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PRIVATISATION AND NATIONALISATION

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PRIVATISATION AND NATIONALISATION

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Executive summary

The recording of privatisation operations is not dealt with in the 1993 SNA. This paper intends to develop recommendations, based on the SNA conceptual framework, in light of the experience of the recent past. It borrows mainly to the ESA95 manual on government deficit and debt (Eurostat) and to the GFS Manual 2001 (IMF).

The main recommendations encompass the case of direct privatisation (direct sale by a government unit) and the cases of indirect privatisation (the sale is made through another public entity, often a public holding company). Some special cases are also dealt with.

The overall rationale is that privatisation operations entail a reshuffling of assets in the balance sheet of the government. The sale of assets generates no flow of income in favour of the government.

The three main recommendations are the following:

- 1. The sale of shares and other equity in a public enterprise is a financial transaction, to be recorded in the financial account.*
- 2. The sale of a non-financial asset is to be recorded in the capital account.*

NB: In all cases when there is a payment to government from the proceeds of sale of assets (financial or non-financial) by a public holding company, the payment is a financial transaction.

- 3. The purchase of shares (nationalisation) is a financial transaction, except if this is operated by mean of confiscation (this is another flow).*

Under the denomination of «privatisation», several types of statistical issues may be considered. The focus in this paper is on the recording of the sale of government assets – the typical case of “privatisation”, especially when it concerns the sale of stake in a public corporation. This sale can be made either directly by government units, or indirectly through controlled corporations (often public holding corporations), agencies or special purpose entities. The overall statistical treatment should also encompass the reverse transaction: the purchase of assets by government units (the case of nationalisation).

Background and reasons for change the SNA

1. These issues were not dealt with in the 1993 SNA, although the general conceptual and accounting framework allows for developing adequate recommendations. The “privatisation” issue was one of the five priority issues defined by the Task Force on Harmonisation of Public Sector Accounting. It has been put forward under issue 25 in the list adopted by the advisory Expert Group for the SNA updating project.
2. Privatisation operations were increasingly undertaken by governments starting from the mid-eighties in most western countries. The transition to market economy in the Central and Eastern Europe during the nineties was also a context where these operations were developed on a large scale. It is also a challenge on other continents.
3. Given the significant impact of these operations on the government deficit and debt in the European context, Eurostat had to organise the reflection and the discussions in order to interpret the SNA and ESA framework in this domain. The result of this reflection is the ESA95 manual on Government Deficit and Debt (EMGDD second edition, part II, 2002). The GFS Manual 2001 of the IMF also adapted its recommendations to this new situation (see the recommendations in §9.38-39). Moreover, the IFRS and the IPSAS have also developed accounting prescriptions (domain of property, plants and equipments...).
4. The SNA update is an opportunity to supplement the conceptual framework, and develop recommendations in order to ensure adequate recording of this sort of operations. Often presented as one-off transactions, they have significant impact on national accounts aggregates and balances, especially for the general government sector.

Recommendation 1: sale of financial assets

The sale of shares and other equity in a public enterprise (privatisation) is a financial transaction, recorded in the financial account. This flow corresponds to a reshuffling of financial assets in the balance sheet of the government.

If the sale of shares and other equity in a subsidiary is made by a public holding corporation – or any other kind of public agency –, the payment of all or part of the sale proceeds to the government is a financial transaction.

Recommendation 2: sale of non-financial assets

The sale of a non-financial asset is a non-financial transaction recorded in the capital account.

However, if the sale of a non-financial asset is made by a public holding company – or any kind of public agency –, the payment of all or part of the sale proceeds to the government is a financial transaction, recorded in the financial account.

Recommendation 3: nationalisation

Nationalisation of private corporation by mean of confiscation is to be recorded as an uncompensated seizure, to be recorded in the other change in the volume of assets account

Nationalisation of a private corporation by mean of purchase of shares (at market price, by mutual agreement) is a financial transaction, to be recorded in the financial account.

I PRIVATISATION

5. Definition: privatisation means usually the giving up of control, by the general government over a public enterprise, primarily by the disposal of shares and other equity in this enterprise. This issue is not dealt with in the 1993 SNA. The word “privatisation” is not quoted.

6. Beyond the typical case of privatisation (the disposal of shares and the giving up of control), the issue to be clarified in this paper is the recording in national accounts of the sale of assets¹, whether it involves a loss of government control or not. In effect, the loss of control as such is neither a transaction, nor it implies a change of institutional sector classification².

7. The issue is the recording of a transaction, made by mutual agreement. This transaction results in restructuring / reshuffling of assets in the balance sheet of the government, what is – as such - neutral on the net worth. The sale of assets generates no flow of income in favour of the government, and in particular no flow of property income (dividend). Income is generated by the entrepreneurial income and not by sale of assets.

8. However, the government often uses the service of financial intermediaries to achieve the privatisation process (valuation of the assets, practical implementation of the sale on the market), even in the context of a direct sale of assets. These expense – the purchase of a financial service - have to be recorded as intermediate consumption. This has an impact on both the net lending / net borrowing and the net worth of the government sector.

In the general case (see I.1 below), the transaction is a sale of financial assets.

I.1 General pattern: the sale of financial assets

a) Direct sale of financial assets

9. The direct sale of financial assets is a financial transaction recorded in the financial accounts of the units involved (the general government and the corporation). It is a withdrawal of shares and other equity (F.5) from the corporation. The counterpart transaction is usually for the government an increase of liquid assets (currency and deposits, F.2).

NB: If the public corporation was not incorporated, the first step in the privatisation process is usually to change the status of the corporation and to issue shares.

b) Indirect sale of financial assets

10. This is the case where the sale of shares in a corporation is not done directly by the government – usually the central government - but by a public corporation (often a public holding corporation) or any kind of agency classified outside the general government sector. In other words an entity acts as an “intermediary” between the government and the corporation to be sold (entirely or partially). In this case, all or part of the proceeds of the sale is paid back to the government.

11. The indirect sale of financial assets is a financial transaction to be recorded in the financial accounts of the units involved, even in the case where the selling unit would transfer only part of the proceeds to its

¹ This paper focuses on the recording of sale transactions made by the government. However, in the general cases of sale of assets, the recommendation is worth also for any other units and sectors.

² Except when compiling accounts for the public sector.

owner, the government. Provided that the selling public entity is an institutional unit; it is recommended to record the flows in two steps:

- The sale of shares by the public unit: this is a classical and direct sale of financial assets, to be recorded as recommended in §9, above (except that the government sector is not involved at this stage).
- The transfer of the sale proceeds (in F.2) to the government is also a financial transaction: the flow in F.2 has a counterpart flow, which is a decrease of the government equity (F.5) in the public unit.

1.2 The sale of non-financial assets

a) Direct sale of non-financial assets

12. The direct sale of a non-financial asset is recorded in the capital account, with a counterpart entry in the financial account (F.2). The transaction in the capital account will be a decrease in GFCF (P.51) if this is the sale of a fixed asset, or a decrease in another asset, K.2 for instance, if this is a non-produced asset (land etc.).

b) Indirect sale of non-financial assets

13. The sale of a non-financial asset by a (non-government) public unit is recorded in the capital account of this unit. However, if the proceeds of the sale are paid back to the owner (the government), this is a financial transaction (F.2), to be recorded in the financial accounts of the unit involved. The counterpart flow will usually be a decrease of the government equity (F.5) in the public unit. This reflects the liquidation of assets in this unit.

1.3 Specific pattern: the restitution of assets to former owners

In the context of restoring property to previous owners, for instance in the case of “transition countries”, two types of restitutions need to be examined:

a) Restitution in kind

14. If non-financial assets (land or buildings for example) are returned back to the former owner, two cases may require different recordings:

- The asset to be returned is roughly the same as the one confiscated in the past (case of non-produced asset): similarly to the former uncompensated seizure (K.8), the flow should be recorded in the other change in the volume of assets account.
- The asset is different in appearance and value (case of produced tangible assets): this should be recorded in the capital account as a negative capital formation (P.5), counterbalanced by a capital transfer in kind (D.99).

b) Restitution through financial compensation

15. Restitution through financial compensation should be recorded as a capital transfer (D.99) counterbalanced by a change in the financial asset used for the transfer (F.2, if currency and other deposits).

I.4 Two special cases

a) Indirect privatisation and restructuring agency

16. It may happen that the government manages privatisation in close relation to restructuring other public sector enterprises through a public holding corporation or any other kind of public agency (or special purpose entity) acting as a “restructuring agency”. In such a context, the proceeds of the sale of shares will not be paid back to the government (like in the usual case of indirect sale of financial assets, see above I.1 b, §11), but kept by the restructuring agency to inject capital in other enterprises in any possible way (grants, loans etc.). This may challenge the sector classification of the restructuring agency and/or the recording of the transactions (sale proceeds, capital injections...).

17. Two main possibilities should be envisaged in national accounts:

- The restructuring unit is a real holding company controlling and directing a group of subsidiaries and only a minor part of its activity is dedicated to channelling funds in the way described above, on behalf of government and for public policy purposes. The favoured solution in this context would be to reroute the transactions made on behalf of government (see SNA93, §3.24, or “Recognizing the principal party to a transaction”, §3.31), through the government itself.
- The restructuring unit, whatever its legal status, acts as a direct agent of government and is not a market producer. Its function is rather to restructure and change the ownership status of public enterprises, and channelling funds from one unit to the other to redistribute income and wealth. This unit should be classified in the general government sector.

b) Privatisation and securitisation

18. Another possible arrangement – also possible in the above-described context - is the case where an agency would securitise the shares and make a prepayment to the government (from borrowing on the market). In addition to the issue of sector classification of the agency (see the paper on “Securitisation”), it should be made clear that any payment linked to the sale of financial assets should be recorded as a financial transaction and have no impact on the net borrowing / net lending.

II NATIONALISATION

19. Definition: nationalisation means the taking of control by the government over assets and over a corporation, usually by acquiring the majority or the whole stake in the corporation.

20. There are two basic means by which government may take assets or corporations into public ownership. The first of these is via appropriation or confiscation of the assets. The second is by purchasing the assets from their current legal owners.

a) Appropriation / confiscation

21. This change in ownership of assets is not the result of a transaction made by mutual agreement. Therefore, this should be considered as an uncompensated seizure (K.8) in the System (SNA, §12.38), to be recorded in the other change in the volume of assets account.

b) The purchase of shares

22. This is the most common way of nationalisation: to obtain control over a corporation the government will buy all or part of the shares in the corporation, at a price which is close to the market

price. There is normally a legal context (a legislation) which ensures that the transaction is made by mutual agreement, even though the owner may have little choice to accept or not the offer, or to renegotiate the price.

This purchase of shares is a financial transaction (in F.5), to be recorded in the financial account.