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The Director-General

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Statistisches Bundesamt Deutschland
Mr Dr Georg Thiel - Präsident
Gustav-Stresemann-Ring 11
65189 Wiesbaden
GERMANY

Subject: Request for ex-ante advice
Sector-classification of "BVG-Fahrzeugfinanzierungsgesellschaft"

Ref.: Your letter dated 23 July 2018 (reference: D204/38131100-BVG-FFG)
Our letter dated 10 September 2018
Your e-mail dated 10 September 2018
Your e-mail dated 15 October 2018
Your letter dated 8 March 2019

Dear Dr Thiel,

Thank you for your letter dated 23 July 2018 and the attached documentation including:

- the analysis by the Statistische Bundesamt (DESTATIS) of the sector-classification of *BVG Fahrzeugfinanzierungsgesellschaft*,
- the legal documents concerning the operations of *BVG Fahrzeugfinanzierungs-gesellschaft*, as well as
- the additional documents and the complementary information provided by Destatis on the 10 September and the 15 October 2018.

After having closely examined the documents provided, Eurostat is now in a position to express a view on this matter.

1. The accounting issue for which a clarification is requested

The issue to be analysed is the sector-classification of *BVG Fahrzeugfinanzierungsgesellschaft* (hereinafter, BVG-FFG), a subsidiary of *Berliner Verkehrsgesellschaft* (BVG) established in 2016 to provide financial resources for the acquisition of rolling stock by BVG, as well as the accounting implications of the transactions carried out by BVG-FFG. The statistical authorities of Germany have asked Eurostat to assess the issue at stake and express its opinion.

Documentation provided

The statistical institute of Germany provided to Eurostat (1) its analysis of the sector-classification of BVG-FFG, together with (2) several legal documents concerning the unit and the legal relation with its shareholder as well as, on request, (3) some additional information on the debt profile and the investment grants.

Description of the case

BVG is the main provider of local public transportation services in Berlin. It has a monopoly position regarding the provision of tram and underground services, and, in addition, provides other services, including bus services, in competition with other corporations (although BVG is, by far, the main provider for this latter activity).

A service contract exists between BVG and the Land of Berlin, which will expire in August 2020. Both parties have already agreed, in 2015 in a letter of intent signed 7 January 2016, to renew the contract beyond that date. The next contract shall cover the years from 2020 to 2035. The letter also states major conditions for the extension; one of these conditions being the acquisition of new rolling stock by BVG to replace the existing fleet and increase its capacity. The acquisition is envisaged to include 700 large-profile and 500-small profile metro train sets and 200 trams. The investment into the rolling stock is planned to amount to up to EUR 3.2 bn, a major investment for BVG given that – at end-2017 – the value of fixed assets on BVG's balance sheet amounted to EUR 4.9 bn.

The acquisition of the new rolling stock shall be financed by incurring new debt on the capital market, rather than through loans (and investments grants) by the Land of Berlin, as was past practice. To implement this new financing model, a new unit has been established in January 2016, *BVG Fahrzeugfinanzierungsgesellschaft* (BVG-FFG). BVG-FFG is a limited company with BVG being sole shareholder. The relation between the two companies is stipulated in various legal documents.

The Land of Berlin will however remain deeply involved with providing investments grants to BVG for the specific purpose of allowing BVG to acquire the rolling stock. To this effect, the letter of intent between BVG and the Land of Berlin states additional details with regard to the financing model. BVG-FFG will take out loans in its own name, however the Land of Berlin commits to covering part of the costs of the investments, i.e. the Land of Berlin will provide dedicated investment grants. The financing plan is set up for 35 years of amortisation of vehicles (up to 2069), as the last procured vehicles are expected to take up service in 2035. The payment of the investment grants by the Land of Berlin to BVG will start in 2020, when the new service contract between BVG and the Land of Berlin will take effect. Therefore, the servicing of the loans is divided into three parts:

- 2016-2019 the BVG will cover the expenditure,
- 2020-2035 the Land of Berlin will carry out the payments of investment grants to BVG,
- 2035-2069, repayment of the remaining debt by BVG.

2. METHODOLOGICAL ANALYSIS AND CLARIFICATION BY EUROSTAT

Applicable accounting rules

- ESA 2010, Chapter 1, paragraph 1.78, recognising the principal party of a transaction.
- ESA 2010, Chapter 2, in particular, paragraph 2.12 dealing with the issue of the definition of an institutional unit. As well as, paragraphs 2.35 to 2.38 concerning the issue of control of an institutional unit. In addition, ESA 2010, Chapter 20, especially paragraphs 20.27 to 20.29 providing rules for the market distinction and 20.309 dealing with public sector control.
- ESA 2010, Chapter 4, paragraphs 4.152 - 4.163 dealing with investment grants.
- ESA 2010, Chapter 4, paragraphs 4.164 - 4.165 dealing with other capital transfers.
- The Manual on Government Deficit and Debt (MGDD), implementation of ESA 2010, 2016 edition: Part I.2 “Criteria for classifying units to the general government sector”.

Availability of national accounting analysis

The national statistical institute of Germany (DESTATIS) has provided to Eurostat an analysis of the case. It concludes that BVG-FFG is not an institutional unit and therefore it has to be classified with its controlling unit. According to the analysis, the controlling unit of BVG-FFG is BVG, which is controlled by government. However, since BVG is currently considered by DESTATIS to be a market producer, the BVG-FFG would be classified with BVG in the non-financial corporations sector (S.11).

Methodological analysis and clarification by Eurostat

BVG-FFG as institutional unit

Taking into account legal aspects, BVG-FFG would appear to be an institutional unit. A priori, the unit seems to comply with all the criteria set out in ESA 2010 2.12. Because of its legal form ("Gesellschaft mit beschränkter Haftung", limited company), it should in principle be:

a) Entitled to own goods and assets in its own right,
b) Able to take economic decisions and engage in economic activities for which it is responsible and accountable at law,
c) Able to incur liabilities on its own behalf,
d) Able to draw up a complete set of accounts.

However, the legal documents provided by the national statistical authorities of Germany indicate, that BVG-FFG is restricted in its decision-making ability in such a way that it would lack autonomy of decision, in the ESA 2010 meaning, and therefore would not be seen as being an institutional unit.

The provisions in its procedural rules state that the two executive directors of BVG-FFG have to be executive staff members of BVG. The rules also stipulate that all transactions concerning the main function of the unit, which is, according to the articles of association, the provision of financial resources to BVG, surpassing a certain threshold in EUR need the approval of the shareholders – in this case, the BVG, since it is the sole shareholder. The threshold is set in such a way (i.e. very low) that, in practice, the executive directors of BVG-FFG cannot enter in any material contract in the name of the company without the consent of the shareholders. Furthermore, in the event that shareholders’ approval cannot be obtained on time, the executive directors may directly take a decision for urgent matters in agreement with the chair of the board of BVG (not acting in its capacity as shareholder). The shareholders’ meeting has the obligation to approve the decision taken by BVG afterwards. This provision is rather theoretical by nature, since BVG is the sole shareholder.

BVG-FFG is also only allowed to act for BVG. It must not act in the name of others, or provide services to other units than BVG. The domination agreement, in particular, restricts the decision-making autonomy of BVG-FFG. It stipulates that BVG has the right to issue directives of any kind to the management of BVG-FFG. Any directive issued by BVG has to be followed by the executive directors of BVG-FFG if it does not contradict the law.

Beyond these provisions, BVG is also allowed to inspect the books and documents of BVG-FFG at any time, and BVG-FFG has the obligation to monthly inform BVG about all actions taken with regard to the financing of the acquisition of rolling stock for BVG.

Furthermore, any operating profit has to be forwarded to BVG, while BVG has to guarantee the liquidity of BVG-FFG.

As a result, BVG-FFG cannot be considered as an institutional unit and should be classified with its parent company, i.e. BVG.

Parent of BVG-FFG

Once it is concluded that BVG-FFG seems to be an entity lacking autonomy of decision in the meaning of ESA2010, one needs to clarify which institutional unit is it's “parent”, i.e. the unit with which BVG-FFG accounts will be aggregated for the purpose of statistical reporting. This step of establishing which institutional unit is the parent of an entity that is not an institutional unit is often described as determining which unit controls that entity (see Diagram 20.1 of ESA 2010 Chapter 20).

While it is indisputable that BVG-FFG is publicly controlled, one may wonder whether the parent is the Land of Berlin itself (through financing) or BVG (through ownership).

ESA 2010 2.36 stipulates, "*a single institutional unit […] secures control over a corporation or quasi-corporation by owning more than half the voting shares or otherwise controlling more than half the shareholders' voting power."* In the case of BVG-FFG, BVG is the only shareholder in the company, and therefore the owner of the majority of voting interest.

The control criteria stated in ESA 2010 20.309 include the following:

"(a) rights to appoint, veto or remove a majority of officers, board of directors etc. […]"
"(c) rights to appoint, veto or remove a majority of appointments for key committees of the entity. […]"
"(d) ownership of the majority of the voting interest. […]"
"(f) rights to control via contractual agreements. […]"

BVG satisfies the criteria mentioned above. The executive directors of BVG-FFG have to be chosen from the ranks of the executive members of staff of BVG. BVG is the sole shareholder in the company and also the sole client, as BVG-FFG is prohibited to act for other clients than BVG.

At the same time, financing is also a criterion of control (ESA 20.309(g)), and as such, the Land of Berlin may be seen, indirectly, as the parent of BVG-FFG, rather than BVG. However, there is no financing commitment of the Land of Berlin in favour of BVG-FFG. The only commitment given by the Land of Berlin is in favour of BVG (through investment grants), which ultimately benefit indirectly to BVG-FFG.

Given that, BVG-FFG is a mere financial vehicle with limited autonomy (as analysed by DESTATIS), and given the statistical treatment envisaged for the BVG-FFG borrowing (see below), Eurostat sees no objection to concur with DESTATIS' opinion that the parent of BVG-FFG is BVG.

Statistical treatment of the loans and of the investment grants

According to the financing model already described, BVG-FFG takes out, in its own name, loans to finance the acquisition of the rolling stock. These funds are forwarded in the form of loans from BVG-FFG to BVG. The funds are solely used to finance the acquisition of the rolling stock. The financing needs covered by the borrowed funds are supplemented by investment grants committed by the Berlin government to BVG.

In line with ESA 2010 paragraphs 20.222 and 20.224[1], and especially as a result of the analysis of the information provided by you, Eurostat considers that the grants provided by the Land of Berlin to BVG are to be recognised as a government support/gift (following ESA 2010 paragraphs 4.164 and 4.165 (f)) aimed at improving the economic sustainability of the BVG's debt level and not as investment grants. Especially that the payments are closely related to the borrowing schedule and do not, as prescribed in ESA 2010 paragraph 4.155, have a form of a lump sum payment or instalments aimed at covering capital formation carried out during an earlier period. Consequently, in this particular case, the grants should be recognised as a debt assumption of part of the loans taken out by BVG-FFG. This should lead to the recording of the part of the payments by the Land of Berlin as a capital transfer (D.99) and part as an investment grant (D.92).

The maximum amount of the debt to be assumed (capital transfer to be recorded in the accounts of the Land of Berlin) should be equal to the difference between the total value of investments in rolling stock planned in the service agreement less the forecasted maximum amount of financing recorded as debt in the accounts of BVG-FFG.

[1] In contrary to ESA 2010 paragraph 20.222, ESA 2010 paragraph 20.224 handles the debt payment by one unit on behalf of another unit, leading only to a partial debt assumption.

The loans taken out by BVG-FFG are only incurred to finance the investment in fixed capital of BVG. Due to this predefined use of funds, and in combination with the contractual commitment of the Land of Berlin to provide investment grants, Eurostat considers that the time of recording of the debt assumption, in this case, would be the time at which each individual loan is taken out. The reason for this is that it is already predefined that the loans will only be used for the acquisition of rolling stock and that the Land of Berlin has already entered into the obligation for the payment of the investment grants.

This leads to the recording of the debt assumption at the moment when the loans are taken out by BVG-FFG every year for the total loan amount. However, the maximum amount to be recorded as the debt assumption is equal to the difference between the total investment in rolling stock and the maximum amount recorded as debt in the accounts of BVG-FFG less the already paid out investment grants, reducing the maximum amount still to be paid.

Consequently, the recording of government expenditure will be split into two phases. In the first years, government expenditure equal to the amount of debt assumed has to be recorded as a capital transfer (D.99), while in the second phase, government expenditure equal to the remaining payments to the BVG has to be recorded as investment grants (D.92) up to the maximum amount of investment grants provided by the Land of Berlin. Starting with the second phase, the assumed debt will be amortised with the last payment extinguishing the assumed debt in government accounts. The detailed recording of the imputed debt and of the investment grants, based on the provided financing information specific to BVG is presented in the annex.

Sector-classification of BVG

Another issue concerns the sector classification of BVG itself.

BVG is established as an "Anstalt öffentlichen Rechts" (institution under public law). It seems to fulfil the "autonomy of decision" criteria under ESA 2010 2.12 and can therefore be considered an institutional unit. The unit is controlled by government (the only shareholder).

The market/non-market delineation is, in a first step, assessed along the so-called qualitative criteria, notably in accordance with ESA 2010 20.27, for the services provided under the monopoly of BVG, and ESA 2010 20.28, for the services provided in competition with private corporations. For the areas in which BVG competes with private service providers, contracts are awarded on the basis of a tendering procedure, seemingly satisfying ESA 2010 20.28. Concerning the monopolistic output, it is sold to both, households and government, where the share of output sold to government consists of reductions in ticket prices based on social criteria. The share of sales to non-government units greatly exceeds 50% of total sales.

With regard to the quantitative criterion, the sales figures used for the computation of the market/non-market test include neither any of the significant current or capital transfers made by the Land of Berlin to BVG, nor the amortisation of investment grants received from the Land of Berlin (and booked as revenue in the profit and loss accounts of BVG). However, included in the sales component are revenues stemming from advertising and other revenues (e.g. revenues from renting operations). An important component of the test is the "output sold to government", i.e. the reductions in ticket prices based on social criteria. Approximately one eighth of total sales originate from these reductions. These payments are directly linked to the social purpose and are classified by DESTATIS as social transfers in kind (D.632). Because any operator of public transportation services in Berlin may benefit from such payments provided by the Land of Berlin, this choice made by DESTATIS appears legitimate. If it was not the case, the payments would need to be excluded from the test. In view of the near monopolistic status of BVG in the public transportation sector in Berlin, it may be nonetheless difficult to genuinely assess this condition. Consumption of fixed capital – cost component in the test – is approximated by using depreciation of fixed assets observed in the financial statement of BVG, weighted by a multiplier of 1.5, as is common practice of the Statistische Bundesamt. It is also believed that the rolling stock, including the portion financed through investment grants, is recorded as fixed assets. The depreciation is recorded as expenditure in the profit and loss account. The investment grants are recorded as liability and the recorded amortisation as revenue.

The sales to production costs ratio of BVG remained for the years 2014-2017 above 50%. Based on the results of the market/non-market test, BVG is currently classified in the non-financial corporations sector (S.11).

This said, Eurostat draws the attention of DESTATIS to the fact that BVG meets the 50% criterion but hardly by a significant margin, which, coupled with the fact that BVG can fund its investments only based on a long term contract with the Land of Berlin, may seem to be pointing to a borderline case. The increasing intertwining between BVG and the Land of Berlin together with BVG quasi-monopoly position may put a question mark on its market character, in the meaning of ESA 2010, if not on its autonomy of decision (although the wording of certain conditions in the letter of intent might raise doubts in this respect). Accordingly, Eurostat encourages DESTATIS to closely monitor future developments in this respect.

3. CONCLUSION

The combined provisions in the legal documents clearly constrict the BVG-FFG in a way that it cannot be considered to have any autonomy of decision regarding its main function. The main function of BVG-FFG is the provision of funds to BVG, which, not only has to agree to all operations, but also has the right to issue obligatory directives. Therefore, BVG-FFG is not an institutional unit and has to be classified with its controlling unit.

Based on the legal documents provided and the fact that BVG is the sole shareholder in BVG-FFG, BVG seems to be the plausible parent of BVG-FFG.

Since BVG-FFG cannot be seen as an institutional unit and BVG is its parent, BVG-FFG has to be classified with its parent institution, BVG, which is currently classified in the sector S.11.

Given the agreement between the Land of Berlin and BVG (letter of intent) stating that the Land of Berlin will provide substantial investment grants enabling BVG to service the loans incurred by BVG-FFG, the latter have to be considered as a debt assumption by the Land of Berlin at inception (i.e. at time of loan drawdowns) for an amount equal to the difference between the total investments in rolling stock less the maximum amount of debt recorded in the accounts of BVG-FFG. The sum of debt assumption (first phase) and of investment grants (second phase) should be equal to the total amount of grants agreed between BVG and the Land of Berlin in the service agreement.

4. PROCEDURE

This view of Eurostat is based on the information provided by the German authorities. If this information turns out to be incomplete, or the implementation of the operation differs in some way from the information presented, Eurostat reserves the right to reconsider its view.

We would like to remind you that Eurostat is committed to adopting a fully transparent framework for its decisions on debt and deficit matters in line with Council Regulation 479/2009 and the note on ex-ante advice, which has been presented to the CMFB and cleared by the Commission and the EFC. Eurostat therefore publishes all official methodological advice (ex-ante and ex-post) given to Member States, on the Eurostat web site.

Yours sincerely,

(eSigned)
Mariana Kotzeva

Annex

Annex

Recording of government expenditure and debt assumption	Debt assumption	Loans taken out by BVG	Annual debt assumtion (new loans taken out by BVG up to the limit of debt to be assumed) = (D.99)	Total debt imputed to government balance sheet	Investment grants to be recorded as (D.92)	Amortisation of assumed debt (F.4)	
Total investments in rolling stock	3,186.0						
Maximm debt incurred by BVG	2,363.5						
Debt to be assumed	**822.5**						
Total investment grants approved	1,342.8						
2020		81.8	81.8	81.8	0.0		**increase of imputed debt**
2021		59.1	59.1	140.9	0.0		
2022		127.9	127.9	268.8	0.0		
2023		189.1	189.1	457.9	0.0		
2024		225.2	225.2	683.1	0.0		
2025		339.7	139.4	822.5	0.0		
2026		197.3			90.0	-90.0	**amortisation of imputed debt**
2027		193.0			90.0	-90.0	
2028		196.2			90.0	-90.0	
2029		85.3			90.0	-90.0	
2030		255.9			90.0	-90.0	
2031		44.5			70.3	-90.0	
2032		10.2			0.0	-90.0	
2033		18.0			0.0	-90.0	
2034		0.0			0.0	-90.0	
2035		0.0			0.0	-12.5	
total B.9			**822.5**		**520.3**		
Total debt imputed (AF.4)				**822.5**		**-822.5**	