311) provides standardised guarantees for housing loans and for specific loans for enterprises.

Information about the stock of guarantees provided is recorded in PSFS as off-balance sheet liabilities. In the case of standardised guarantees, PSFS only provides the stock of guarantees and thus, no information on the separate flows (guarantees being granted versus guarantees being cancelled). This information is only available when the financial statements of KredEx Fund are published, within six months.

SE provided prior to the mission the list of one-off guarantees. The list only disclosed 0.8 million euro of stock of government guarantees, 0.4 million euro related to rental contracts by the Ministry of Foreign Affairs and 0.5 million euro as a guarantee provided to the EIB in the context of the Cotonou agreement.

*Discussion and methodological analysis*

SE provides in EDP questionnaire table[9] 9.1 the total of guarantees, including both one-off and standardised guarantees. Eurostat enquired why during the April 2017 notification, the stock values of guarantees included in table 9.1 and table 9.4 were the same (335 million). Eurostat noted that the later table should only include standardised guarantees. SE confirmed that it was likely a rounding effect as SE only considered 0.8 million euro of one-off guarantees.

SE updated prior to the mission table 9.1. Eurostat noted that after this update, table 9.1 presents a lower stock value of guarantees[10]. As other tables had not been modified, the stock value of guarantees in table 9.1 exceeded the stock value of standardised guarantees in table 9.4 (319.5 versus 335 million euro). Eurostat also noted that in table 9.1 the amounts of guarantee cash calls (recorded as expenditure) have ranged between 0.3 and 0.5 million euro in the 2014-2016 period. In contrast, repayments by the original debtor recorded as revenue have ranged between 1.1 and 1.3 million euro in the same period. Eurostat enquired about the

[9] Guarantees are reported to Eurostat in the EDP questionnaire tables 9.1 to 9.4. All references to tables in the following paragraphs on guarantees should be read as references to EDP questionnaire tables submitted in the April EDP notification period (or updated prior to the mission).
[10] SE has provided, prior to the mission, an updated questionnaire table 9.1. This table now shows a stock of guarantees of 319.5 million euro in 2016. In the version submitted in the April 2017 notification, the value of the stock was 335 million euro.

possible explanations of this unusual relationship (that repayments exceed cash calls) over a multi-annual period.

Eurostat also noted that table 9.4 includes information about expenditure recorded in ESA accounts which does not reconcile with the information included in table 9.3 concerning capital transfer expenditure relating to provisions on standardised guarantees (item 3d). Finally, Eurostat admitted its difficulties in reconciling the amount of guarantees called as table 9.1 and table 9.3 include lower values of guarantees called (cash payment) than the amounts included in table 9.4 for the years 2013-2015 (in 2016 the values were the same).

SE confirmed that it will review the compilation of these EDP questionnaire tables before the October 2017 notification to address their consistency.

<u>Standardised guarantees: housing loans</u>

In the context of the discussion of guarantees, Eurostat and SE discussed in more detail the recording of student loan guarantees. SE explained when the government honours the guarantee:

- The government takes over the obligation of the borrower permanently (this applies for instance in cases the borrower dies or is permanently disabled) => the State is paying the residual loan amount to the bank; payment is recorded in PSFS as social benefits.
- The borrower fails to follow the payment deadlines => the government pays the loan and request repayment (recorded in PSFS as a financial transaction)
- The market interest rate for loans is exceeding the level of 5% => the government is covering the difference between the market interest rate and ceiling interest rate (transfer recorded as social benefit).

In national accounts all these occurrences of payments are treated as debt assumptions and are recorded as expenditures in D.99 Other capital transfers. SE explained that student loans are also guaranteed by parents or other relatives of the student, and that the government generally recovers from these other guarantors any payment made because of default of the loan. These revenues are recorded in revenues as capital transfers (D.99).

*Findings and conclusions*

*Action point 14: SE will review the presentation and consistency of the EDP related Questionnaire Tables 9.1, 9.2, 9.3 and 9.4. Deadline: End of September 2017.*

### 4.3.2. Capital injections in public corporations, dividends, privatisations

SE provided prior to the visit a list of capital injections to public corporations and a list of dividends paid from 2013 (including the superdividend test result). SE confirmed that there had been no interim dividends.

The list of capital injections to public corporations includes two injections in 2015 to AS Nordic Aviation Group and OÜ Transpordi Varahaldus of 41 and 32 million euro respectively. These capital injections were recorded as D.923 - Capital injections to own capital recorded as capital transfers. The situation of these two companies was also discussed under section 4.1.4.

### 4.3.3. Debt assumptions, debt cancellations, debt write-offs and foreign claims

This issue was treated under section 4.1.1 within the point dealing with public units in liquidation, the case of Estonian Air.

### 4.3.4. Centralised treasury function: intragovernmental deposits and overdrafts

*Introduction*

In Estonia, the MoF (State Treasury) manages day-to-day cash flows of all State entities, State owned foundations (such as museums, theatres, hospitals etc.) and social security funds since 2011. Different entities with positive and negative cash positions balance each other internally so decreasing the borrowing needs for the State. The State Treasury guarantees that State entities can make payments subject to their budget limits and/or cash balances whenever they need.

On 29 July 2016, Eurostat provided an opinion on the recording of intra-governmental deposits. Eurostat's opinion on the treatment of intragovernmental deposits was that the cash reserves of social security funds should be recorded as deposits held in central government accounts (S.1311). The assessment also indicated that overdraft taken by S.1311 on deposit accounts of S.1314 should be recorded as short-term loans (AF.41) with counterpart financial corporations.

*Discussion and methodological analysis*

SE explained that the State Treasury uses four local banks – Swedbank, SEB Bank, Nordea Bank and Danske Bank - for collecting revenues and channelling domestic and foreign payments. Prior to the mission, SE provided a note on the application of Eurostat's opinion from September 2016 transmission (changes affected time series starting from 2012):

1) financial account:
a. AF.2 Cash and deposits liabilities appeared in central government subsector (S.1311). Counterpart of the liabilities is social security subsector (S.1314)
b. At the same time AF.2 Cash and deposits claims of S.1311 toward financial institutions sector (S.12) increased
c. For S.1314 claims in AF.2 Cash and deposits counterpart changed from S.12 Financial institutions to S.1311
2) government sector debt: S.1311 debt increased by the amount of AF.2 liabilities; general government debt at the same time was not affected

On the basis of this note, Eurostat considered that SE is largely following Eurostat's advice, in particular by recording deposits by the social security sector as deposits held in central government.

As regards the part of the advice regarding overdrafts, SE acknowledged that this has not been implemented due to the practical difficulties to do so. Once the funds from S.1314 are deposited in the State Treasury accounts, these are fungible and therefore it is not possible to assess whether overdrafts on their positions by units belonging to S.1311 have been funded by other units of the same subsector or by units belonging to S.1314.

*Findings and conclusions*

*Eurostat recognised the practical difficulties linked to the full application of its advice (once amounts are deposited or payments are made from the account, it is not possible to specify whether part of the amount deposited by S.1314 has been used through overdrafts by a particular government entity) and therefore accepted the approach taken by SE.*

**4.3.5. UMTS. Emission permits. Environment taxes and others**

*Introduction*

Prior to the mission, Eurostat requested a note from SE detailing the treatment of the one-off fees paid for Universal Mobile Telecommunications System (UMTS) licences. SE confirmed to Eurostat that there are some problematic aspects in implementing the guidance note "Mobile phone licences, exploration rights and other licences" published on 27 March 2017. According to this guidance, the licence fees on radio frequencies should be recorded as rents (D.45) and should be distributed over the life-span of the licence. Currently, these amounts are recorded as NP; Acquisitions less disposals of non-produced non-financial assets.

In Estonia the use of radio frequencies is permitted on the basis of a frequency authorisation. The frequency authorization is granted for a term of up to one year, except under very specific conditions. Upon the grant of the right to use radio frequency band by way of public competition, the Minister of Economic Affairs and Communications may determine a one-off authorisation charge and a deposit for participation in the competition. One-off authorisations charge is determined as a fixed charge or, in the case of auction, as a starting price. The deposit is equal to all participants and it will be returned after the winner of the competition is determined.

Until now such charges are levied only when some frequency has been taken into specific use for first time. For instance, in 2013 frequency 790-862 MHz was auctioned to be taken into use for mobile networks, while previously it was used for TV broadcasts. Frequency authorization has to be extended (renewed) each year and a government fee has to be paid for that purpose. In case this fee is not paid, the frequency authorization cannot be renewed and the operators should apply again.

It should be noted that even in the case of public competition/auction, where one-off authorisation charge is paid, the state fee has to be paid also. Without payment of the state fee, the frequency authorization is not granted. If several persons have concurrently submitted application for the use of the same radio frequency, the Technical Surveillance Authority shall organise an auction in order to grant frequency authorisation.

*Discussion and methodological analysis*

Eurostat agreed with SE that the state fee has to be paid each year and therefore could be recorded in the respective year.

In the case of one-off fees, the recording is more problematic. In principle, the one-off fee is co-related with the state fee and thus, gives the right to the operators to use the frequency only for one year. SE has followed this argument and has recorded the one-off fees in the year these were cashed. However, Eurostat noted that it is economically reasonable to assume that the holder of the frequency authorisation will wish to keep the authorisation for longer than one year.

The amounts of one-off fees are included in the following table:

| Year | EUR |
|---|---|
| 2010 | 1,661,703 |
| 2011 | 2,454,213 |
| 2012 | 274,258 |
| 2013 | 6,088,704 |
| 2014 | 5,100,645 |
| **Total** | **15,579,521** |

Eurostat also acknowledged that, as the licences were auctioned without a fixed duration, it is uncertain over which time period these one-off fees should be distributed. Given this extraordinary circumstance, the retroactive application of the guidance note does not seem to be desirable as it will correct the past recording with a new one which is based on assumptions as regards the time duration of the licences. Eurostat recognised that, while other methods can be used to estimate which is the expected duration (for instance comparison with the market), it does not seem justified to correct past data if there is no certitude about the duration.

SE agreed with this assessment.

As regards future auctions, Eurostat noted that, as the guidance note is fully applicable from its publication, future auctions would have to be recorded in accordance with it and therefore SE would need to estimate the expected duration of the licence if the terms of reference of the auction does not set the duration.

<u>Emission permits</u>

Eurostat and SE discussed how SE obtains the necessary data to record the revenue linked to the sale of emission permits. SE explained that it obtains the number of permits sold from the website of European Energy Exchange at www.eex.com and the number of permits allocated for free is obtained from the Ministry of the Environment of Estonia. SE noted that the number of permits allocated for free was negotiated by Estonia and the European Commission for the trading period of 2013-2020[11].

However, SE confirmed that it does not have information on the origin of the permits surrendered. That means that SE does not know: 1) whether the surrendered permit was issued domestically or not and 2) for domestic permits, whether the permit was given for free or whether it was auctioned.

In 2013 Estonia sold permits for the first time. From that date the number of surrendered permits has exceeded the number of granted permits. When recording the tax revenues from emission permits, SE does the following assumptions:

- Since the number of surrendered permits has been higher than the number of permits granted in Estonia from 2013, SE makes the assumption that Estonian companies buy permits from abroad only when they have used the ones issued domestically first.

[11] The numbers of permits are also available at http://ec.europa.eu/clima/policies/ets/registry/index_en.htm

- SE makes the assumption that companies use first free permits before surrendering sold permits.

In practice, this method means that revenues from permits sold in year T are recognised in B9 in year T+1.

The MGDD states that when compilers cannot identify, within the surrendered permits, between free and sold permits, the market price could be still calculated on the basis of the permits issued through auctions. MGDD recognises that this method would not make a difference provided that it would be possible to identify the domestic permits and accepts that, as a proxy, compilers use a kind of 'first in first out' method in the sense that domestic permits are considered to be surrendered first.

In 2013 Estonia sold 4.091 permits for an amount of 18.1 million euro. This amount was included in the working balance. The adjustments made by SE in 2013 reduced the revenue by 18.1 million and recorded accounts payable for that amount. In 2014 Estonia sold 1.244,5 permits for 7.4 million euro. As in 2014 the accumulated number of surrendered permits had exceeded the accumulated number of permits granted by Estonia, SE recognised the full amount received in 2013 for the sale of permits as tax revenue during 2014. The amount received in 2014 was entirely recorded as tax revenue in 2015.

| | 2013 | 2014 |
|---|---|---|
| **Working balance** | **18.1** | **7.4** |
| **Non-financial account** | | |
| **D.2 revenue** | 0 | 18.1 |
| **B.9** | 0 | 18.1 |
| **Difference between working balance and B.9** | 0-18.1=-18.1 | 18.1-7.4=10.7 |
| **Financial account** | | |
| **AF.2 assets (Stock end of the year)** | 18.1 | 18.1 + 7.4 = 25.5 |
| **AF.8 liabilities (Stock at the end of year – decrease from the D.2 revenues + increase from the inflow of cash)** | 0 - 0 + 18.1= 18.1 | 18.1-18.1+7.4=7.4 |
| **incl. F.8 transaction** | 18.1 – 0 = 18.1 | 7.4 – 18.1 = 10.7 |
| **B.9F (change in the AF.2 – change in the AF.8)** | (18.1-0) - (18.1-0) = 0 | (25.5-18.1) – (7.4-18.1) = 7.4 – (-10.7) = 18.1 |

Eurostat noted that the approach followed by SE is an adequate approximation to the MGDD as long as the number of surrendered permits exceeds the number of permits issued domestically every year. If this trend changes, SE would need to reassess its approach as continuing with it without adjustments would mean that all revenues from emission of permits are recognised the following year for a long time. This is because the historical excess of surrendered permits versus issued permits (negative stock of permits) is so large that it would not be corrected in the short term. In other words, permits auctioned in year t would be recognised as revenue in year t+1 as the number of permits surrendered in years t-10 to t-1 exceeded permits issued/auctioned in years t-10 to t-1 by a sufficient margin to compensate the possible difference.

Environment taxes

The new government of Estonia has announced its intention to introduce new taxes, in particular to increase and introduce new environmental taxes. The most relevant tax was the road tax which was discussed in section 4.2.1.

Public Private Partnerships and Concessions

SE confirmed to Eurostat that it is normally informed at an early stage of the preparation and discussion of Public Private Partnerships in Estonia, although this is more challenging for contracts prepared by municipalities. SE also noted that as PPP projects are included in the general government following national rules, public bodies in Estonia do not have incentives to use PPP contracts for reporting purposes.

SE also confirmed that there are no concessions in Estonia.

*Findings and conclusions*

*As regards the recording of revenue linked to UMTS licences, given the fact that contracts do not have a fixed duration in Estonia, Eurostat considers that the present method used by SE to record UMTS revenues is appropriate.*

*Action Point 15: SE should continue its efforts to be involved in the early stage of the preparation of Private-Public- Partnerships (PPPs) and concession contracts, including those initiated by local authorities. Deadline: Ongoing.*

## 5. Other issues

### 5.1. ESA2010 Transmission Programme relating to the GFS tables

Eurostat and SE agreed to follow-up bilaterally a list of issues such as conscripts' expenditure, interest expenditure and market valuation of debt. Eurostat thanked SE for its efforts to regularly provide GFS voluntary information.

### 5.2. Any other business.

Eurostat announced the publication of guidelines on energy performance contracts and enquired whether the guidelines would have any impact in Estonia. SE confirmed that energy performance contracts are rare in Estonia and that no impact is expected.