IMF Committee on Balance of Payments Statistics

*BPM6* Update
Direct Investment Task Team (DITT)

**Approved/Final Version**

# D.8 Public-Private Partnerships

## D.8 Public-Private Partnerships[1]

*Cross-border Public Private Partnerships (PPPs) have increasingly become one of the prominent modes of financing public infrastructure in several economies. While the* Balance of Payments and International Investment Position Manual, sixth edition*, uses the same definition of PPPs presented in other international statistical standards, regarding direct investment (DI), it only states that a nonresident private unit involved in this arrangement may be a direct investor when a production unit, a branch (that is, a direct investment enterprise, is created when this investment has substantial operations over a significant period in the host territory. There is no other specific guidance on the treatment of cross-border transactions and positions of these PPP arrangements involved in a DI relationship. Given the significance of these arrangements in many economies and the need to ensure consistency in the treatment by compilers across macroeconomic statistics, this note recommends the development and inclusion of guidance in the balance of payment manual, preferably in an appendix, on the concepts, definitions, scope, and statistical treatment of PPPs under DI.*

### SECTION I: THE ISSUE

#### BACKGROUND

1. **Public-Private Partnerships (PPPs) are increasingly becoming one of the prominent modes of financing public infrastructure projects in a number of economies.** The number of PPP projects globally is estimated to have grown to over 6.4 million[2] by 2020 from 1984. PPPs to developing countries averaged US$79 billion per annum between 2007–2011 from about US$30 billion between 2002–2006, and PPPs have spread across the globe with over 134 developing countries implementing new PPP projects in infrastructure alone.[3] However, the magnitude of PPPs in direct investment (DI) is not known.

2. **In the international statistical guidance, PPPs are defined as long-term contracts between two units, whereby one unit acquires or builds an asset or set of assets, operates it for a period, and then hands the asset over to a second unit.** This definition is presented in the *Balance of Payments and International Investment Position Manual, sixth edition (BPM6*) (paragraph 4.111), and other macroeconomic statistics manuals.[4] Such arrangements are usually between a private corporation, resident or nonresident, and a government, but other combinations are possible, with a public corporation as either party or a private nonprofit institution as the second unit. For easy reference, the second unit will

[1] Prepared by Mr. Wilson Phiri (Bank of Zambia), Ms. Rita Mesias and Mr. Bruno Rocha (both IMF), and Mr. Piet Swart (South African Reserve Bank).

[2] Private Participation in Infrastructure Database.

[3] World Bank Group Support to Public-Private Partnerships Lessons from experience in client countries, FY02–12.

[4] *External Debt Statistics: Guide for Compilers and Users* (*2013 EDS Guide*, Appendix 1), the *Government Finance Statistics Manual 2014* (*GFSM 2014*, paragraph A4.58), the *Public Sector Debt Statistics: Guide for Compilers and Users* (*PSDS Guide*, paragraphs 4.120), the *System of National Accounts 2008* (*2008 SNA*, paragraph 22.154), and the *European System of Accounts 2010* (*ESA 2010*, paragraph 15.41). The World Bank presents a definition of PPPs as does Eurostat's *Manual on Government Deficit and Debt* and *A guide on the Statistical Treatment of PPPs*; see these definitions in Annex I. Annex I also presents a Typical PPP Project Structure and Funds Flow graphic.

be referred to as the private corporation. These schemes are referred to by different names depending on the type of contracts that are in place.[5]

## CURRENT STATISTICAL TREATMENT OF PPPs

### *Economic Ownership of the Asset*

3. **The statistical treatment of PPPs transactions and positions depends on the economic ownership of the asset(s)[6] involved, but the decision about economic ownership of the asset(s) and whether to record PPP-related assets and liabilities in the government's or the private corporation's balance sheet is not straightforward.** Typically, the assets have service lives much longer than the contract period so that, for this reason alone, the government will control[7] the assets, bear the risks, and receive the rewards for a major portion of the assets' service lives. Thus, it is frequently not obvious whether the private corporation or the government owns the assets over their service lives or which party bears most of the risks and benefits from the majority of the rewards.[8] Annex II describes the current statistical treatment of PPPs based on the guidelines in the *System of National Accounts 2008 (2008 SNA).*

### *PPPs in Balance of Payments, International Investment Position (IIP) and External Debt Statistics (EDS)*

4. **The *BPM6* only provides limited references to the economic ownership of the asset, and a treatment akin to financial leases is "adopted" for some PPPs.**[9] In paragraph 4.111, the *BPM6* indicates: "As with leases, the economic owner of the assets related to such an arrangement is determined by assessing which unit bears the majority of the risks and which unit is expected to receive a majority of the reward of the assets."

5. **If the private sector corporation is a nonresident, it is recommended the classification of the positions as external debt depending on who is the economic owner of the fixed asset during the contract period and the nature of the contract** (see *EDS Guide 2013*, Appendix 1). Detailed advice

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[5] Examples are private finance initiatives (PFIs); design, build, operate, and transfer schemes (DBOT); build, own, and transfer schemes (BOTs); or build, own, operate, and transfer schemes (BOOTs). For ease of reference, the remainder of this section will refer to PPPs.

[6] Annex III includes some criteria for determining the economic ownership of PPP-related assets (see Box A4.4 in *GFSM 2014*). While it is not possible to prescribe rules applicable to every PPP type of arrangement, the considerations presented in this annex should guide the decision on which party is the economic owner of the asset(s) during and at the end of the PPP contract period.

[7] The International Public Sector Accounting Standards Board (IPSASB)'s *Handbook of International Public Sector Accounting Pronouncements* uses a "control approach" to determine the ownership of the asset while statistical international standards use the "risk and rewards approach" (see paragraphs BC5.13–14). The risks and rewards approach was adopted in the *2008 SNA* and *GFSM 2014*, because at the time there was no accounting standard available for PPPs. Additional discussion on this issue, see a recent IMF publication on PPPs: "*Mastering the Risky Business of Public-Private Partnerships in Infrastructure* (imf.org)."

[8] The *Manual on Government Deficit and Debt*, implementation of *ESA 2010* (*MGDD*) presents an extensive assessment of risks and reward to determine the PPPs' asset ownership, see section 6.4.

[9] For example, a build, own, operate, transfer (BOOT) scheme could be found to assign the risks and rewards of ownership to the government, so the private partner would be treated as a provider of a financial lease.

on different treatment arrangements, with numeric examples, is provided in the *PSDS Guide* paragraphs 4.123–4.126; and additional information in the *GFSM 2014* paragraphs A4.64–A4.65. Annex III reproduces some general principles for recording PPPs in external debt. None of the international statistical standards include references for the statistical treatment of PPPs under direct investment (DI) despite demand from users for such information. The *BPM6 Compilation Guide* (*BPM6CG*), however, refers to production sharing agreements (PSAs),[10] and DI (see Chapter 10, Box 10.1) that introduces some elements for assessing the relationship between PPPs and DI. The *BPM6CG* provides broad guidelines on adapting the *BPM6*-based guidelines for determining the nature of cross-border transactions and positions, in the context of PSAs. The guidelines for the compilers include the following:

- *Identify* the operating company and establish the existence of a DI relationship between the operating company and its foreign owner(s). The government agency may not be the operating company.
- *Create* an artificial production unit; this unit may be identified as a branch when a nonresident unit has substantial operations over a significant period in the host territory, but no separate legal company is established for those operations. Each branch is a direct investment enterprise (DIE).
- *Establish* the direct investor. In the case where the contracting parties comprise a single foreign investor and the government, the former is the direct investor.
- *Identify* the rights of contracting parties with regard to participating interests that are usually linked to shares in profit production (or profits). These participating interests, from a statistical viewpoint, do not provide the criteria for determining a DI relationship.
- *Record* the direct investor's share in the financial account, under DI, equity and investment fund shares.

6. **The existence of a production unit, a branch, or other type of unit is an important element in applying the *BPM6* guidance for determining the statistical treatment of PPPs in DI.**[11] For example,

- *If a foreign firm is not considered the economic owner of the asset* and if the external operations of a construction enterprise are substantial enough, they constitute a branch resident in the economy of operations. Therefore, a large-scale construction project contracted by a nonresident enterprise that takes a year or more to complete will usually give rise to a resident branch (*BPM6CG,* paragraph 12.93). Accordingly, there would be a DI relationship between the parent (direct investor) and the branch (DIE).
- *If the foreign firm/investor is considered the economic owner of the asset, this might require the creation of a notional unit (DIE)* so that the notional unit owns the immobile, nonfinancial asset, like land or a building, and then the foreign investor (direct investor) owns the notional unit; this is done to comply with the requirement in the SNA that land is always owned by a resident (with the only exception being for territorial enclaves like embassies, consulates, and military bases).

[10] PSAs are arrangements between a government and investors that govern exploration and production rights.

[11] An example of a PPP that includes a DI relationship is in airports. For example, Malaysian airport holdings has a stake (11%) in Hyderabad airport India along with a local private corporation (63%) and the government (26%).

7. **This note therefore presents the definition of PPPs arrangements, describes current frameworks for the statistical treatment of PPPs arrangements included across different international standards, and presents some elements to consider for the classification of PPPs arrangements under DI relationship.** With the recognition by the authoring group of this note that the methodological framework of DI remains relevant for the treatment of PPPs arrangements under DI relationship, this note examines areas that need further methodological guidance and clarifications.[12]

## ISSUES FOR DISCUSSION

### *Issue 1—Methodological Framework for Recording PPPs Arrangements under DI Relationship*

8. From the preceding, it is evident that the treatment of PPPs does not require change in the core framework of DI statistics or external sector statistics (ESS). However, additions and clarifications are needed to bring concepts, definitions, and scope of PPPs arrangements present in other statistical frameworks, mainly government finance statistics (GFS) and national accounts, for the appropriate classification of PPPs transactions and positions in ESS, including DI. The additional elements to consider could be the following: (i) sectoral classification of the government unit participating in the PPP (for instance, only units of the general government); (ii) type of the asset, for instance assets that are public assets; (iii) use of the asset, for example assets that will be used for public services; (iv) the type of unit that will mainly cover the payments for the services provided by assets involved in PPPs, for example if the government or users; (v) the relevance of distinguishing PPPs from concessions (see Annex I); (vi) the presence of Special Purpose Vehicle (SPV),[13] or other units, in PPPs; and (vii) the relevance of the information in the PPPs contracts for an adequate classification of flows and stocks of these arrangements.

9. The options to address this issue are:

- **Option A:** Include an appendix in the BPM providing detailed guidance on the concepts, definitions, and scope of PPPs arrangements, the associated DI transactions and positions and how to treat these in the balance of payments and international investment position, respectively.
- **Option B:** Maintain the status quo but provide practical guidance on how to compile PPPs related DI transactions and positions in the *BPM6CG*.

### *Issue 2—Clarification on the Treatment of the SPV/DIE in the Generic Models of PPPs Arrangements*

10. The treatment of the SPV//DIE is key in DI relationships and *BPM6* already provides considerable guidance on notional units in paragraphs 4.34 to 4.40 as well as on branches in paragraphs 4.26 to 4.33. In the case of PPP's arrangements, because of their characteristics of long-term contract and large

[12] PPPs arrangements also involve issues related to data compilation, including source data (e.g., the use of data with confidentiality restrictions for certain projects). Given that these compilation issues do not have direct impact on the methodology, they could be discussed in the context of compilation guidance such as in the *BPM6CG*.

[13] SPV is used here to reflect that these entities are unlikely to meet the statistical definition of special purpose entity. One reason for setting up an SPV is when a PPP is relying on a project-finance structure.

magnitude projects, it is highly possible that these DIEs play an important role as well. Current statistical frameworks made limited references to the role of DIEs in PPPs arrangements.

11. The options to address this issue are:

- **Option A:** No changes in the updated BPM and explain the above issues in other documents (e.g., compilation guide and clarification notes).
- **Option B:** Provide detailed guidance on the application of the existing guidance on branches and notional units in the case of PPPs arrangements. The DI relationship could be explained using different PPPs initiatives such as those included in footnote 5 of this Guidance Note (GN). These explanations could be included in the Appendix recommended in Issue 1.

***Issue 3—Ownership of the Asset Issue: Clarification of the Role of the Economic and Legal Ownerships of the Assets in PPPs Arrangements under DI***

12. International statistical standards present the relevance of the economic ownership of the assets to determine the adequate treatment of PPPs arrangements. The classification is different if the economic owner of the assets is the government or the private entity. In the *BPM6*, the concept of ownership of assets is based on economic ownership. The economic owner is the party who has the risks and rewards of holding the asset.

13. The options to address this issue are:

- **Option A:** No changes in the updated BPM and explain the above issues in other documents (e.g., compilation guide and clarification notes).
- **Option B:** Since the economic ownership of the asset in a PPP arrangement is relevant for the adequate statistical treatment of PPPs transactions and positions, Appendix recommended in Issue 1 will discuss relevant alternatives to determine what unit involved in PPPs arrangements under DI has the economic ownership of the asset.

***Issue 4—Recording Issue: Reporting of PPPs Arrangements under DI***

14. **PPPs transactions and positions in DI are not separately identified in the current presentations of ESS.** Transactions and positions of PPPs falling within DI should be recorded in the corresponding DI categories, equity and debt instruments in the financial account, and investment income in the current account.

15. The options to address this issue are:

- **Option A:** A supplementary "**of which PPPs**" line to be included under the DI functional classification in order to track the evolution of PPPs related DI given the increase in such transactions and positions globally.
- **Options B:** No changes in the current reporting of DI statistics in the current and financial accounts.

## SECTION II: OUTCOMES

### RECOMMENDATION FOR ISSUE 1—OPTION A

16. This GN proposes Option A of including an annex in the BPM providing guidance on the concepts, definition, scope and treatment of PPPs related DI and associated transactions and positions.

### RECOMMENDATION FOR ISSUE 2—OPTION B

17. This GN recommends Option B because it will recognize the importance of establishing criteria for imputation of either a notional unit or a branch (DIEs) in PPPs under DI. Although additional discussion and examples can be included also in the *BPM6CG*, the authoring team supports to include this discussion in the new BPM.

### RECOMMENDATION FOR ISSUE 3—OPTION B

18. This GN recommends Option B to include guidance on how to treat PPPs arrangements under DI depending on whether the economic owner is the government or a private corporation.

### RECOMMENDATION FOR ISSUE 4—OPTION B

19. Separate identification of PPPs within the DI functional classification in the balance of payments and IIP would have analytical value, particularly for economies that are actively involved in PPPs arrangements. However, given that data of these projects can present some confidentiality issues, and that PPPs arrangements may be large but infrequent and limited in some countries, this GN does not recommend introducing a specific breakdown to separately identify PPPs in the updated BPM.

### SUMMARY OF DISCUSSIONS WITHIN THE DITT

20. **The DITT members were generally supportive of the recommendations of the drafting team to provide further guidance on concepts and treatment of PPPs arrangements.** The vast majority who commented agreed with the recommendation of the drafting team to provide a detailed appendix on the concepts, definitions, scope, and statistical treatment of PPPs related to DI in the update of the BPM. However, two DITT members supported including the guidance in the *BPM6CG* only.

21. **All DITT members who commented agreed with the recommendation of the drafting team to provide further guidance on the treatment of PPPs arrangements related to DI by including relevant aspects of PPPs arrangements described in other statistical frameworks, such as GFS.** Further, all agreed with the recommendation that it is not necessary to separately identify PPPs in DI classification in the balance of payments and IIP.[14]

[14] One member of the DITT suggested that the GN should also cover the treatment of large construction projects undertaken by nonresident as trade in services or in DI. This issue will be addressed in a clarification note on the recording of construction and, therefore, is not covered in this GN.

RECOMMENDATIONS APPROVED BY THE JUNE 2021 COMMITTEE MEETING

**Provide additional guidance on the concepts, definitions, scope, and statistical treatment of PPPs related to DI.**[15] This should include: (i) the conceptual guidance on PPPs in an annex of the *BPM7*, and (ii) guidance on the sources and compilation methods will be developed in the *BPM7 Compilation Guide*. Separate identification of PPP arrangements in DI classification in the balance of payments and IIP is not required.

[15] A summary of the Balance of Payments Committee discussion on this GN is available here.

## Annex I. Examples of Definitions of PPPs

1. **The World Bank defines PPPs as long-term contracts between a private party and a government entity, for providing a public asset or service, in which the private party bears significant risk and management responsibility, and remuneration is linked to performance.**[16] The PPPs are described in terms of the type of asset involved; what functions the private party is responsible for; and how the private party is paid. The PPP contract defines functions for which the private party is responsible for and these include design (engineering work), build or rehabilitate, finance, maintain and operate. These commonly include infrastructure projects[17] and their transactions are likely to be classified as resident-to-resident, particularly if the private corporation creates a separate unit to construct and/or operate the asset (although in such instances that unit may incur external assets and/or liabilities to its nonresident parent and other parties, which need to be recorded).[18]

2. **The *Manual on Government Deficit and Debt*, implementation of *ESA 2010* (*MGDD*), 2019 edition presents a definition of PPPs as long-term contracts but with "government paying to a nongovernment partner all or a majority of the fees under a specific contractual arrangement, thus covering most of the total cost of the service provided."** The definition highlights that the contract is for the provision of "public assets" and government agrees to buy services from a nongovernment unit (a partner), resulting from the use of specific "dedicated assets," which the nongovernment unit builds to supply public services (Figure 1). Government would normally enter into a contract with one or several experienced commercial partners, directly or through an SPV set up for the specific purpose of the PPP, for the delivery of services derived from a specific asset.

3. **The *2008 SNA* presents additional characteristics of PPPs:**

- *In the contract period the PPP contractor has the economic ownership.* Once the contract period is over, the government has both economic and legal ownership. It is not easy to establish which unit is the legal owner of an asset during the contract period or how the implicit transactions when its economic ownership changes should be recorded.

- *PPPs vary greatly*. A general description that includes the most common arrangement is as follows. A private enterprise agrees to acquire a complex of fixed assets and then to use those assets together with other production inputs to produce services. Those services may be delivered to the government, either for (i) use as an input to its own production (for example, motor vehicle maintenance services) or (ii) distribution to the public without payment (for example, education services), in which case the government will make periodic payments during the contract period.

4. *The private enterprise expects to recover its costs and earn an adequate rate of return on its investment from those payments*. Alternatively, the private enterprise may sell the services to the public (for example, a toll road), with the price regulated by the government but set at a level that the private

[16] *World Bank Public Partnerships Reference Guide Version 3*, 2017, page 5.

[17] For example*, roads, tunnels, bridges, rails, ports, airports, water supply, and sewerage treatment work or distribution system, hospitals, schools, housing projects, prison facilities, electricity generation and distribution facilities, and pipelines.*

[18] *EDS Guide 2013*, paragraphs 4.119–4.126, Appendix 1.

enterprise expects will allow it to recover its costs and earn an adequate rate of return on its investment. **Eurostat's Guide for PPPs, *A Guide to the Statistical Treatment of PPPs* (2016), presents a definition that links a long-term contract with sources of payments for the provision of a public asset.** [19] Thus, it defines PPPs as "a long-term contractual arrangement for the provision of a public asset and related services in exchange for performance-based payments linked to the asset's availability and/or use and the delivery of the related services." This definition of a PPP requires the participation of two units, an authority and a partner.

a. The "authority (that is, the public authority that enters into the PPP contract) is classified as a part of the general government.[20] If the authority is classified outside the general government sector, Eurostat does not consider this contract to be a PPP."

b. The *partner* should not be part of the general government and, "in the vast majority of PPP projects, it is a SPV created for the sole purpose of entering into a PPP contract with an authority." [21]

   i. If the partner is a SPV or non-SPV (this case is unusual) controlled by private entities, the contract/project will be considered a PPP.

   ii. if the partner is a SPV or non-SPV controlled by the government,[22] [23] and it is to be classified as general government unit, the project/contract will not be considered a PPP.

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[19] As defined by the *GFSM 2014*, a public asset is any store of value representing a benefit or series of benefits accruing to the economic owner by holding or using the resource over a period of time, which is considered part of the general government.

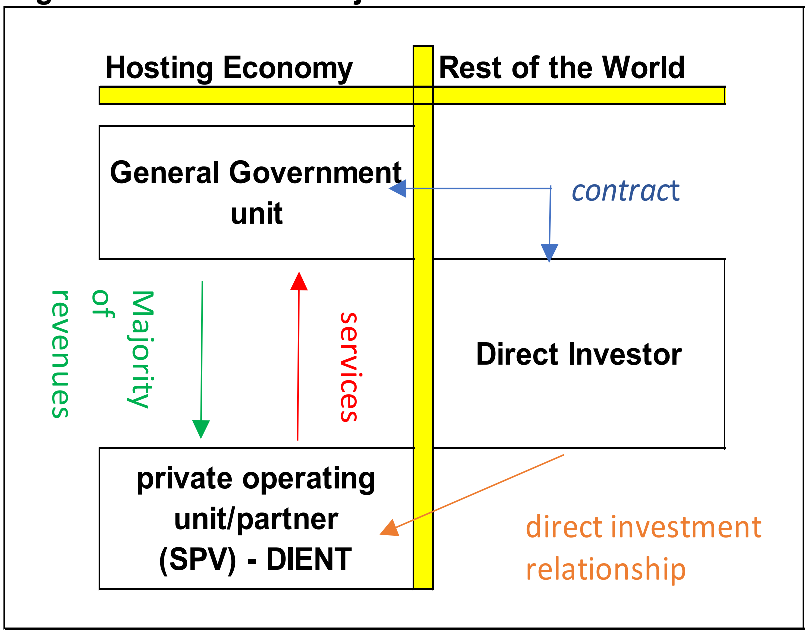
[20] The coverage of the general government includes the central government and regional or local governments.

[21] See Chapter 2 for this definition and characteristics of PPPs.

[22] The government control of an SPV can be established in a number of ways including, for example, through ownership rights, contractual rights, financing arrangements, law, regulation or vetoes over the SPV's important decisions. See *ESA 2010* paragraphs 2.38, 20.309, and 20.316–20.318 and *MGDD 2016* Chapters I.2.3 and I.6.2. Annex IV for criteria of control of a unit in this Guide and the *BPM6*.

[23] This Guide includes a second step to determine a partner controlled by government is included in the general government sector. If the partner is not a market producer, it will be classified in the general government sector. Otherwise, if the partner is a market producer, although controlled by the government unit, it will be classified outside of the general government sector.

**Figure 1: Basic PPP Project**




5. **The nature of activities that PPPs are involved in varies greatly.** Generally, the private corporations construct and operate assets of a kind that are usually the responsibility of the general government or public corporations. These commonly include roads, bridges, water supply and sewerage treatment works, hospitals, prison facilities, electricity generation and distribution facilities, and pipelines.[24]

***PPPs and Concessions***

6. **A key feature of PPPs is that government is the main purchaser of the services from the partner.** Under the Eurostat's definition of a PPP, the general government unit is the direct source of most of the revenues that the partner is entitled to receive under the contract. This is the case when the demand for the asset or the use of it is originated from the general government unit itself (e.g., a hospital paid for by a government unit on an availability basis) or from users (e.g., a road, paid for by a government unit on a demand (shadow toll) basis). If the majority of the partner's revenues is sourced directly from the users of the asset, Eurostat will consider the project to be a concession, and the statistical treatment will be assessed under separate rules (which are outside the scope of its guide).[25]

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[24] The Eurostat's Guide includes in Chapter 2 a detailed list of typed of assets that can be included in PPPs arrangements.

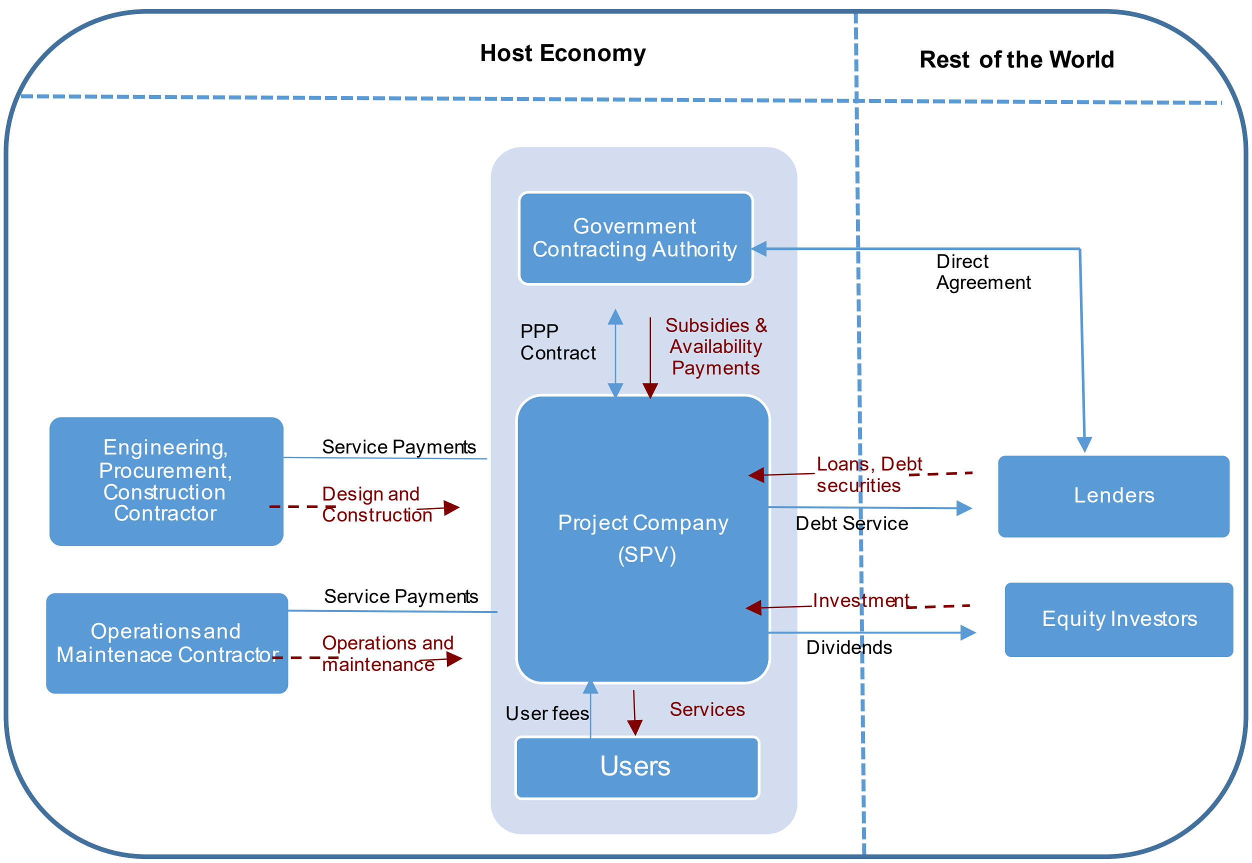
[25] The *International Public Sector Accounting Standards–IPSAS 32* refers to "service concessions," not directly to PPPs and have the same purpose, which is to provide public service. As a result, this similar objective would possibly allow to align PPPs with *IPSAS 32*. Although there is merit to ensure that the language and definitions across all manuals and the IPSAS are fully consistent, it is understood that it is outside the scope of this guidance note, which is to clarify the statistical treatment of PPPs under DI.

*PPP Contracts*

7. **The complexity and variety of PPP contracts[26] preclude the enumeration of detailed rules governing the transactions to be recorded concerning the ownership and use of the assets.** Instead, all the facts and circumstances of each contract should be considered and then a statistical treatment should be selected that best brings out the underlying economic relationships. The contracts include aspects such as the disposition of the assets at the end of the contract, the required operation and maintenance of the assets during the contract, and often allows government to specify the design, quality, capacity use, and maintenance of the asset in accordance with government standards. At the end of the contract period, the government may gain legal and economic ownership of the assets, possibly without payment.

8. **Figure 2 illustrates one of the typical PPP project structures with the external parties.** This structure suggests the existence of DI and related transactions and positions and these should be measures and recorded appropriately in the external sector accounts.[27]

**Figure 2. Typical PPP Project Structure and Funds Flow**




[26] Additional characteristics of PPPs contract can be found in the *MGDD*, Section 6.4.

[27] Potential DI transactions in Figure 1 include interest, dividends, and equity; and debt instruments such loans and debt securities, if the equity investment is 10 percent of the voting shares of the project company.

## Annex II. Statistical Treatment of PPPs in the *2008 SNA*

1. **The following description of the statistical treatment of PPPs is based on the guidelines prescribed in the *2008 SNA*.**[28]

- ***If the government is considered the economic owner of the asset(s)*** *during the contract period but does not make any explicit payment at the beginning of the contract, a transaction must be imputed to cover the acquisition of the asset(s).* The recording of these depends on the specific contract provisions, how they are interpreted, and possibly other factors. Most frequently, these contracts will be recorded as the acquisition of the asset through an <u>imputed financial lease</u> because of the similarity with actual financial leases. In other cases, for example, a loan that equals the market value of the asset at acquisition could be imputed, the actual government payments to the private corporation could be partitioned so that a portion of each payment represents the repayment of the loan[29] and the remainder could represent an expense for use of goods or services, subsidies, in accordance with the contract.

- ***If the private corporation is considered the economic owner of the asset(s) during the contract period,*** *any debt associated with the acquisition of the asset(s) should be attributed to the private corporation*. Normally, the government obtains legal and economic ownership of the assets at the end of the contract without any significant payment. However, two approaches are possible to account for the acquisition of the asset(s) by government:

  - *Over the contract period, government gradually <u>builds up a financial claim</u> (e.g., other accounts receivable) and the private corporation gradually accrues a corresponding liability (e.g., other accounts payable),* such that both values are equal to the residual value of the assets at the end of the contract period. At the end of the contract period, government records the acquisition of the asset, with a reduction in the financial claim (other accounts receivable) as the counterpart entry. The other unit records the disposal of the asset, with a reduction in the liability (other accounts payable) as the counterpart entry. Implementing this approach may be difficult because it requires new transactions to be constructed using assumptions about expected asset values and interest rates.

  - *An alternative approach is to record the change of legal and economic ownership from the private unit to government <u>as a capital transfer</u> at the end of the contract period*. At the end of the contract period, government records revenue in the form of a capital transfer that finances the acquisition of the asset and the private unit records an expense in the form of a capital transfer payable to government, financed by the disposal of the asset. The capital transfer approach does not reflect the underlying economic reality as well as the first alternative, but data limitations, uncertainty about the expected residual value of the assets, and contract provisions allowing various options to be exercised by either party make recording a capital transfer acceptable on pragmatic grounds.

2. **For the statistical treatment of PPPs, Eurostat's Guidelines recommends to follow three steps:** (i) identifying the issues that typically influence the statistical treatment; (ii) analyzing the

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[28] Chapter 22.

[29] See financial leases in the *GFSM 2014* paragraphs A4.10–A4.15.

significance of the issues that influence the statistical treatment (identified in step 1); and (iii) concluding the statistical treatment, mainly to establish if the PPP is off-balance sheet of the government. The first step is all about the assessment of the PPP contract and its related provisions.[30]

[30] Eurostat's Guidelines include an annex with a table of typical PPP contract provision that may influence the statistical treatment of PPPs.

## Annex III. Determining the Economic Ownership of PPP-Related Assets

### *2008 SNA*, CHAPTER 22, *GFSM 2014*, AND *PSDS GUIDE*.

1. The economic owner of the assets related to a PPP is determined by assessing which unit bears the majority of the risks and which unit is expected to receive a majority of the rewards of the asset. The factors that need to be considered in assessing economic ownership of PPP-related assets include those associated with acquiring the asset and those associated with using the asset.

2. Some of the risks associated with acquiring the asset are:

- The degree to which the government controls the design, quality, size, and maintenance of the assets;
- Construction risk, which includes the possibility of additional costs resulting from late delivery, not meeting specifications, or building codes, and environmental and other risks requiring payments to third parties.

3. Some of the risks associated with operating the asset are:

- Supply risk, which covers the degree to which the government is able to control the services produced, the units to which the services are provided, and the prices of the services produced;
- Demand risk, which includes the possibility that the demand for the services, either from government or from the public at large in the case of a paying service, is higher or lower than expected;
- Residual value and obsolescence risk, which includes the risk that the value of the asset will differ from any price agreed for the transfer of the asset to government at the end of the contract period;
- Availability risk, which includes the possibility of additional costs or the incurrence of penalties because the volume and/or quality of the services do not meet the standards specified in the contract.

4. The relative importance of each factor is likely to vary with each PPP. It is not possible to state prescriptive rules that will be applicable to every situation. The provisions of each PPP arrangement must be evaluated to decide which unit is the economic owner.

5. **The *MGDD* presents as far as risks are concerned, as a basic rule, the PPP assets are to be classified in the partner's balance sheet and not in the government balance sheet, if the following conditions are met:**

- the partner bears the construction risks;
- the partner bears at least one of either availability or demand risk, as designed in the contract and in some cases at the same time both availability and demand risks. It must be stressed that, in most contracts, only one kind of risk triggers the whole (or almost whole) payment from government to the partner; the payment is based either on availability indicators of the asset, or on use/attendance of the asset. The latter case is only observed when this depends on the final users and not on the government-paying unit; and
- the risks are not incurred by government through other means, such as through (e.g.) government financing, government guarantees and early redemption clauses.

6. If the above conditions are met, it is also important to consider all other mechanisms in place specified in the contract, in order to check whether there could be an allocation of the risks to government via other means. If this would not be the case, the accounting treatment of the PPP would be similar to the treatment of an operating lease in national accounts; it would be classified as a purchase of services by government.

## Annex IV. Some General Principles for Recording PPPs In External Debt

- ***The economic ownership of an asset remains with a nonresident private enterprise, and where this is constructed by this enterprise,*** until transferred to government on completion of the contract, any prepayments for the asset by the government are claims on a nonresident enterprise (i.e., external debt of the private nonresident corporation). If the government only pays to the private nonresident corporation and obtains economic ownership on completion, and needs to borrow abroad to finance this purchase, then the government will incur external debt when it borrows.

- ***The economic ownership of an asset remains with the government during the contract period,*** but it does not make any explicit payments to the private nonresident corporation, a financial lease is imputed, hence external debt for the government (see also *PSDS Guide*, paragraph 4.125 and *GFSM 2014*, paragraph A4.64).

- ***Where there are lease arrangements between the government and a nonresident private corporation***, these are classified in the normal way as operating or financial leases, and hence external debt or not, depending on whether the government or private corporation gains most of the risks and benefits of ownership as a result of the contracts entered into. For instance, if the private corporation continues to legally own the asset but the government makes payments both to cover the costs of operating the asset and to meet the financing costs, then a financial lease, and hence external debt, arises for the government and should be recorded as such.

## Annex V. Control of a Unit Related to a DI Relationship

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|---|---|
| The following is a non-exhaustive list of examples of government control, which are given for illustrative purposes only: If government has a 51% share in the ownership and voting rights of the SPV, the SPV is deemed to be controlled by government through its majority share; | A DI relationship arises when an investor resident (direct investor) in one economy makes an investment that gives control or a significant degree of influence on the management of an enterprise (DIE) that is resident in another economy. Ownership of 10 percent or more of the voting power in the enterprise is evidence that a DI relationship exists. A direct investor is an entity or group of related entities that is able to exercise control or a significant degree of influence over another entity that is resident of a different economy; a direct investor can be an enterprise, but can also be, for example, an individual, household, or government. A DIE is an enterprise subject to control or a significant degree of influence by a direct investor. (See paragraphs 6.9 and 6.11 in the *BPM6*). |
| If government has a 25% share in the ownership of the SPV which gives it rights to veto important decisions of the SPV (for example through shareholder agreements or through general company law), the SPV is deemed to be controlled by government through those rights. This is the case even if the veto rights mirror veto rights held by other owners of the SPV; and | |
| If government has no share in the ownership of the SPV but has rights to veto important decisions of the SPV through a financing agreement or a contract, the SPV is deemed to be controlled by government through those veto rights. | |

In all the examples mentioned above, the SPV is classified inside the general government sector and the project will be on balance sheet for government.