

## Government deficit and debt

# Eurostat decision on the allocation of Mobile Phone Licences (UMTS)

**Eurostat**, the **Statistical Office of the European Communities in Luxembourg**, has taken a decision to specify the common rules according to the European System of Accounts (ESA 1995), to be implemented by Member States for the recording of the allocation of mobile phone licences.

Following a 1998 Decision of the European Parliament and of the Council<sup>1</sup>, all EU Member States will attribute third generation (or UMTS) mobile phone licences by 1 January 2002. In this process, different procedures of allocation are possible: sale of the licences by auction or comparison of offers («beauty contest»).

The allocation of mobile phone licences is presently on the agenda of most Member States. Due to the importance of the amounts involved, there is a need to define a common statistical treatment at EU level for what is, basically, the same economic event.

### Eurostat decision

**Eurostat decided that the transaction must be treated as *the sale of a non-financial asset* (the licence), recorded at the time the licence is allocated. In this general case, the sale proceeds have an impact on the government net borrowing / net lending: they increase the government revenue and so reduce once-for-all the deficit of the year when the licence is allocated. The actual schedule of cash payment does not influence the recording of the transaction.**

**The characteristics of some contracts may lead to consider special cases (see below), where the transaction should be viewed as *a rent for the use of a non-financial asset* (the electromagnetic spectrum), recorded over the life time of the licence. In the case of a rent, the impact on the government net borrowing / net lending is spread throughout the duration of the licence.**

To treat the transaction as a tax or as a sale of a service was rejected on the following grounds:

- The transaction *is not a tax*: in principle, a licence recorded as a tax would be automatically granted to any applicant. Moreover, recording a tax would not fit well with the case of a sale by auction of a rare good.
- The transaction *is not the purchase of a service* provided by government: payments are obviously out of proportion with the cost of producing the service.

The issue was discussed by a sub-group of national experts and the working group on national accounts where all Member States are represented. Eurostat requested then a formal consultation

of the Committee on Monetary, Financial and Balance of Payments Statistics (CMFB). The result of the CMFB consultation is annexed to this news release.

Eurostat's decision is consistent with the opinion of the majority of the CMFB, taking as well into consideration the reflection of international organisations (IMF, OECD, UN).

Eurostat will monitor the implementation of the current decision by EU Member States.

## **Additional elements on the different cases**

### **1. General Case**

The transaction is a sale of a non-financial asset (the licence).

*Rationale in national accounts:* the licence is an asset recorded in the corporation's balance sheet. With this asset, they will produce a market service consumed by the users of the mobile phones.

Provided that the amount is known with certainty from the beginning, the transaction flow is recorded in the capital account at the time of the sale, whatever the modalities of payments are (actual payment flows are recorded in the financial account).

The accrued base time of recording is when the licence is attributed.

### **2. Special cases**

Special cases should be considered according to some characteristics of the contracts (length of the contract - more or less than five years - and uncertainty of the value of the sale at the time of the transaction).

Payments shall be recorded as rent - spread every year over the life time of the contract – for the two following types of contracts :

1. The contract applies to a relatively short period (five years or less).
2. The full purchasing price is not agreed in the contract (the price is set only for the first few years - five years or less).

In the case of a contract where by far the largest payment is made at the beginning and only small residual regular payments depend on the performance of the corporation (franchise type contracts), the payments at the beginning are treated as the sale of a non-financial asset (the licence), while the residual regular payments are recorded as rent for the use of another non-financial asset (the spectrum).

## **Examples of allocation in the EU**

Four Member States have already allocated (or started to allocate) the UMTS licences.

**Finland:** four licences were granted for free in 1999 on the basis of a comparison of offers ("beauty contest").

**Spain:** four licences were sold in March 2000 on the basis of a comparison of offers. Amount of receipts: 0,52 billion euro (0,1% of GDP).

**United Kingdom:** five licences were sold by auction in April 2000. Amount of receipts: £22,5 billion, (2.4% of GDP). Payment is expected in the second half of 2000.

**Netherlands:** a sale of five licences by auction has started and will be achieved before the end of July 2000. Amount of receipts is not known for the time being.

For **Spain**, the **United Kingdom** and the **Netherlands**, the sale proceeds should be recorded in government accounts in 2000 (according to the general case of the decision).

In the other Member States, the procedure of allocation of mobile phone licences is not yet finalised.

1. Decision N° 128/1999/EC of the European Parliament and of the Council of 14 December 1998 on the coordinated introduction of a third-generation mobile and wireless communications system (UMTS) in the Community, OJ L 17/1, 22 January 1999.

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# CMFB OPINION ON THE ALLOCATION OF MOBILE PHONE LICENCES

On 15 June, the CMFB has given a preliminary opinion on the treatment of the transfer of mobile phone licences<sup>1</sup>. Meanwhile, the international statistical community, as represented in the Intersecretariat Working Group on National Accounts (ISWGNA), has also reflected on this subject. Moreover, further discussions have taken place at the plenary meeting of the CMFB on 29 June. This has led to further clarification of the CMFB opinion, as stated below.

As the ESA 95, which keeps consistency with the SNA 93, includes no unambiguous provisions on how to treat the new case of mobile phone licences in national accounts, and the ISWGNA has opened the discussions on this topic in the framework of the SNA 93, the following clarification is deemed to be an interim solution.

- In principle, the payments for mobile phone licences should be recorded as the purchase of an asset (by the corporate sector from general government).
- Only in case of specific contracts, with features spelled out below, these payments should however be recorded as a rent for the use of an asset. These features are:

either

the contract applies to a relatively short period, that is by convention 5 years or less

or

the full purchasing price is not agreed in advance but a price is set for a limited period of use only (by convention 5 years or less); as soon as the full purchasing price is then agreed, the rental contract is changed into a purchase of a licence.

In the case of a contract where by far the largest payment is made at the beginning, and only small residual regular payments depend on the performance of the corporation (franchise-type contract), the payments at the beginning are treated as the purchase of a non-financial (non-produced) asset (AN.229), while the residual regular payments are recorded as a rent for the use of another non-financial (tangible non-produced) asset.

## **Further clarification of the CMFB opinion on the MOBILE PHONE LICENCES Treatment in national accounts**

The « spectrum » itself is a "tangible nonproduced asset" (AN.21), as it is a natural non-produced (non-financial) asset "subject to effective ownership and ... capable of bringing economic benefits to their owners, given the existing technology" (ESA 7.18).

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<sup>1</sup> Available on request.

## **Option "sale"**

In case the length of the license to exploit the spectrum is infinite, a full transfer of ownership occurs and payments correspond to the acquisition of a non-financial asset (K.2). The time of recording is the time of completion of the sale (ESA 1.57), irrespective of the time of payments. The non-financial asset acquired is then recorded in AN.21 "Tangible nonproduced assets" (ESA 7.18 and Annex 7.1 Definition of each asset category). Because the market value of the spectrum is now zero from the point of view of the government ("the present value of expected future return" ESA 7.40-7.43), it must appear in the balance sheet of the purchaser (corporate sector).

When government grants a right/lease to use a tangible non-produced asset "over a specified period of time" payments are in principle recorded as rent (ESA 4.74). However, licenses with a definite length of more than a considerable number of years (say 5 years, 10 years or 20 years) would follow, by convention, the case of indefinite contracts. Hence, payments correspond to the acquisition of a non-financial asset (K.2). However, the non-financial asset acquired is then an "intangible nonproduced asset" (AN.22), as general government retains ownership of the spectrum. In the general government balance sheets, the total value of "nonproduced assets" (AN.2) decreases by the amount of the sale and the reconciliation requires two entries in the other changes in volume of assets accounts, in AN.21 and AN.22 (reclassification K.12.22) (ESA 6.33).

- In case the contract is non-transferable, the asset acquired is recorded in AN.229 "Other intangible nonproduced assets" (Annex 7.1 Definition of each asset category).
- In case the contract is transferable, the asset acquired might be recorded in AN.222 "Leases and other transferable contracts" (Annex 7.1 Definition of each asset category).

If the total payment for the licence is made at the moment of the sale, the value of the licence is equal to this payment. If payments are spread over various periods, known in advance, then the value of the licence is equal to the present value of the flow of payments (discounted cash flow), which is computed using the current long-term interest rate. In the latter case, government is deemed to have acquired a financial asset (liabilities of the corporate sector).

In case of specific contracts, where by far the largest payment is made at the beginning and further regular payments depend on the performance of the corporation, the payment at the beginning may be treated as the purchase of a non-financial (non-produced) asset (AN.229), while the residual regular payments are recorded as a rent for the use of another non-financial (tangible non-produced) asset.

## **Option "rent"**

The payments for mobile phone licences should in principle be recorded as rent "in return for putting the tangible non-produced asset at the disposal of another institutional unit" (ESA 4.41) if the government retains the ownership of the spectrum. In case the financial obligations of the initial purchaser are then settled by way of an initial lump sum payment, the system records it as the purchase of a financial asset by the corporate sector (liability of the general government) (ESA 4.75).

## **Subsequent sale**

In the case of transferable licenses, any subsequent sale is without effect on the general government accounts. Any payments made by a subsequent purchaser/tenant to the initial purchaser/tenant (above the cost of transfer of the financial asset) are treated as the acquisition of a tradable right to use the spectrum that is a non-financial asset (K.2 – ESA 6.12). The time of recording is the time of completion of the subsequent sale (ESA 1.57), irrespective of the time of payments. The non-financial asset acquired is recorded in AN.222 "Leases and other transferable contracts" (ESA 7.19 and Annex 7.1 Definition of each asset category).

## **Committee on monetary, financial and balance of payments statistics (CMFB)**

The CMFB is an advisory committee of senior statisticians from government statistical offices, central banks, the Commission and the European Central Bank (ECB).

On cases which raise questions concerning statistical treatment regarding the calculation of government deficit and debt, Eurostat consults the CMFB before taking its final decision.

### **Consultation of CMFB**

- Eurostat consults the CMFB and notifies its proposals including a timetable.
- The process aims to identify the "best" technical solution for which there is a large support.
- The CMFB seeks advice from its working party, Financial accounts working party, from National accounts working party and from any other expert source it considers appropriate.
- The CMFB opinions are based on ESA 95 rules.
- The CMFB consults its members, analyses results and informs Eurostat of the outcome of the consultation.

### **The process is transparent**

- Eurostat makes its decision and informs at the same time, the Commissioner, the National statistical institutes (NSIs) concerned and the CMFB.
- Eurostat informs the CMFB and the NSIs on which methodological grounds the decisions are based.
- The outcome of the consultation of CMFB and the final decision of Eurostat are made publicly available at the same time.