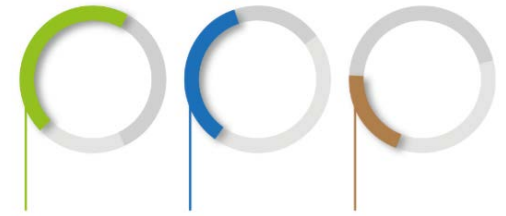
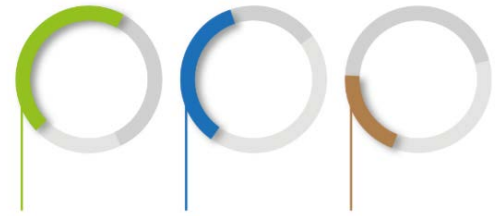


Seminar hosted by the Central Statistical Office, Poland
Warsaw, 28 April 2017



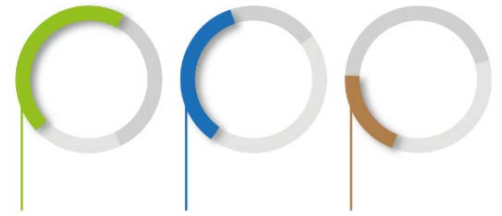
About EPEC

- Established in 2008
- Part of EIB's Advisory Services, EPEC services also accessible through the European Investment Advisory Hub
- A unique cooperative initiative of the EIB, the European Commission and EU Member and Candidate States
- Team of 14 professionals
- **Membership:** now over 40 Members (e.g. PPP Units, Ministries of Finance)
- **Mission:** “to help the public sector deliver better PPPs in Europe”

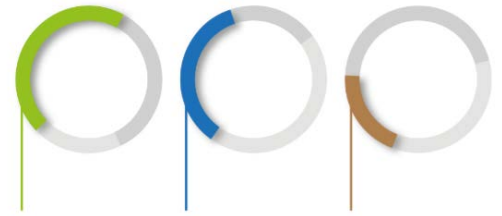


Agenda

- An overview of the Eurostat rules
- PPP stakeholders perception of the Eurostat rules & motivation for producing the Guide
- An introduction to the Guide
- A closer look at the Guide
- Discussion / Q&A

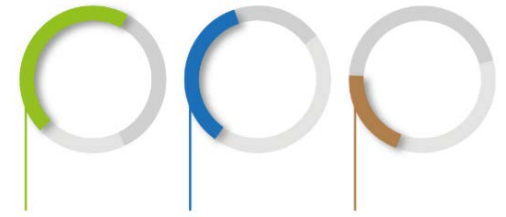


An overview of the Eurostat rules



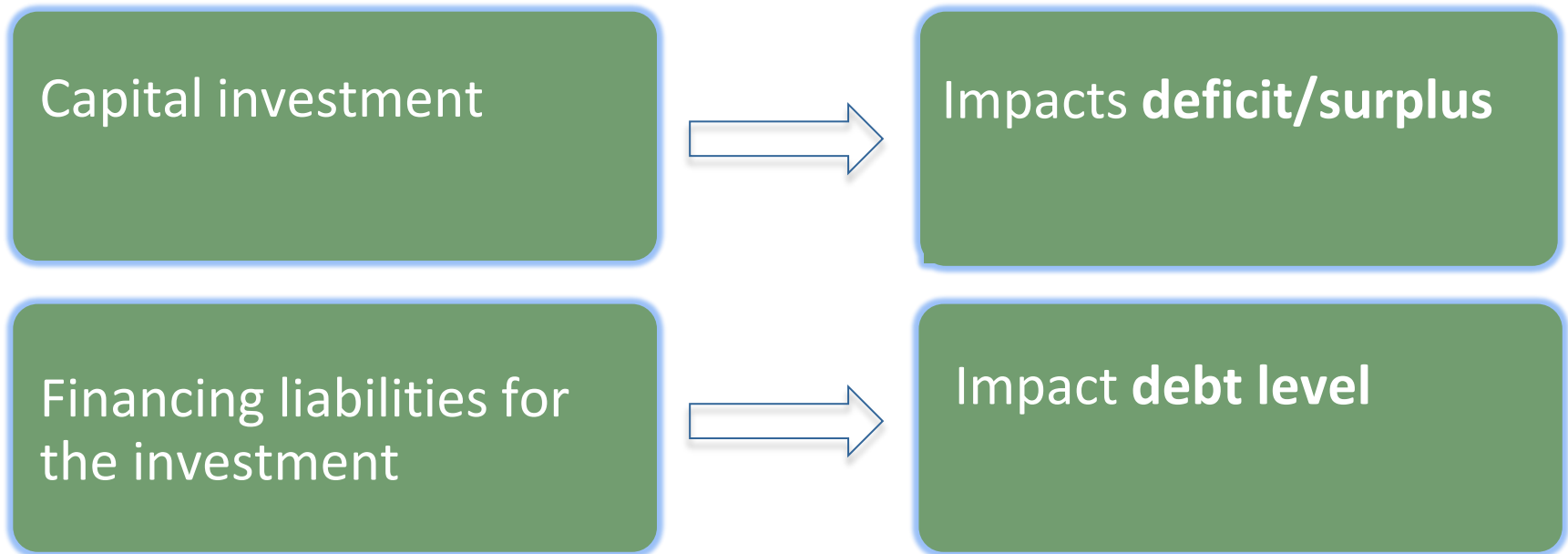
Why are the Eurostat rules important?

- EU controls on levels of government deficit and debt: **Maastricht criteria**
- Who should record PPPs (and concessions) and **how?**
- Issue becomes more critical in an era of **fiscal constraints**
- Eurostat rules relate to **statistical treatment** - not to be confused with accounting rules/practices and budgeting



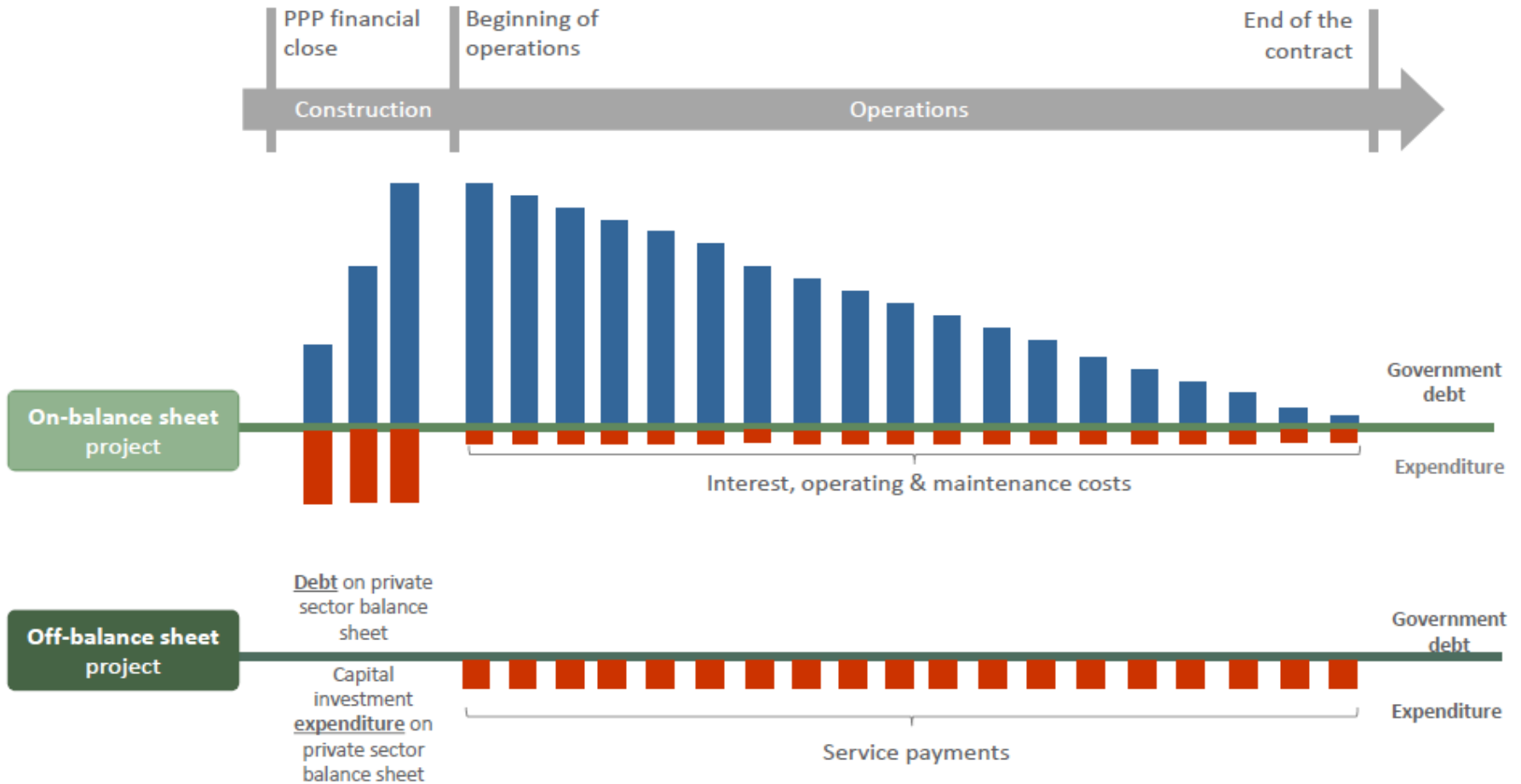
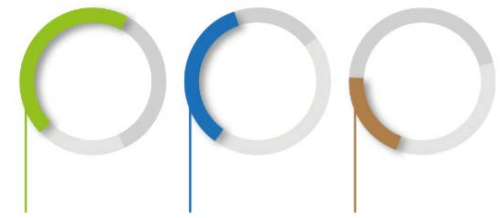
What do the Eurostat rules imply?

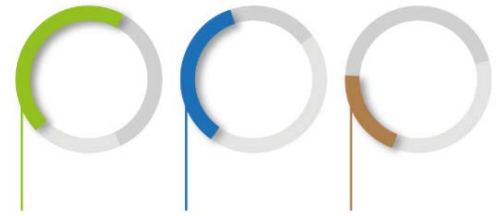
If the asset is “on balance sheet” for government:



If the asset is “off balance sheet” for government then government only records regular payments for services over the long-term

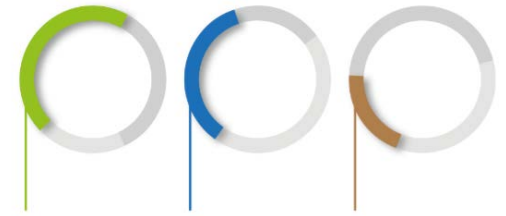
Impact on government deficit and debt





Where are the Eurostat rules?

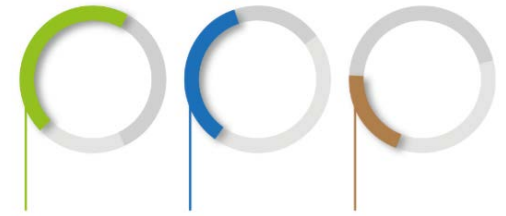
- Overarching methodology for EU economic statistics European System of Accounts (ESA10) of September 2014, replacing ESA95
- Revised Eurostat Manual on Government Deficit and Debt (latest edition dated March 2016)
- Eurostat advice on individual cases – PPP projects in Member States
- And now also in *A Guide to the Statistical Treatment of PPPs...*



What do the rules look at?

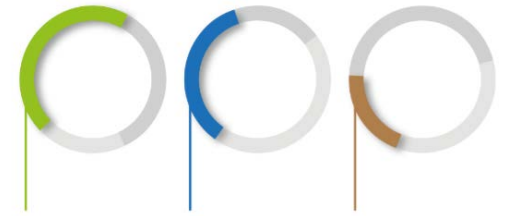
The “economic ownership” of the asset, involving analysis of:

- the parties involved
- the structure of the project
- how the contract allocates risks and rewards between the parties

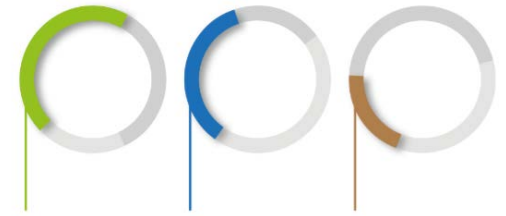


Timing of the statistical treatment assessment

- Assessment is based on the PPP arrangements at financial close and the rules in force at that time
- If the PPP contract arrangements change: assess the change against the rules in force at the time of the change

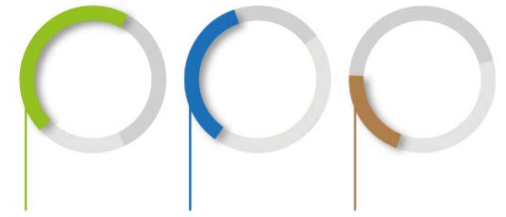


PPP stakeholders perceptions of the Eurostat rules & motivation for producing the Guide

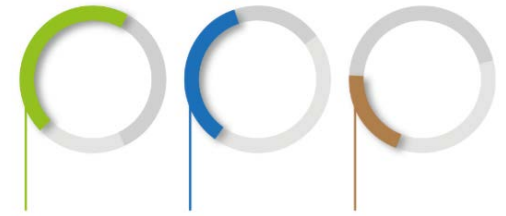


Why produce the Guide?

- Concerns about “Eurostat rules” being an obstacle to PPP deal flow
- Calls for more clarity and stability around the rules
- Acknowledgement that the statistical treatment often plays a key role in decision to procure PPPs
- EPEC/Eurostat response – collaboration to produce a detailed and practical guide

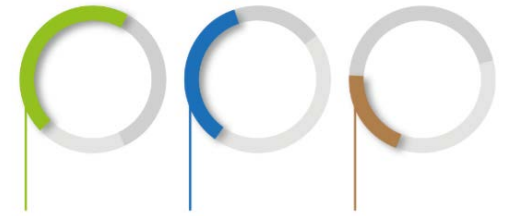


An introduction to the Guide



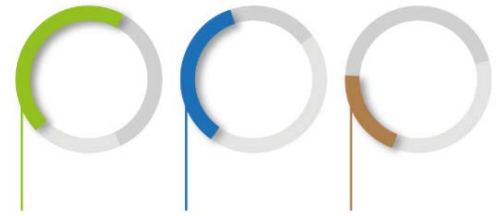
About the Guide

- Aimed (mainly) at public sector PPP stakeholders
- Explains Eurostat's interpretation of the rules and approach to assessing statistical treatment
- Based on existing rules (ESA 2010, MGDD 2016)
- Clarifies (but does not change) the existing rules



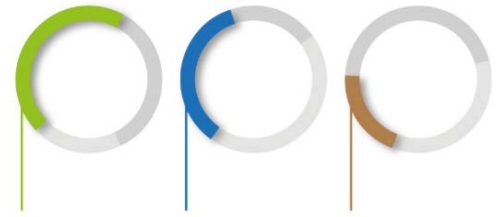
About the Guide

- Applies to PPPs only
 - not concessions
 - not energy performance contracts
- Applies to projects that reach financial close after 29 September 2016

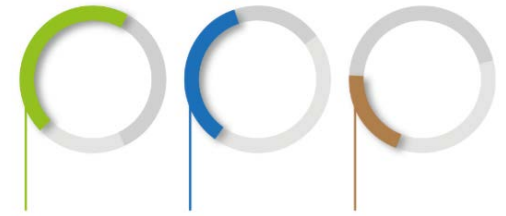


About the Guide

- Constitutes **official Eurostat guidance** and is the reference point for Eurostat advice and decisions on PPPs
- Comprehensive coverage of PPP contract issues will bring **clarity and stability**
- A useful tool for **PPP practitioners and national statistical authorities**

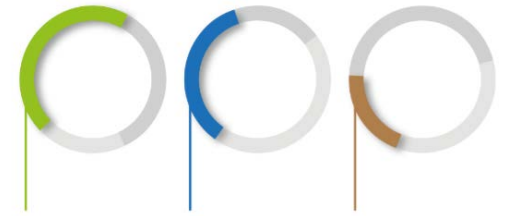


Using the Guide



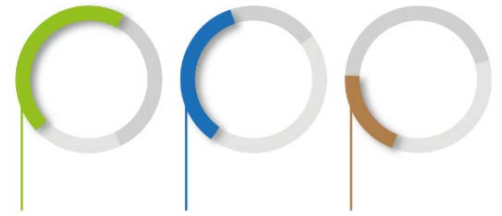
What is the Guide?

- A practical and user-friendly guide on the statistical treatment of PPPs
 - A “contract-feel”
 - Covers typical PPP contract provisions and structures
 - Captures EU-wide market practice
 - As clear and precise as possible on how specific contract provisions affect the statistical treatment



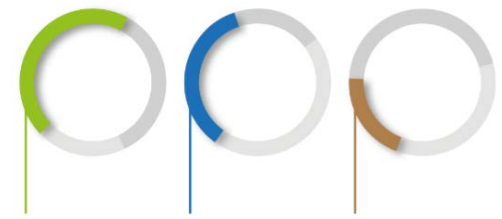
Before you start

- It is detailed and technical and assumes a good working knowledge of PPPs
- It is comprehensive but will not address every detail of every transaction
- Consider substance / commercial impact rather than form
- It should be used as a whole and not in discrete sections
- It does not deal with “value for money” or “bankability”
- On or off balance sheet – fiscal risk needs to be managed



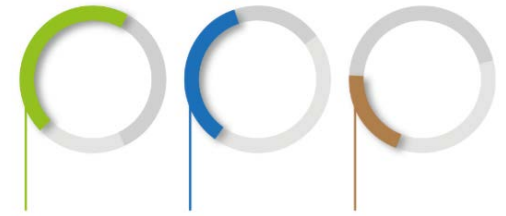
Chapter 2: Is the project a PPP?

- Who are the **parties** involved?
- What is the nature of the **asset** and of the **works**?
- **How long** is the contract for?
- What **services** are included?
- Where do **revenues** flow?



Chapter 3: The influence of PPP contract provisions

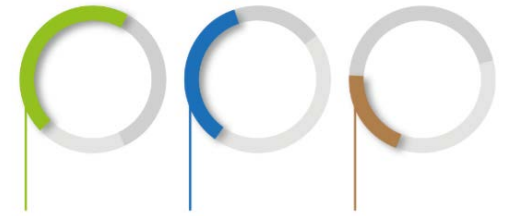
- Theme 1 – The project site
- Theme 2 – Design and construction of the asset
- Theme 3 – Operation and maintenance of the asset
- Theme 4 – The payment mechanism
- Theme 5 – Other payment arrangements
- Theme 6 – Compensation, relief and force majeure events
- Theme 7 – Changes to the PPP contract
- Theme 8 – Changes in law
- Theme 9 – Insurance
- Theme 10 – Warranties and indemnities
- Theme 11 – Early termination of the PPP contract
- Theme 12 – Compensation on early termination of the PPP contract
- Theme 13 – Expiry of the PPP contract
- Theme 14 – Financing arrangements
- Theme 15 – Government influence
- Theme 16 – Miscellaneous provisions



Chapter 3: The influence of PPP contract provisions

Eurostat's comment:

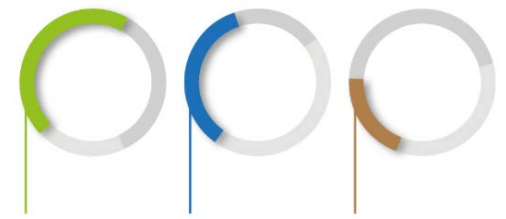
- does not influence
- does influence
 - MODERATE
 - HIGH
 - VERY HIGH
 - ON BALANCE SHEET FOR GOVERNMENT



Chapter 4: Concluding the assessment

Step 1: identify issues that have an influence on the statistical treatment

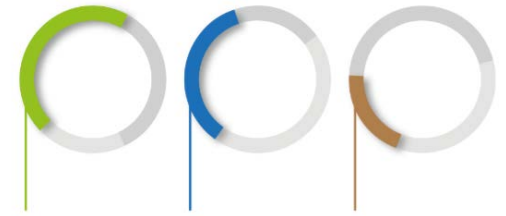
- No influential issues – **OFF BALANCE SHEET**
- Influential (ON BALANCE SHEET) issues – **ON BALANCE SHEET**
- Influential (VERY HIGH/HIGH/MODERATE) issues – **MOVE TO STEP 2**



Chapter 4: Concluding the assessment

Step 2: analyse the significance of the issues identified (and re-categorise if appropriate)

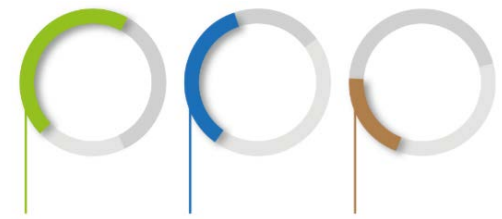
- Project-specific analysis
- In some cases, might lead to **re-categorising** (e.g. a MODERATE importance issue as a HIGH importance issue)
- In **extreme cases** may lead to re-categorising as ON BALANCE SHEET
- **No re-categorising** where specific **thresholds** have been specified (e.g. 20% equity is always MODERATE)



Chapter 4: Concluding the assessment

Step 2 example

- The contract applies **no deductions** for the first 5 years of the operational phase
- The Guide categorises this “grace period” as a **MODERATE** importance issue (Theme 4.7.2)
- The Guide’s reference point for a **reasonable grace period** is **6 months**
- At step 2, given the degree to which this specific project departs from the Guide’s reference point, the issue is **re-categorised** as **HIGH** importance



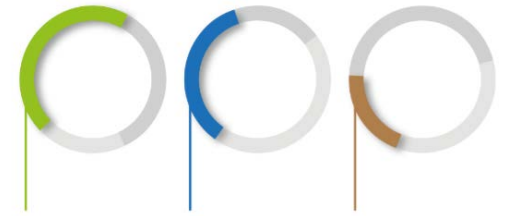
Chapter 4: Concluding the assessment

Step 3: reaching a conclusion

- Strong presumption of OFF BALANCE SHEET treatment if:

	VERY HIGH	HIGH	MODERATE
Issues identified	≤ 1	0	≤ 2
Issues identified	0	≤ 2	≤ 1
Issues identified	0	≤ 1	≤ 4
Issues identified	0	0	≤ 7

- If thresholds are not met, further analysis may be undertaken and will include assessing the Authority's control of the asset

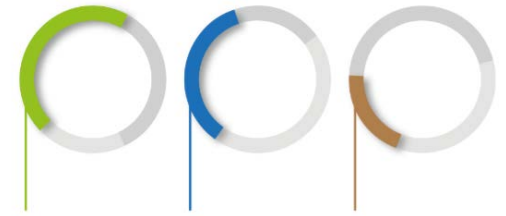


Chapter 4: Concluding the assessment

Step 3 example

- Authority contributes 35% of financing (e.g. capital contribution) – **VERY HIGH** (Theme 14.4)
- Authority takes 20% equity share with profits – **MODERATE** (Theme 15.1)
- Authority third party revenue forecast is 6% of payments to Partner – **MODERATE** (Theme 5.5)

Project is **OFF BALANCE SHEET** for government

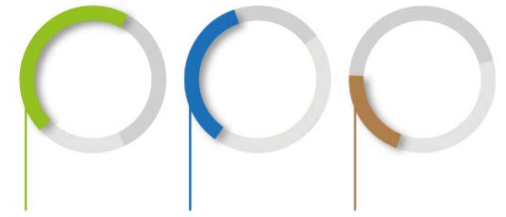


Chapter 4: Concluding the assessment

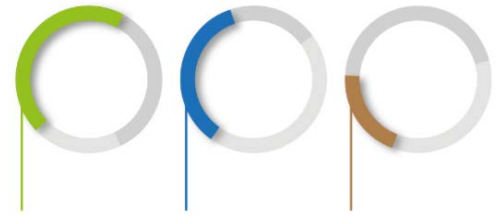
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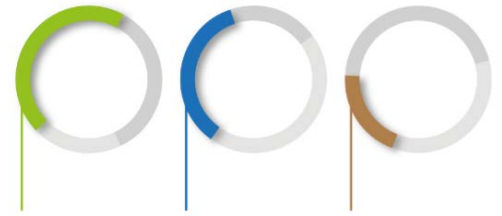
Project is **ON BALANCE SHEET** for government



A closer look at the Guide

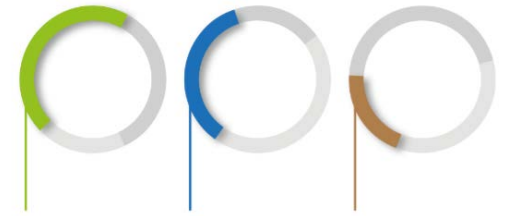


Chapter 2: The Features of a PPP



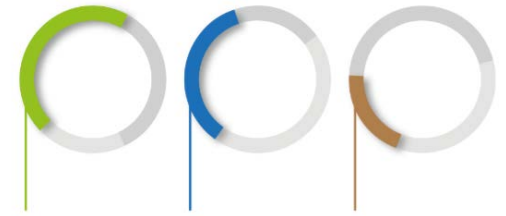
Sector classification of the contracting parties

- Authority must be **public** (government) and Partner must be **private** (non-government)
- General rules (**not PPP-specific**) apply
- Watch for **government control of the Partner** (e.g. through equity, direct government investment instructions to national public banks)
- Different tests for **SPVs** and other entities



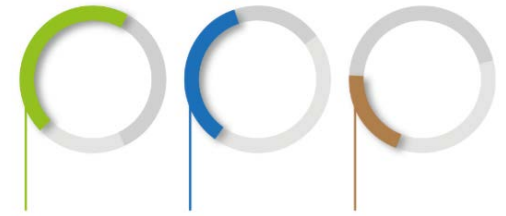
Source of Partner revenue

- Majority Partner revenue from government = PPP
- Majority Partner revenue from users = concession



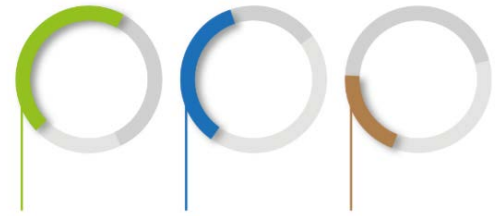
The asset

- Clearly identifiable
- An element of specific design
- **Examples** may include accommodation, roads, bridges, IT systems
- PPP asset may have **interfaces** with other projects/infrastructure
- Value of works relevant on refurbishment, renovation or upgrade of existing assets (**50% rule**)



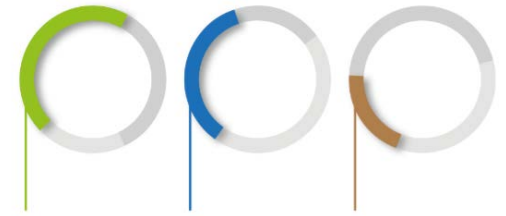
Economic life of asset / contract duration

- Short-term contracts (< 10 years) unlikely to be PPPs
- Asset life should be longer than the contract
- But contract should include major maintenance/ replacement of the asset
- As an indication, operational period > 10 years likely to be a PPP (e.g. roads, accommodation projects)



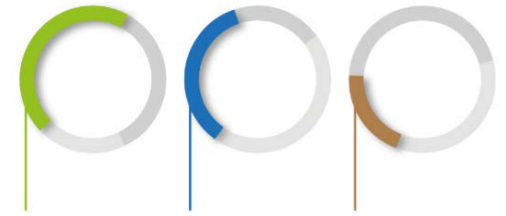
Scope of services provided by the Partner

- Maintenance is the core service for a PPP
- Inclusion / exclusion of **secondary services** (e.g. cleaning, catering) does not affect whether a project is defined as a PPP

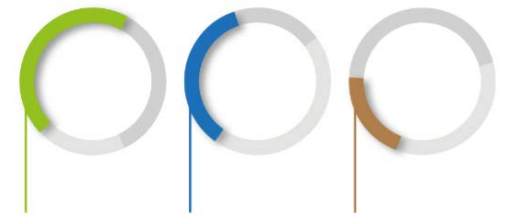


Government revenues from the project

- Government revenues > 50% government payments, the project is not a PPP
- Test applied at financial close (use best estimates) AND reviewed throughout the contract life
- Applies to all types of third party revenue (e.g. road user charges, out of hours use of schools)
- Does not catch purely internal government funding arrangements (e.g. central government funding for school pupils received by local government)

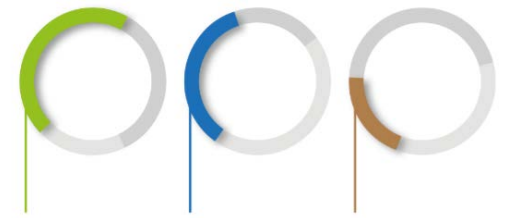


Chapter 3: The PPP Contract (some examples)



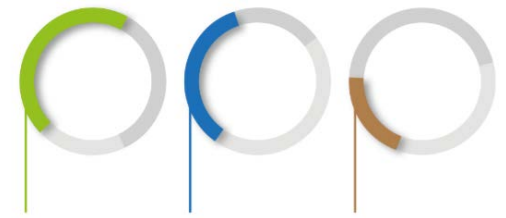
Theme 2 – Design and construction of the asset

- Completion criteria → objective and robust
- Phased completion → “useable” phases linked to proportional Operational Payments
- Snagging → minor issues only (not availability-related)
- Links to Theme 5 (Payments) and Theme 6 (Compensation, Relief and Force Majeure Events)



Theme 3 – Operation and maintenance of the asset

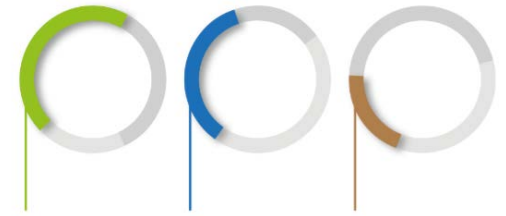
- Core maintenance service (Partner) vs “secondary services” (Partner or Authority)
- Operation and maintenance standards → genuinely linked to the asset being useable; monitored/applied through the contract
- Maintenance costs → risk/reward must sit with the Partner



Theme 4 – The payment mechanism

Availability-based

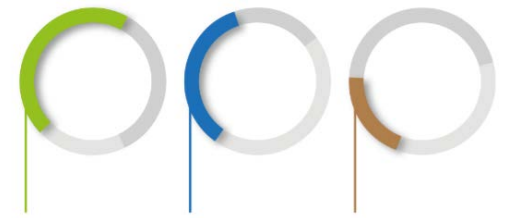
- An effective availability regime → genuine availability standards and appropriate levels of deductions
- Deductions → calculated objectively and not open to negotiation
- Proportionality →
 - full availability = full payment
 - zero availability = zero payment
 - in between = broad proportionality



Theme 4 – The payment mechanism

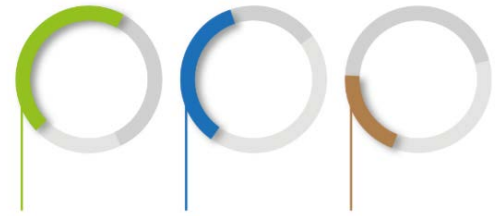
Demand-based

- Banding mechanisms affect the principle of proportionality
- Minimum revenue/use guarantees (any amount) →
ON BALANCE SHEET



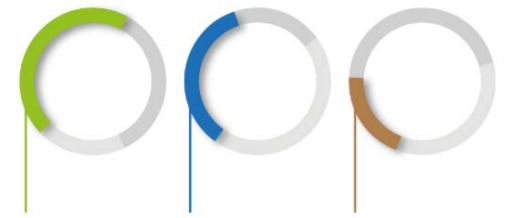
Theme 5 – Other payment arrangements

- Payment commencement → asset is available for use
- Third party revenues received by the Authority/government
 - > 50% of payments to Partner = on balance sheet (Ch. 2)
 - ≥ 20% of payments to Partner = HIGH importance
 - < 20% of payments to Partner = MODERATE importance
 - < 5% of payments to Partner = no influence



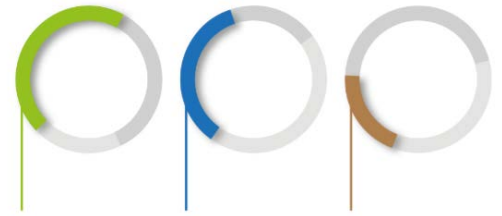
Theme 6 – Compensation, relief and force majeure

- The **list of events** → finite and events well-defined (no “or similar” catch-all provisions)
- Some **due diligence is expected** (the occurrence of the event, or its consequences, must not be reasonably foreseeable)
- Events should **exclude acts/omissions of the Partner**
- Special attention given to **public law doctrines** (e.g. economic re-balancing)



Theme 12 – Compensation on early termination

- Market value of the contract (set through re-tendering or estimated) can be used for Partner default compensation (detailed conditions apply)
- Other methods of calculating Partner default compensation (e.g. book value, senior debt) → might influence
- Force majeure compensation → should be lower than full compensation for Authority default / Authority voluntary



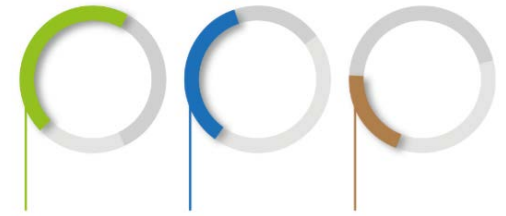
Theme 13 – Expiry of the PPP contract

Asset returns to the Authority for no payment
→ no influence if:

- Operational Phase > 10 years

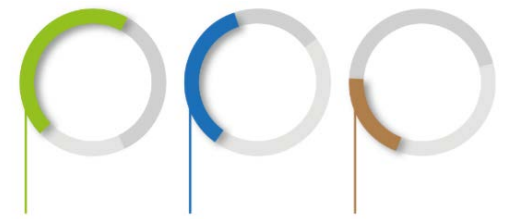
AND

- The Partner is forecast to recover its investment/lifecycle costs over the life of the contract



Theme 14– Financing arrangements

- Relevance of government financing defined by specific thresholds applied to total construction cost:
 - $\geq 50\%$ = on balance sheet
 - $< 50\%$ but $> 1/3$ = VERY HIGH importance
 - $\leq 1/3$ but $> 10\%$ = HIGH importance
 - $\leq 10\%$ = MODERATE importance
- Apply 2.5 multiplier to highest-risk finance and a sensible multiplier to finance between lowest and highest risk

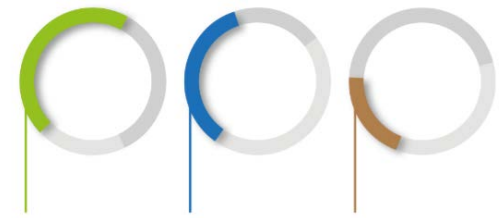


Theme 14– Financing arrangements

- Authority can have rights of approval/veto over refinancing
 - Subject to reasonableness
 - No right to force a refinancing
- Authority can share in refinancing gains
 - Authority takes share generated by its actions

OR

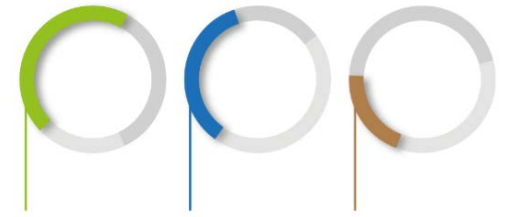
- Authority take a specified % share (fixed no higher than 1/3)



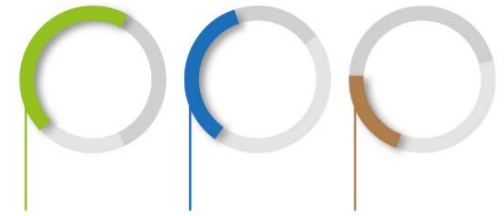
Theme 15 – Government influence

Government equity → 3 issues to consider:

- Control → Partner classification issue (Chapter 2)
- Capital invested → government financing (Theme 14)
- Profit share → government reward (Theme 15)
 - ≥50% = on balance sheet
 - <50% but >1/3 = VERY HIGH importance
 - ≤1/3 but >20% = HIGH importance
 - ≤20% but >10% = MODERATE importance
 - ≤10% = NO INFLUENCE



Concluding remarks & questions



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<http://ec.europa.eu/eurostat/help/support>