

Challenges with the delineation of public sector: borderline between the financial corporations and general government sectors



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- 1** The classification of entities in the European framework
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1. The classification of entities in the European framework

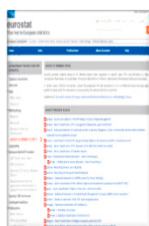
Methodology



European system of national and regional accounts in the European Union (ESA2010)



Manual on Government Deficit and Debt (MGDD)



Specific advices issued by Eurostat in particular cases



Committee on Monetary, Financial and Balance of Payments Statistics (CMFB)



1. The classification of entities in the European framework

- The existing rules on the delimitation of institutional sectors occasionally raise doubts specially in the classification of entities engaged in financial activities and, at the same time, with a strong influence in their activities by government units:



General
government
sector

Non-market producers that are controlled by public sector and units involved in the redistribution of income and wealth.

Financial
corporations
sector

Market producers that are mainly involved in providing financial intermediation or financial auxiliary services



- Some complex classification issues arose especially since 2008, after relevant government interventions in financial institutions



2. Borderline cases

- The analysis of the rules on the classification of entities presented in the various international statistical manuals may lead to different understandings by different statistical authorities and sometimes to inconsistent statistical recordings:
 - **Captive financial institutions or government units?**
 - **Defeasance structures or financial corporations?**
 - **Protection funds or financial corporations?**



2. Borderline cases

➤ Captive financial institutions or government units?

Different understandings may arise from the interpretation of ESA2010 and MGDD in relation to the sector classification of captive financial institutions



ESA §2.20 - only captive financial institutions with no independence of action are to be classified in general government



MGDD §47 and §48 of Part I.6 - if certain conditions are met all government controlled captives financial institutions would be classified in the government sector

In practice, in recent cases, all units which have the features of captive financial institutions controlled by government have been classified inside government



2. Borderline cases

➤ Captive financial institutions or government units?



The case: Hungarian Eximbank

Eximbank is a government controlled Hungarian Export-Import Bank



Eximbank is a captive financial institution:
General government sector

Hungarian
statistical
authorities



Eximbank acts on its own risk:
Financial corporations sector



2. Borderline cases

➤ Defeasance structures or financial corporations?

The relevant question is which body assumes the majority of the risk



ESA § 2.57 - the financial intermediation process channels funds between third parties with a surplus and those with a lack of funds. A financial intermediary does not only act as an agent for other institutional units, but places itself at risk by acquiring financial assets and incurring liabilities on its own account

Financial entities under resolution may have residual activities which may still be considered as financial intermediation



2. Borderline cases

➤ Defeasance structures or financial corporations?

Additionally, different interpretations may occur on the classification of banks included in the ECB MFI list:



ESA § 2.67 – the aggregate of subsectors of deposit-taking corporations, central bank and money market funds, coincides with Monetary financial institutions as defined by the ECB



MGDD (footnote 70 of §15 of Part I.5 and footnote 89 of §41 of Part I.6) - owning a banking license and/or the inclusion of an entity in the MFI list are not sufficient criteria to classify entities in the financial corporations sector



2. Borderline cases

➤ Defeasance structures or financial corporations?

The case: Portuguese Banif



Banif is a residual entity that arose from the resolution process of the Banco Internacional do Funchal, S.A.. It is an institutional unit that may be seen as still producing financial intermediation services, in which government has no responsibility for repaying the remaining liabilities



Banif was reclassified from financial corporations sector to the **general government sector**, considering Banif as a defeasance structure that holds problematic assets (27 against 24 votes)



2. Borderline cases

➤ Protection funds or financial corporations?

The main issues are the degree of control by the public sector and the autonomy of decision



MGDD (§13 of Part I.5) - if the protection fund has a full autonomy of decision, it should be classified as a financial auxiliary, otherwise the unit should be classified in the general government sector

However, this rule does not have always a straightforward application: it is sometimes subjective to say that a specific protection fund acts as an “auto-pilot” entity (with all its activity regulated by law) or, on the contrary, that it has a proper internal and autonomous decision-making process



2. Borderline cases

➤ Captive financial institutions or government units?



The case: Hellenic deposit and Investment Guarantee Fund (TEKE)

TEKE is a legal entity of private law which comprises three different activities: a resolution fund, a deposit guarantee fund and an investment fund



TEKE activity is controlled by the Greek government and that it is financed by compulsory payments from financial corporations, and it acts much as an auto-pilot: **General government sector**



Supported by a CMFB consultation

Bank of Greece

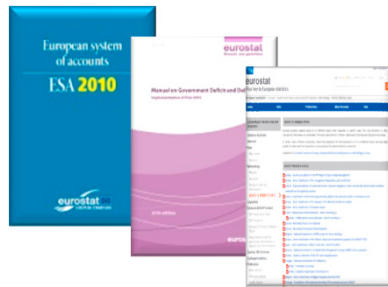


TEKE is not controlled by the Greek government; it has autonomy of decision:

Financial corporations sector



3. Challenges in the delineation of the public sector



- ❑ Theoretical rules and principles on the classification of entities and its implementation could be enhanced and further harmonized in the various statistical manuals
- ❑ The application of the current framework leads, in some cases, to different interpretations, and inconsistent statistical recordings may arise

- ❑ Borderline cases show that there is no consensus between the statistical entities in the classification of entities



The existing rules could be considered insufficient





3. Challenges in the delineation of the public sector

Eliminating existing inconsistencies between different methodological documents

Clarifying the rules by minimizing the room for subjective interpretations and/or ad-hoc decisions

The classification of entities should depend on the economic rationality

The mechanic application of rules, based on administrative details and procedures, should not be the main criteria to classify entities

An involvement of the whole statistical system should be reached to achieve a broader consistency and clarity of the application of rules



4. Conclusions

- The **rules** on the classification of entities established in the European framework are, in some cases, **not straightforward**, leading to different interpretations by the statistical authorities, which may be critical in some **borderline cases**
- Depending on their specificities, entities can be classified in the **financial corporations sector** or in the **general government sector**, with significantly different impacts in statistical aggregates
- An involvement of the whole European statistical system should be reached in order to perform a **review of the sector classification rules**
- Moreover, besides ensuring a correct sector classification, the clarification of rules would contribute to guarantee a **unique classification of entities** and **consistency between different statistical domains and across countries**



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Thank you for your attention



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