eurostat
EUROPEAN COMMISSION

Directorate C: National and European Accounts

Luxembourg, 16/10/09
ESTAT/C-3/MHF/LA/AK/dm D(2009) **30272**

Mr Bill Keating
Director - Macro-economic statistics
Central Statistics Office
Ardee Road, Rathmines
IRL - Dublin 6

Subject: Preliminary view on the ESA95 accounting treatment of the National Asset Management Agency (NAMA) and related majority privately owned SPV

Ref.: Your letter dated 22 September 2009

Dear Mr Keating,

Thank you for your letter regarding the treatment of the National Asset Management Agency (NAMA) and related majority privately owned SPV and the accompanying analytical note. I would like to inform you of the preliminary view of Eurostat on the above-mentioned case.

The accounting issue for which a clarification is requested

Description of the case

In order to restore stability to the Irish banking system in the context of the financial crisis, the Irish Government is establishing the National Asset Management Agency (NAMA), which will arrange and supervise the purchase of approximately €77 billion worth of property related loan books from certain financial institutions. The draft legislation to enable the creation of this body was published on 10 September 2009 (the National Asset Management Agency Bill 2009). The Bill was presented to the National Parliament on 16 September, and it is planned that the Bill will pass into law at the end of October.

NAMA, once established, will create a Special Purpose Vehicle (SPV) to purchase certain assets from participating institutions in order to further the purposes of the legislation – most of these assets will be loans associated with property development. This SPV will have a majority of private equity. It will fund the purchase of the loan books from financial institutions by issuing securities, most of which will be backed by a guarantee from the Irish Government.

Because of the large amounts involved, CSO asked if Eurostat would examine the details and advise if it considers CSO's analysis to be consistent with Eurostat's Decision on the statistical recording of public interventions to support financial institutions and financial markets during the financial crisis, which was published on 15th July 2009.

Given the critical national importance of the issue, CSO staff, along with representatives of the Department of Finance and of NAMA, also visited Eurostat on 13 October 2009 to provide further information, including about recent developments.

Methodological analysis and clarification by Eurostat

Eurostat welcomes the detailed analysis provided by the CSO focusing on the classification of NAMA and the related SPV.

Classification of NAMA

The National Asset Management Agency (NAMA), is publicly owned and has as its purpose to conduct a specific government policy (to arrange and supervise the purchase of impaired related loan books). Therefore, according to the decision of 15 July 2009 of Eurostat on the statistical recording of public interventions to support financial institutions and financial markets during the financial crisis (later: the decision of Eurostat), it is to be classified within the general government sector.

Classification of the SPV

NAMA will delegate the purchase and management of the selected loans to a separately created *SPV*, which will be jointly owned by the private investors (51%) and NAMA (49%). The subscribed capital of this SPV will be EUR 100 million. This SPV will purchase the assets from banks using debt securities which it issues, which will consist of securities guaranteed by the Irish government (95%), and subordinated debt securities (5%); the latter will only be redeemed if the SPV makes profits.

In order to decide on the classification of the SPV, according to the Eurostat decision and the related Guidance note, in the case of majority privately-owned special purpose entities, three factors have to be examined in more detail: the purpose of the institutional unit, the duration for which the unit is established, and whether the losses it is expected to make are small in comparison with the total size of its liabilities.

The purpose of the SPV

According to the analysis of the Irish Central Statistical office, the sole purpose of the SPV would be the purchase and management of loan books from financial institutions that are currently in distress as a result of the financial turmoil.

The Irish authorities also clarified that this SPV cannot be used for other purposes in the future, as this would require the Parliament to pass another Bill, which is not probable. Moreover, the definition of assets to be purchased cannot be enlarged without prior consultation with European Commission services.

The duration of the SPV

As regards the duration of the special purpose vehicle created by NAMA, the proposed legislation on NAMA clearly states that its lifetime is temporary and linked to the financial crisis. Section 219 of the legislation also provides that, at the end of 2012, the Minister of Finance will examine the extent to which NAMA has achieved its objectives and decide whether its continuation is justified. This examination could also take place at any time before then if the Minister so decides.

The updated Guidance note on the Decision of Eurostat reinforces the idea of a temporary scheme, which in the case of newly created majority privately-owned bodies means that "*the entity is only* *active acquiring assets (including granting loans) during the period of the financial crisis, and the entity simply disposes of assets or retains them until maturity is the subsequent period*". The SPV will be required to purchase assets defined in the legislation and, due to the necessary administrative procedures, is expected to do so by the end of June 2010.

The size of expected losses

Concerning the expected losses for government, the Decision does not set a quantitative threshold, therefore a rather detailed analysis has to be carried out, especially of the guarantee arrangements, the design of the scheme and the elements which will be in place to reduce the risks for government arising from the entity.

Regarding guarantees, the majority of the bonds issued by the SPV itself to finance the purchase of assets will be backed by government guarantee. The subordinated debt issued by the SPV is not guaranteed by government, and its repayment is conditional on the SPV making a profit.

The design of the scheme in the proposed legislation provides an assurance that potential losses born by the government could be expected to be limited. According to the business plan, the net present value of the SPV will be 4.8bn euro, under the condition that the real estate prices in Ireland will increase by 10% in the coming 10 years. Eurostat is not in a position to judge whether this condition in plausible, however the presence of market investors is reassuring (those providing 51% of the equity of the SPV).

Moreover, other elements, put in place to reduce the exposure of government to losses, also ensure compliance with the Eurostat decision. The price paid for the loans of banks are calculated from the value of assets already written down by the banks and then a 30% haircut is applied on these book values. This so-called "LTEV- long term economic value" is paid for the assets, which are assessed individually by the experts. The current market value is 15% lower than the LTEV but Irish authorities believe that under the current conditions the market values for properties are artificially low.

An important additional element – which Eurostat understands will shortly be introduced into the legislation - is a levy to be imposed on participating banks if the SPV were to have losses at the end of the operating period. The Irish authorities confirmed that under the new proposal, the participating banks have to pay a tax surcharge on their operating profits until the loss of the SPV is recouped.

Conclusion

Based on the preliminary information provided, Eurostat agrees with the CSO's analysis that NAMA should be classified inside the general government sector, and that the master SPV should be classified in the financial corporations sector.

Procedure

This preliminary view of Eurostat is based on the information provided by the country authorities. If this information turns out to be incomplete, or the implementation of the operation differs in some way from the information presented, Eurostat reserves the right to reconsider its view. To this end Eurostat would request to be informed of the final details of the operation.

In this context, we would like to remind you that Eurostat is committed to adopt a fully transparent framework for its decisions on debt and deficit matters in line with Council Regulation 479/2009 and the note on ex-ante advice, which has been presented to the CMFB and cleared by the Commission and the EFC. Eurostat is therefore publishing all official methodological advice (ex-ante and ex-post) given to Member States on the Eurostat website. In case you have objections concerning this specific case, we would appreciate if you let us know. In any case (regardless of whether you have objections or not) we would like to receive an answer from you on the issue no later than 30 October 2009.

Yours sincerely,

Luca Ascoli
Head of unit C.3