



CMFB WORKSHOP ON THE CLASSIFICATION OF DEVELOPMENT BANKS

Next steps in the statistical framework – rearranged transactions

Malgorzata Szczesna-Rundberg
Directorate D – Government finance statistics (GFS) and quality

CMFB Workshop – ECB Frankfurt am Main
13 November 2018

Statistical issues in EDP/GFS

- **In which sector should a development bank be classified?**
 - General government sector
 - Financial corporations sector
- **Are some activities of a development bank should be recorded in government accounts?**
- **Rearranged transactions**
 - Government is at the origin of some transactions
 - Bank is entrusted by government to perform tasks which contribute to the implementation of specific government policies/interventions

Why do we rearrange transactions?

- Rearrangement is recording of a transaction/program in government accounts even if it was carried out by a development bank
- *Rearranged transactions* are recorded to "**bring out the underlying economic relationships more clearly**" (ESA2010, 1.72)
- Current MGDD provides already some guidance on rearrangement
- No special rules for development banks; the same guidelines are applicable to all financial and non-financial corporations
- **On-going methodological work on more extensive guidance on rearrangement of transactions**

When do we rearrange?

When a development bank is:

- I. Acting as a '**government agent**' or at **government request** with regard to a specific transaction/program
- II. Sharing with government '**exposure to risk and rewards**' with regard to a specific transaction/program
- III. Carrying out a **non-market transaction/program**

I. Bank acts as a 'government agent' or at government request

What is considered as a government request?

- **Government request** is an instruction that results in limiting the operational autonomy of the bank with regard to the specific transaction/program or government influences the day-to-day management of a transaction/program
- General mandate given by government to the entity in its role as an owner (on general policy and/or strategy) **is not** considered as a request

What is meant by acting as 'government agent'?

- Following the request, government takes all the risks and rewards from the specific transaction/program: a bank acts as 'accounting tool' for government, which is often reflected in its annual report (through separated accounts)

What indicates the government request?

- a) There is evidence that **government has requested** the bank to carry out the specific transactions through instruction (decree, formal letter, official statement, decree) or any other evidence – statements in annual reports (of units concerned, of supervisory authorities, of auditors)
- b) Government predetermines most of **terms of a transaction or a program** (e.g. interest rate, individual beneficiaries, loan amounts, etc.) such that the bank's ability to effectively influence the contracts becomes negligible
- c) Government representatives constitute **the majority of members in investment committees of the bank** deciding on the specific transaction (persons representing the executive, legislative or judicial government powers)

II. Bank shares with government 'exposure to risk and rewards'

- A development bank acts for government taking **no or minor risks but it is interested in getting the rewards**
- Government provides **the general framework** of a transaction/program and it does not impact the day-to-day management of a transaction (e.g. by a specific request)
- Bank shows high **involvement in implementation of a transaction** and it has incentives to perform at best (to get rewards in form of a larger operating margin)
- Usually, government takes over risks through the existence of dedicated **guarantees**

What indicates 'sharing risk and rewards'?

When government imposes the general conditions of a transaction/program **AND** if:

- a) Government assumes substantially **most of the risks and rewards related to a transaction/program**, despite a development bank has legal ownership.
- b) A bank is compensated for **at least half of the losses** arising from the transaction. This is notably the case when transactions are accompanied by additional government guarantees on related assets and/or on liabilities.

III. Bank carries out the non-market transactions

- Government influence does not always have to be demonstrated by the existence of the legal instructions to undertake a specific transaction/program
- In some cases, government influence is recognised **through the mere (non-market/non-commercial) characteristics of the transaction/programme** (in form of subsidies or transfers)

What indicates the non-market transaction?

- The conditions used in the contract between the business partner and the bank are set below the terms usually applied by the entity, **in particular not covering the administration and borrowing cost incurred**
- The contract is fundamentally associated with permanent losses
- The bank enters into rescue operations linked to financial and non-financial institutions with burden is out of proportion to the possible benefits resulting from such operation

Impact on government accounts

- Various statistical impacts possible both on deficit and debt
- Actual impact depends on a specific rearrangement issue as well as on the original recognition in the government source data

Some examples:

- **Impact on debt:** rearrangement/re-routing of loans granted by a development bank at the specific request of government (*if not already recognised in the source data*);
- **Impact on deficit:** re-routing of investment grants to beneficiaries provided at the specific request of government (*if not already recognised as government expense in source data*);

Work in progress

- Ongoing methodological work in cooperation with the statistical community
- Discussions in Eurostat Task Forces and Working Groups
 - Distinction between **sufficient and/indicative** criteria for rearrangement of transactions
 - Implementation details, wording, formulations in order to account for a heterogeneity observed across Member States
 - Practical implications for the recording in the accounts
- **Next step:** EDPS WG meeting in December 2018
- **Aim:** Update of the MGDD chapter related to rearranged transactions foreseen for first half of 2019

Conclusions

- Activities of development banks are challenging area for government statistics as they are strongly oriented towards the interests of government
- On-going work to harmonise accounting practices in the Member States
- Case-by-case analysis

Thank you for your attention!