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# THE Accountant

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## Paul Kazarian:

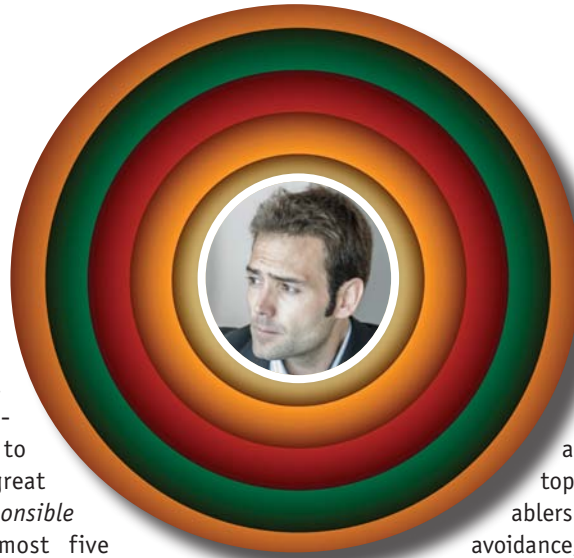


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# Trust's all folks!



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Carlos Martin Tornero, *The Accountant* Editor  
 Journalist of the Year – Regulatory Issues 2014  
 (winner)

Journalist of the Year – Investment 2015  
 (shortlisted)

State Street UK Institutional Press Awards



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So this is farewell. This is my last editorial as I move on to pastures new (a great title called *Responsible Investor*) after almost five eventful years writing for *The Accountant*, as well as contributing to our sister publication *International Accounting Bulletin*.

Who would have thought that accountancy was going to be that much fun? No wonder the years have flown by while I've been closely monitoring this profession.

In the rear-view mirror I can still see, let's call them, evergreen topics which we will probably keep debating well into the future. Here listed are just a few:

An IFRS world without "that country in-between Canada and Mexico" as Hans Hoogervorst, IASB chairman, once said (convergence being a consolation prize).

The EU audit reform and the apparently thorny issues (for some) of rotation and caps on non-audit services (will the reform survive?).

The slightly chimerical emergence of non-financial and sustainability reporting, which accountants want to claim as their property (well done so!).

The lack of healthy competition among accountancy firms, where Big Four inbred families hoard the vast majority of market share, (quite ironic for free market economies, which call this phenomenon consolidation, rather than an utter market failure).

The accounting scandals, whose slap-on-the-wrist response from overwhelmed regulators, surely make investors and everyone (i.e. all stakeholders) wonder if either the auditors were turning a blind eye or that their function is to become a utility bill that serves no further purpose.

Of course, the avoidance of tax avoidance, accountants' favourite topic as chief designers, enablers and marketeers of such avoidance, which contradicts the public service function that profession leaders say accountancy serves.

And the flip side of avoidance: the drop in the tax revenues that pay for public services, and the lack of expertise (and willingness) of governments even to properly account for those shrinking resources, perhaps using IPSAS. But ignorance is bliss and makes politicians unaccountable.

And that's all fair enough. If accountants cannot promote transparency and serve the public interest, because first and foremost they are hired guns of their clients, let's just not pretend otherwise. However, make no mistake, trust can't be earned without encouraging frankness and transparency.

And, believe me, I've talked to stakeholders from the entire world, and everyone is obsessed with recovering trust.

Well, the soul-searching continues, my friends, trust is not possible if you are not a transparency champion. That's why we've devoted much of the ink of this last issue to Paul Kazarian's crusade for transparency in the context of Greece's bailouts.

That's one of his messages: transparency is the precondition for recovering taxpayers' trust. Does this strike any chord? Aren't investors and other stakeholders the taxpayers of accountants' clients?

I hope our readers found this publication relevant under my editorship. Thanks for all your support. I wish you all the best of luck in the future. And remember: that's all, trust's all folks!

**Carlos Martin Tornero**



# Greece's government accounting, "the biggest lie of the century" – Kazarian

Paul B. Kazarian answered fundamental questions about his investigation on Greece's public debt after his presentation at our *The Accountant & International Accounting Bulletin* conference

**Q.1 Audience member:** I might be asking the obvious, but could you elaborate more on why you consider government balance sheets one of the most important reforms, especially for Greece? And, would you comment on how your team's four years of extensive work discovered the size of the Greek government's debt and the amount of Greek debt relief?

**Paul B. Kazarian:** Those are some of the most important questions, and I appreciate you asking. When we are turning around companies, the first thing we have to know is: "Where are they now?" It's such an obvious question. Can you imagine going into any financial situation and not knowing your assets? Not knowing your liabilities? Governments are vastly more complex, so the balance sheet is an even more essential first step.

One legendary hedge fund investor who helped us when we first started back in 1988 said to me when we first considered investing in Greece: "Paul, you won't believe this. You're going into a space where you have to explain to people why a balance sheet is absolutely the starting point for knowing where they are". They [governments] are trying to develop trust. They're trying to develop confidence. And they don't list their financial assets. They don't list their fixed assets. They don't list their non-financial liabilities. They can't even correctly calculate their debt.

And then [governments] go on to try to make decisions; and the decisions they make can destroy, literally, €10 billion, €20 billion, €40 billion in value on a [Greece] population of 11 million and no one is held accountable and nobody discloses the losses. It's like you almost have to pinch yourself when you see some of these numbers. Could the government really have lost €625 million a week since 2014? The answer sadly appears to be yes.

We have a large number of accountants on the team and they ask: "Why are you so focused on the balance sheet? There are other financial statements". Yes, but you want to start with a balance sheet. You want to know the assets. You want to know the calculations. You want to know the valuation. You want to know what assets you're putting on the books for €2 billion that are worth zero, and you want to know ones that you have that you're not putting on your books.

And governments [such as Greece] don't want the transparency, because if you think about it, and I'll just wrap up quickly, if you spend money to buy assets and there's no record of the asset on your balance sheet, what do you think happens to those assets in Greece after they buy them? They can just walk away. Would you have trust? No. That's a horrible thing to say, but that's what we've

found. And looking at the rest of Europe, by the way, it doesn't get an A for quality of transparency of government balance sheet numbers.

I will mention more about the biggest lie of the century, the fake Greek government debt mountain and the failure to report the impact of the debt relief on balance sheet net debt, in a minute as this is the most often asked question.

**Q.2 - Audience member:** You commented on the importance of the government being transparent and reporting accurate financial facts in order to win the trust and confidence of taxpayers and prevent the growing populism from destroying western democracy. Would you elaborate?

**Paul B. Kazarian:** History has proven over and over again that for western democracy to survive the assaults of financial recklessness and populism, the government must win the trust and confidence of the voters and demonstrate that political leadership is a capable financial steward. As we unfortunately see today, most governments do not report a balance sheet. They do not talk about the change in Taxpayers' Equity (which is the government assets less government liabilities), they don't talk about the return on government assets, and they don't talk about the change in GDP as a percentage of the decline in Taxpayers' Equity. In no small part, this is because (based on reviewing the numbers that are reported for the most financially transparent sovereign

governments) Taxpayers' Equity has declined by over double digits annually during the past decade, the return on assets (ROA) has been in the negative high single digits, and the change in GDP as a percentage of the decline in Taxpayers' Equity (which is known as the Value Creation Ratio or VCR) can be as low as a very disappointing 30%.

**Q.3 – Audience member:** Would you elaborate as to why countries seeking to significantly change their financial performance and win the trust and confidence of key stakeholders need senior professionals with decades of successful experience in finance, accounting, and turnaround management?

**Paul B. Kazarian:** Any turnaround is all about the people making the right decisions and quality execution of the decisions. Without judgment built over decades, major decisions will most likely be made in error. And, the execution of even those decisions that, by luck, were made correctly will be executed with continuous errors at higher costs over extended periods of time. These are the facts of reality and the facts of life. Successful professionals know that accurately

(continued on page 24)



## THE WILLIAM PITT THE YOUNGER AWARD FOR EXTRAORDINARY LEADERSHIP IN STRENGTHENING DEMOCRACY THROUGH GOVERNMENT FINANCIAL MANAGEMENT: PAUL B. KAZARIAN

Investor and philanthropist **Paul B. Kazarian** is the chairman and CEO of Japonica Partners and the Charles & Agnes Kazarian Foundation. This entrepreneurial firm founded in 1988 is a private global turnaround investor and manager, whose investment situations include underperforming large cap multinational conglomerates and governments. Before that, Kazarian served as an investment banker at Goldman Sachs.

Kazarian has been actively involved in the promotion of transparency within government finances, becoming one of the most prominent advocates of the international benchmark IPSAS (International Public Sector Accounting Standards).

In the context of Greece's successive bailouts, a country of which Kazarian is one of the largest government bonds holders, he has led the debate on transparency and sound public finance management, notably stimulating intellectual discussions compiled in the campaign website *Most Important Reform*.

Some would argue that he has skin in the game, but thanks to Kazarian we know that Greece's gross debt could be less than 74% of GDP, lower than Germany's 80% of GDP.

Those are figures we would get, if we used IPSAS, which by the way, Germany doesn't want to hear about them.

The William Pitt the Younger Award recognises the work of an individual who has contributed to democracy by winning the trust and confidence of taxpayers through advancing transparency and

accountability of government financial reporting and improving government financial performance.

Carlos Martin Tornero, editor of *The Accountant* said: "Kazarian's work is breaking the shameful silence imposed by short-sighted and self-serving politicians, regulators and other stakeholders of the global

financial industry. His quest for transparency and accountability should be commended and celebrated."

Vincent Huck, editor of *International Accounting Bulletin*, said: "It is an extraordinary challenge that Kazarian is putting to the profession: to dig into its skill and knowhow in order to stand up for transparency in the public interest – a mantra not too far from accountants' intrinsic role, but too often forgotten. So far the profession is coy to rise to the challenge beyond words but talk is cheap!"

Paul Kazarian said: "I am humbled and honoured to

receive **The William Pitt the Younger Award for Extraordinary Leadership in Strengthening Democracy through Government Financial Management**. If western democracy is going to survive populist assaults, governments must regain the trust and confidence of voters with better financial transparency, performance, and accountability. Governments must accept the responsibility to educate current and prospective voters on the importance of internationally comparable government financial statements, especially the impact of government's decisions on the government's balance sheet."



Carlos Martin Tornero, Paul Kazarian and Vincent Huck

### William Pitt the Younger Award acceptance speech by Paul B. Kazarian

Allow me first to warmly thank the Editors of *The Accountant* and the *International Accounting Bulletin*, especially editors, Carlos Martin Tornero and Vincent Huck, for this great honor of being awarded the William Pitt the Younger Award for Extraordinary Leadership in Strengthening Democracy through Government Financial Management. I am obviously extraordinarily humbled to have my name associated with the legendary William Pitt the Younger.

Both of these prestigious publications, with a history extending back to 1874, and their editors, have accepted the very noble

challenge of assisting the accounting profession to help save western democracy, with the cornerstone of government financial management, transparency and accountability, from a growing tidal wave of destructive populism and reckless government financial management.

Our world governments are missing the fresh innovation and quality of government financial management that William Pitt the Younger brought to government over 200 years ago. If western democracy is going to survive populist assaults, governments must regain the trust and confidence of voters with better financial transparency,

performance, and accountability. Governments must accept the responsibility to educate current and prospective voters on the importance of internationally comparable government financial statements, especially the impact of a government's decision on the government's balance sheet.

As many of you know, our firm, Japonica Partners, has historically focused on large multinational corporate turnarounds. It was only in 2012 when we visited Greece that we began to see what happens when a sovereign government's financial management, transparency, and accountability hit rock bottom and even then continues to dig ever-

deeper holes. In a country considered to be the cradle of democracy, how was it possible that government financial transparency and accountability are not only absent but viewed by the political and business elite as a plague to be avoided and – importantly – an Anglo Saxon system to be vilified?

Truthful financial information is not part of their current system. Numbers are to be crafted to say whatever the elite want in order to serve short-term vested interests. The level of brazen untruthfulness is a warning shot to all western democracies.

I will mention just one Greek example. The example may well be the biggest government financial fictional fabrication (aka a lie) of this century. The example is the Greek government debt Chimera. Not a day goes by where there are not dozens of references to so-called mountainous Greece debt. And, the leadership in Greece is the most vocal, telling the world that because its debt is 311 billion euros or 177% of GDP, its finances are unsustainable and the country needs more debt relief to survive.

This, of course, keeps not only investors at bay, but suffocates the economy, and puts fire sale prices on government assets, but – importantly – keeps the focus away from government financial performance and allows the populists to have many enemies to vilify, including those in northern Europe and the IMF.

Those within the government who have attempted to report the correct number

according to international accounting standards have been sidelined, and the IPSAS effort put on the same track as the last seven promises to implement international



accounting for the government, a track to nowhere.

In economic reality and correctly calculated in accordance with international accounting standards, Greece government net debt at the end of 2015 was an estimated 72 billion euros not 311 billion euros. Or, 41%

of GDP, not 177% of GDP. The sources of the difference are not difficult to understand. Greece debt has undergone at least five major debt restructurings since 2010. This means Greece has a huge competitive advantage with debt metrics about half of member state peers.

And, as for debt relief, Greece has received 354 billion euros in debt relief, 17 times more than the Eurozone (EZ) programme country average, but very little of this has been reflected as a reduction in debt, and citing the debt relief numbers within Greece is basically taboo.

Greece has been in a depression for over half a decade. Greece is a lesson in what can happen when a democracy falls to populism and disregards sound government financial management and education of its citizens.

Much of western democracy is under threat of populist assault in no small part for the same reasons Greece has fallen into the abyss and is having such difficulty emerging. If western democracy is going to survive, all key stakeholders must be educated on balance sheets (theirs and their governments), on proper accounting that reflects economic reality, and on the benefits of government financial transparency and accountability.

Thank you again for this extraordinary honour and best wishes in your work to save western democracy from destructive populist assault. ■

6 October 2016,  
Millennium Gloucester Hotel, London

#### BRIEFING: WILLIAM PITT THE YOUNGER

“Son of William Pitt the Elder, Earl of Chatham, William Pitt was Britain’s youngest prime minister, winning the post at the age of 24 in 1783. He is remembered for his tough policies against corruption, fiscal reform, shifting power toward the House of Commons and the union with Ireland. Pitt entered Cambridge at 14 and Parliament at 22. He was Chancellor of the Exchequer in 1782-83. The Tories and friends of George III helped him become prime minister. Unlike his father, Pitt the Younger had a talent for finance. He restructured Britain’s finances, and negotiated new tariffs with France. In 1798 the Irish revolted against his policies. His solution, the Act of Union 1800, included Catholic emancipation which was rejected by the king. Pitt resigned in protest in 1801. Returning as prime minister in 1804, he gained the support of the Austrian, Russian and Swedish leaders in an attempt to defeat Napoleon’s armies. The news of Napoleon’s victory at Austerlitz in 1806 is said to have caused Pitt’s death.”



“Pitt’s political fortunes were determined in part by the impact of events such as the French Revolution and Wars, and George III’s mental illness, and his early years as premier evidenced a determined commitment to reform of the British state. He offered in some ways a new ‘reformist’ model of active, pragmatic prime ministerial leadership followed by many of the most significant political figures of the next half century of

varying party allegiances. The second half of Pitt’s ministry, however, was dominated by the consequences of the French Revolution and the outbreak of war with France in 1793. The wartime situation made it more difficult for Pitt to pursue his administrative reforms and Pitt was forced into a series of expedients to raise the vast sums necessary to sustain the war effort, including in 1799 Britain’s first income tax. The international context also made a resolution of Irish issues more pressing. Following the rebellion of 1798, arose the Act of Union of 1800, a major triumph for Pitt, which saw the United Kingdom of Britain and Ireland come into being on January 1, 1801.”

“Pitt was full of paradoxes. Thus, he was a brilliant scholar who relied on aristocratic privilege to take his degree without taking any examinations; “the champion of the rule of law who nevertheless suspended habeas corpus for most of the 1790s; the denouncer of Whig jobbery and corruption who himself entered Parliament from a ‘rotten borough’ and shamelessly rewarded his own placemen and cronies. Advised to drink port every day for medical reasons, Pitt became a “three-bottle-a-day man”, and ended his life as an alcoholic. Also, at the end of his life, William Pitt was so heavily in debt that the House of Commons had to raise £40,000 to pay off his creditors after his death.”

(Source: JIS Rapid Response Memorandum: William Pitt the Younger) ■



## Strengthening Democracy Through Government Financial Management

### GREECE AND THE EU

Paul B. Kazarian  
 JAPONICA PARTNERS  
 THE CHARLES & AGNES KAZARIAN FOUNDATION  
 The Accountant & International Accounting Bulletin  
 Conference and Awards

Japonica Partners' core competency is discovering, investing in, and then turning around large multi-national conglomerates. However, in 2012, we extended our reach to become one of the largest private investors in Greece government bonds with a goal of helping to accomplish one of the greatest financial turnarounds in history.

Over the past four years, we have built a team of over 100 professionals to assist in our Greek investment. As an aside, over the past four years, we've worked with almost 30 accountants from EY, Deloitte, KPMG, and PWC; several dozen economists; half-a-dozen statisticians; a dozen lawyers; five PR firms; and, scores of former government officials. Also of interest, our team has made more than 250 presentations and we've worked with more than 80 members of the media. Based on our team's extensive work during the past four years, we've concluded that democracy is strengthened through better government financial management for those three reasons (see box).

### How Government Financial Management Can Strengthen Democracy

- Advances transparency and accountability of government financial reporting
- Wins the trust and confidence of taxpayers
- Improves government financial performance

### The Status Quo: Destructive Populism

- Governments see cooking the books after the outcome as the goal, rather than better financial management.
- Fictional fabrication of government numbers is the norm.
- Media, think tanks, rating agencies, and economists have a counter-productive understanding of international accounting standards and economic reality.
- Citizens have almost zero education in understanding a balance sheet, their own or their government's.

It is distressing but hard to otherwise conclude that the status quo is increasingly becoming destructive populism. From our work over the past four years, we have reached those four findings (see box). The Alternative is effective management and communication of government balance sheets prepared in accordance with International Public Sector Accounting Standards (IPSAS)

Many have suggested the IMF as the lead steer on improving government financial management and reporting. We have found that the IMF has the tools and the potential but struggles with implementation. Points worthy of note (see box). Reader of the fact sheet contained in Appendix Two (see page 23) have found the *IMF and Greece: 12 Helpful Facts to Better Understand Greece Government Debt Sustainability (Part 2 of 4)* to be very revealing as to both the strongly siloed functioning of the IMF and the politicalisation of the promulgated noble principles of the IMF. The IMF has the infrastructure. It's not being implemented.

### The IMF has the Tools and the Potential but Struggles with Implementation

- The Fiscal Affairs Department has the publications and technical expertise for report compilation.
- Long list of statements of support for IPSAS.
- Little evidence of assisting in using IPSAS to improve decision-making.
- Political application of rules and guidelines.
- See Appendix 2: IMF and Greece: 12 Helpful Facts to Better Understand Greece Government Debt Sustainability (Part 2 of 4)

## Example 1 of 2: Greece Government Debt and Debt Relief

### Key Stakeholder Statements on Greek Government Debt and Debt Relief

- **The Greek PM:** Debt relief by year-end is an "indispensable condition" to returning to the markets. (Sept. 2016)
- **The Greek FM:** If Greece's EU partners kick the can two years down the road on debt relief, then investors will remain far away, it will be bad for the government and the country, and there should be a discussion about Greece's place in Europe. (Oct. 2016)
- **2017 Budget:** Talks on the restructuring of public debt will play a decisive role on the developments of 2017 as they are a crucial step in restoring investor confidence, the (country's) long-term credit rating and the credibility of the economy. (Oct. 2016)
- **IMF:** Greek government debt remains unsustainable and requires substantial debt relief. (Sept. 2016)
- **Rating Agencies:** S&P: Greece has the highest debt/GDP ratio of all sovereigns we rate. (July 2016). Fitch: Greece has the second highest debt/GDP ratio of all the countries we rate. (Sept. 2016)
- **International Commentators:** For example, Former Citi Vice Chairman: Greece government debt is the barrier to confidence and debt relief is essential. (Sept. 2016)

Let's first set the background (see box with stakeholder views): Greek **Prime Minister's** recent speech in New York; the **government's** official position when it submitted the **2017 budget** this week; the **IMF recent Article IV on Greece** (need for substantial debt relief). The Greek **Finance Minister** said yesterday (5 October) in Parliament that if Greece's EU partners kick the can two years down the road on debt relief, then investors will remain far away, it will be bad for the government and the country, and there should be a discussion about Greece's place in Europe. Yet again, the government is stoking populism by seeking to blackmail Europe.

The **rating agencies** have followed the official pronouncements with headline comments on Greek Government debt: Greece has the highest debt/GDP ratio of all sovereigns **S&P**; and for **Fitch** the second highest.

And, representing the international talking head community, a well-known **international commentator and banker** writes that, Greece government debt is the barrier to confidence and debt relief is essential. You will often hear the kicking-the-can-down-the-road comment about Greek debt restructurings, as if the time value of money and economic reality did not exist when measuring debt.

### Actual Text from May 2016 EU-Greece Agreement on Short-Term Measures has No Debt Relief

- Eurogroup Statement: "For the short-term, the Eurogroup agrees on a first set of measures which will be implemented after the closure of the first review up to the end of the programme and which includes:
  - ✓ Smoothing the EFSF repayment profile under the current weighted average maturity;
  - ✓ Use EFSF/ESM diversified funding strategy to reduce interest rate risk without incurring any additional costs for former programme countries;
  - ✓ Waiver of the step-up interest rate margin related to the debt buy-back tranche of the 2nd Greek programme for the year 2017."
- Dijsselbloem Statement: "The short term is basically a debt management... The possible debt relief -- mainly talking about the medium term package-- will be delivered at the end of the programme, so we are talking mid-2018."
- Regling Statement: "Under the short-term measures, the ESM in our own responsibility will do debt management exercises." As these measures include lengthening maturities, "in the short run, interest costs may go up."

As one more point of background on debt relief, let's review the actual text from the 3rd Programme. The actual text from the May 2016 EU-Greece agreement on short-term measures contains no debt relief despite Greek government statements to the contrary.

### The Current Political Accounting for Greek Debt and Debt Relief

Background facts: Greece rated CCC and 25-year bonds YTM approximately 8%. ESM 30-year bond YTM less than 1%.

	Called Debt Relief	Reported as Reduction in Net Debt
1. €60 billion of 30-year below 1% loans mostly to refinance existing debt.	No	No
2. Rebates of interest and principal.	No	No
3. Concessional loans to purchase financial assets.	No	No
4. Restructured loans with lower interest, grace period, maturity extensions.	Yes	No
5. Change terms on bonds to reduce interest rates and extend maturities.	Yes	No
6. Paying more interest by using swaps to change interest rate profile.	Yes	No
7. Haircut the face value of debt.	Yes	Yes

At the heart of the matter is how Greek debt and debt relief are measured and reported. This table (right) illustrates the current political accounting for Greek debt and debt relief. By way of background facts: Greece bonds are rated CCC and its 25-year bond has a yield to maturity of approximately 8%. The European Stability Mechanism (ESM), which provides much of Greek funding at close to its cost of funding has 30-year bond borrowing costs of less than 1%. The table provides seven transactions and the current political labeling.

Transaction number one is 60 billion euro of 30-year, below 1% loans mostly to refinance existing debt. Under the current political accounting, this is **not called debt relief** nor is it considered a deduction in debt. The same is true for rebates on interest and principal as well as concessional loans to purchase financial assets. Restructured loans with lower interest, grace periods, and maturity extension, are called debt relief but do not have any reported reduction in Net Debt. The same is true for **changed terms on bonds to reduce interest rates and extend maturities**, as well as paying more interest (yes, actually paying more) by using swaps to change interest rate profile. The only transaction called both debt relief and reported as a reduction in net debt is a **haircut to the face value of debt**. When, in fact, all of these items, except number 6, are actually debt relief in economic reality and reduce net debt.

### Since 2010, Greece Has Received €354 Billion in Debt Relief, which is 17 Times More than the EZ Programme Country Average

(€, Billions)

SN		Greece	Greece Multiple of Peers	Peer Average	Portugal	Ireland	Spain	Cyprus
1.	Total Debt Relief/Forgiveness % of GDP	201%	17x	12%	16%	7%	2%	24%
2.	Months in Programme(s)	75+		28	37	36	18	22
Official Sector Debt Relief:								
3.	Pre-Third Programme	€ 182		€ 17	€ 29	€ 14	€ 21	€ 4
4.	Third Programme (to Date)	€ 23		NA	NA	NA	NA	NA
5.	Total Official Sector Debt Relief	€ 205		€ 17	€ 29	€ 14	€ 21	€ 4
6.	Private Sector Debt Forgiveness	€ 149		€ 0	€ 0	€ 0	€ 0	€ 0
7.	Total Debt Relief and Forgiveness	€ 354		€ 17	€ 29	€ 14	€ 21	€ 4
Southern Axis EU Member States Contribution to Greece								
8.		€ 91						
9.	2015 GDP	€ 176		€ 373	€ 179	€ 215	€ 1,081	€ 17

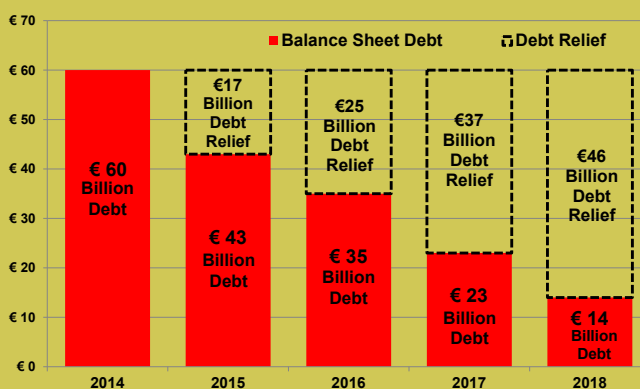
Notes: Japonica Partners collaborative analysis. Based on EC, IMF, and Bloomberg data. Debt relief calculated as of 3 August 2016 according to IPSAS/IFRS.

In stark contrast, the real calculations of debt relief can be found on this slide:

Since 2010, Greece has received 354 billion euros in debt relief, which is 17 times more than the Eurozone programme country average.

### ESM 3rd Programme Debt Relief Will Increase Greece Net Worth by €46 Billion

(€, Billions)



Note: Estimate as of 31 December 2015.

The 2015 ESM 3rd Programme by itself has the potential to provide debt relief of 46 billion euros, which from a balance sheet perspective will increase Greece government net worth. What is particularly surprising here is that for the current government so desperately seeking to gain some kind of political win from debt relief, they do not acknowledge this as debt relief.

A recent Harvard Business School article by a London Business School Page 4 of 8 professor, Michael Jacobides, explains this by saying it is byzantine not classic Greek logic where the current government would rather not take credit for having new concessional loans so as not to have to give credit to prior governments for their much larger success on winning debt relief.

**Greece 2015 YE Balance Sheet Net Debt, Correctly Calculated in Accordance with International Accounting or Statistics Rules is 41% and 58% of GDP, Respectively: Summary (€, Billions)**

1. Rules:	International Accounting Standards (IPSAS/IFRS)	2008 System of National Accounts (2008 SNA)	European System of Accounts 2010 (ESA 2010)	IMF Debt Sustainability Analysis (DSA)	Lisbon Treaty Excessive Deficit Procedure* (EDP)	
					FFV	PV
2. Gross Debt	€ 125	€ 155	€ 155	€ 203	€ 311	€ 155
3. Gross Debt % of GDP	71%	88%	88%	116%	177%	88%
4. Net Debt	€ 72	€ 102	€ 102	€ 183	NA	NA
5. Net Debt % of GDP	41%	58%	58%	104%	NA	NA

Debt metrics for Greece EZ member state peers are not reduced under ESA 2010, 2008 SNA, or IMF DSA as there is no qualifying concessional or reorganized debt; and under IPSAS/IFRS, Portugal, Spain, and Ireland would report lower debt by approximately €23 billion, €18 billion, and €12 billion respectively.

This slide, which has taken an enormous effort by our team, shows the gross and net debt of the Greece government debt under six different debt measurement frameworks. As you can see, Greece government 2015 year-end balance sheet net debt, correctly calculated in accordance with international accounting standards or international statistics rules is 41% and 58% of GDP, respectively. To increase our confidence in our analysis, one of the Big Four confirmed our debt numbers following an almost half-year assignment and a 54 page Expert's Opinion. The international accounting standards are IPSAS and IFRS. The international statistical frameworks are 2008 SNA and ESA 2010. Under the IMF debt sustainability guidelines, Greece government net debt is higher but is still only 104%.

Under the Lisbon Treaty, there is the EDP headline measurement, which uses face value, and for Greece is the more familiar 177%. However, EDP submission forms also have a table for the disclosure of present value of gross debt, under ESA 2010, which for Greece would be 88%. It is worth noting that the Greece government has left this table blank with no present value of debt number inserted where required. Debt metrics for Greece EZ member state peers are not reduced under ESA 2010, 2008 SNA, or IMF DSA as there is no qualifying concessional or reorganized debt; and under IPSAS/IFRS, Portugal, Spain, and Ireland would report lower debt by approximately €23 billion, €18 billion, and €12 billion, respectively.

Notes: Japonica Partners collaborative analysis. \*EC 479/2009 "Whereas (4)" states "The definition of 'debt' laid down in the Protocol on the excessive deficit procedure needs to be amplified by a reference to the classification codes of ESA 95". 2015 GDP of €176 billion from EC AMECO database and financial asset data from Eurostat (accessed 19 July 2016).

**Greece Has Been Given a Significant Debt Competitive Advantage, with a Debt Burden of About 50% of Investment Grade EZ Member State Peers, but Earns Worse Ratings and Higher Borrowing Costs**  
(% of GDP, except as otherwise indicated)

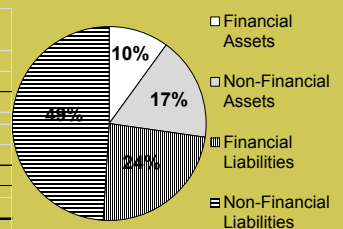
	August 2016 Credit Ratings (M/S&P/F/D)	2015 Balance Sheet Net Debt	2016 Annual Debt Service	2016 Net Cash Interest	Next 5-Years Unfunded Debt Service	3-Year Govt Bond Yields (YTM)
<b>Greece as % of Peers</b>		52%	50%	57%	27%	8.56%
Greece	Caa3/B-/CCC/CCCH	41%	6%	2.0%	16%	8.68%
Ireland	A3/A+/A/AH	54%	9%	2.8%	46%	-0.43%
Spain	Baa2/BBB+/BBB+/AL	69%	13%	2.9%	58%	-0.09%
Italy	Baa2/BBB-/BBB+/AL	113%	15%	4.0%	74%	0.03%
Portugal	Ba1/BB+/BB+/BBBL	80%	11%	4.6%	61%	0.98%

Notes: Japonica Partners collaborative analysis. Future Face Value of Debt (Maastricht) as a percentage of GDP: Greece 177%, Ireland 94%, Spain 99%, Italy 133%, Portugal 129% (EC AMECO data accessed 3 August 2016). Based on EC, Eurostat, IMF, Member State MOFs, and Bloomberg data (Govt Bond Yields as of 4 October 2016).

To put these debt numbers in perspective, our team compared the Greek numbers to four peer countries, and we also expanded the comparison to include three additional debt metrics. As you see, Greece has been given a significant debt competitive advantage, with a debt burden of about 50% of investment grade Eurozone member state peers, but earns worse ratings and higher borrowing costs. Not only is Greece government net debt 52% of peers, but Greece is also 50% of 2016 annual debt service, 57% of 2016 net cash interest, and 27% of the next 5-year unfunded debt service.

**At Year-End 2015, the Greece Government had Over ½ Trillion Euros in Assets and Liabilities to Manage or Mismanage, which is €48,060 per Citizen (€, Billions; as of 31 December 2015)**

SN	Balance Sheet Item	Amount
1.	Financial Assets	€ 52
2.	Non-Financial Assets	€ 90
3.	Total Assets	€ 142
4.	Financial Liabilities	€ 125
5.	Non-Financial Liabilities	€ 255
6.	Total Liabilities	€ 380
7.	Net Worth	-€ 238
8.	Total Assets and Liabilities	€ 522



To overcome the lack of a government balance sheet, our team developed an estimate of major balance sheet categories and an estimated net worth for the Greek general government. As you can see, at year-end 2015, the Greece government had over ½ trillion euros in assets and liabilities to manage, which is 48,060 euros per citizen. To state what should be obvious, these are enormous amounts to manage without proper financial statements.

Notes: Japonica Partners collaborative analysis. Working draft balance sheet. For additional details, see Japonica Partners 30 April 2016 USC Global Leadership Summit presentation: mostimportantreform.info/MAGARIAN\_USC\_20160430.pdf.

**Analysis Indicates that €69 Billion, or on Average €625 Million Per Week, of Greece Government Asset Value was Lost from 2014 to August 2016**

One last slide of importance is our team's historical analysis of Greece government assets. The analysis indicates that 69 billion euros, or on average 625 million euros per week, of Greece government asset value was lost from 2014 to August 2016 (which is the latest date of our analysis). The significance of this loss is **breath taking**. Additional details on <http://mostimportantreform.info>

SN	Greek Government	2014	2016	Identified Value Lost	
				Amount	Percentage of 2014
1	Financial Assets	€109 Billion	€71 Billion	€40 Billion	37%
2	Non-Financial Assets	€115 Billion	€86 Billion	€29 Billion	25%
3	Total Assets	€224 Billion	€157 Billion	€69 Billion	31%
4	Value Lost Per Week			€625 Million	
5	Value Lost Per Greek Citizen			€ 6,275	

Notes: Japonica Partners collaborative analysis. Identified Value Lost may differ from change in Financial Assets due to additions and disposals. From 30 June 2014 to 3 August 2016 or closest date of data available. Per week calculation based on 109 weeks. Based on population of 10.9 million from EC AMECO database and unconsolidated general government financial asset data from Eurostat (accessed 3 August 2016). Non-Financial Assets estimate based on data from Japonica Partners 30 April 2016 USC Global Leadership Summit



## Example 2 of 2: The EU CEPS Balance Sheet Task Force

EU General Government are a Very Significant Part of the Economy with Total Expenditures an Average 46% of GDP

SN	Country	Total Expenditure % of GDP	SN	Country	Total Expenditure % of GDP
1	Finland	58%	15	Germany	44%
2	France	57%	16	Malta	43%
3	Denmark	56%	17	Spain	43%
4	Greece	55%	18	United Kingdom	43%
5	Belgium	54%	19	Czech Republic	43%
6	Austria	52%	20	Luxembourg	42%
7	Hungary	51%	21	Poland	41%
8	Italy	51%	22	Bulgaria	40%
9	Sweden	50%	23	Cyprus	40%
10	Portugal	48%	24	Estonia	40%
11	Slovenia	48%	25	Latvia	37%
12	Croatia	47%	26	Romania	36%
13	Slovakia	46%	27	Ireland	35%
14	Netherlands	45%	28	Lithuania	35%
			<b>Average:</b>		<b>46%</b>

To put the importance of the government's role within Europe in perspective, let's look at the contribution to GDP. On average, EU general government total expenditures are 46% of GDP. Greece general government is 55% of GDP. To put this in layman's terms, **how government finances are managed or mis-managed really matters.**

Source: EC AMECO database; 2015 data (5 July 2016).

### Examples of Government Actions Designed to Misrepresent Reporting Economic Reality

1. Concessional loans without recognition
2. Expensive PPPs to avoid budget costs
3. Sale and leasebacks
4. Government employee pensions non-reporting
5. Impaired financial and fixed assets
6. Primary balance illusions
7. Delayed payments on asset procurement of defense assets
8. Excluding capital grants from expenses
9. Excluding new borrowing to fund "temporary" investments
10. Issuing premium bonds and booking at par.

### Government Balance Sheet Status in the EU

1. Consolidated balance sheets are the exception not the rule.
2. Single-entry accounting (in contrast to double-entry) is the most common.
3. Knowledge of consolidated financial statements as a management tool to improve performance and minimize risk is almost non-existent.
4. Limited management capability exists to realize better balance sheet performance.
5. Significant performance gaps exist between potential balance sheet performance and current status.

Review of the team's summary of findings regarding the status of government balance sheets in the EU, and government actions designed to misrepresent reporting economic reality.

## Key Balance Sheet Metrics for Global Benchmarks Highlight Wide Performance Gap (2001 to 2015)

	Rank #1	Rank #8	Median	Definition
1. Value Creation Ratio	NWI 70% of GDP	0.3x	2.0x	Change in GDP per unit change in Net Worth start point to end point.
2. Return on Assets (ROA)	4%	-38%	-7%	Average annual change in net worth as a % of total assets.
3. Net Worth % of GDP - Latest	38%	-158%	-66%	Latest period end net worth as a % of latest year GDP.
4. Net Worth Annual % Change	19%	-13%	-4%	Average annual percentage change in net worth during period.
5. GDP Change to Debt Change Ratio	651%	53%	147%	GDP increase per unit of debt increase start point to end point.
6. Net Debt % of GDP - Latest	3%	64%	30%	As reported balance sheet net debt as a % of GDP.

Notes: 2001 to 2015 data or all available data from this period.  
 Value Creation Ratio: Full period change in GDP divided by change in Net Worth.  
 Return on Asset (ROA): Change in net worth as a percentage of assets.  
 Net Worth as % of GDP - Latest: Latest period end (2014 or 2015) net worth divided by corresponding year GDP.  
 Net Worth Annual Percentage Change: Annual change in year end net worth.  
 GDP Change to Debt Change Ratio: GDP increase as a % of debt increase.  
 Net Debt % of GDP - Latest: Latest period end (2014 or 2015) net debt (debt less financial assets) derived from respective government balance sheets divided by corresponding year GDP.

A primary goal of the Task Force is to develop key balance sheet metrics that can be used to highlight potential performance gaps. To advance this mission, the team began by identifying those countries, anywhere in the world, that had government financial statements of sufficient quality to make comparisons. The team identified the following countries: Australia, Canada, France, Israel, New Zealand, the Swiss Federation, the United States, and the UK Whole of Government.

The next step was to identify a handful of key performance metrics (KPIs) that had the balance sheet at the core and combined these numbers with other financial statements as well as with one of the most economic statistics, GDP. As an aside, some of our analyses use GNI, when the GDP number appears to be statistically misleading. The six KPIs we settled on are as per the box (left). As you can see, all the KPIs have a very wide range from those ranked number one to those ranked number eight (last among the group). Let me take a minute to review the medians for each of the six KPIs. The average Value Creation Ratio is 2.0 times, which means that GDP increases at twice the rate of the decline in net worth. You can think of this as **the price paid for the growth in national wealth.** Yes, this gives the government the full credit for the GDP growth that is overly generous. And yes, this ratio compares a flow and a stock number, but so does the debt to GDP ratio. The median return on assets was a not very impressive negative 7%. The median net worth as a percentage of GDP is a negative 66%. The median annual change in net worth was a negative 4%. The GDP change to debt change ratio was 147%, which means that GDP increased by a multiple of debt. And, net debt as a percentage of GDP was 30%.

### Value Creation Ratio: Increase in GDP per Citizen as % of Change in Net Worth per Citizen (Local Currency, Billions)

Global Benchmark	Value Creation Ratio	Increase in GDP per Citizen	Decrease in Net Worth per Citizen	Beginning Year
New Zealand, Government of	Net Worth Increased 70% of GDP	25,000	Increased 17,609	2001
Swiss Confederation	Net Worth Increased 4% of GDP	6,543	Increased 247	2009
Canada, Government of	10.1x	24,704	-2,451	2001
Australia, Commonwealth of	3.3x	38,559	-11,568	2001
Israel, Government of the State of	0.6x	49,512	-77,317	2006
United States Government	0.6x	23,021	-36,863	2001
United Kingdom (Whole of Government)	0.4x	5,132	-13,132	2010
France, Republic of	0.3x	5,180	-20,407	2006

Additional details on the Value Creation Ratio for each benchmark. As you can see, **New Zealand and the Swiss** are top ranked with both a GDP increase and a net worth increase. The UK and France are the bottom with only 0.4 and 0.3 increases in GDP as percentage of the decline in net worth.

Notes: Nominal GDP from EC AMECO and IMF World Economic Outlook (Oct 2015) databases. Net worth data from respective government financial statements. France and Swiss liabilities adjusted for pension commitments. UK assets adjusted for undervaluation of infrastructure assets. Canada and United Kingdom based on prior year GDP due to 31 March fiscal year end.

**Return on Assets Ratio (ROA)**  
(Change in Net Worth as a Percentage of Assets)

There is a wide performance gap on net worth return of assets ratios.

Additional details on the ROA for each benchmark. Once again, New Zealand and the Swiss take top rank with positive historical averages. The United States is at a distant bottom with a minus 38%.

	Historical Average	2011-2014 Average
<b>Global Benchmark</b>		
New Zealand, Government of	4%	-2%
Swiss Confederation	0.46%	0.52%
Canada, Government of	-1%	-6%
Australia, Commonwealth of	-4%	-13%
United Kingdom (Whole of Government)	-11%	-10%
Israel, Government of the State of	-16%	-23%
France, Republic of	-17%	-18%
United States Government	-38%	-37%

Notes: Net worth and asset data from respective government financial statements. France and Swiss Net Worth adjusted for pension commitments. UK net worth adjusted for undervaluation of infrastructure assets. Historical average from oldest available data point (since 2001) to newest data point: Australia 2001-2015, Canada 2001-2015, France 2006-2014, Israel 2006-2014, NZ 2001-2015, Switzerland 2010-2014 UK 2011-2014, US 2001-2015.

**A Framework to Understand How Knowledge and Management of a Government Balance Sheet Improves Financial Performance and Risk**

	Financial Performance	Risk
<b>Knowledge</b>	<b>Q1:</b> To have true and fair internationally comparable knowledge of government financial performance, the balance sheet, the supporting consolidated financial statements, and notes are the starting point for decision-making and accountability.	<b>Q3:</b> The balance sheet at the core of consolidated financial statements provides standardized and quantified knowledge of risks (especially large, complex, and expanding liabilities) and helps expose masking of financial risks.
<b>Management</b>	<b>Q2:</b> Capable management using three balance sheet related decision-making tools (modified T-accounts, financial statements, and performance gaps) can improve financial performance and changes in net worth, and minimize errant decisions.	<b>Q4:</b> Early risk management of potential asset impairment or opaque liabilities is an effective process to reduce costs by limiting or avoiding the materialization of these risks and strengthens accountability.

Given that the Task Force mission is to educate a very wide range of individuals, an early step in the process was to develop a one-page sheet that facilitated communication and education on why and how a balance sheet is important. As a result of a long collaborative process, the Task Force developed a slide titled: A Framework to Understand How Knowledge and Management of a Government Balance Sheet Improves Financial Performance and Risk. The framework has four quads. The two column headings are Financial Performance and Risk. The two rows under each column heading are Knowledge and Management.

The Task Force knows that an important part of its role is to make its work immediately implementable. To advance this outcome-focused goal, the Task Force selected three basic decision-making tools. The first two items you will be familiar with: a modified T-account and the four financial statements. The third tool, performance gaps, uses the KPIs we discussed earlier

**Three Basic Decision-Making Tools**

1. Modified T-Accounts
2. Financial Statements (Four)
  - Balance Sheet
  - Performance Statement
  - Cash Flow Statement
  - Statement of Changes in Net Worth (Taxpayers' Equity)
3. Performance Gap

**Tool 3 - Performance Gap Framework: EU Summary**

(€, billions)

	Value Creation Ratio KPI		Return on Asset (ROA) KPI	
	Ratio	GDP Increase	Ratio	Net Worth Change
EU Current (Est.)	0.3x	€ 309	-8%	-€ 1,212
Benchmark KPI	0.8x	€ 825	-5%	-€ 757
Performance Gap	0.5x	€ 516	3%	€ 454
Performance Gap % of GDP		4%		3%

Let me take a minute to explain the third tool, the performance gap. To develop an early working draft performance gap analysis, the Task Force selected two KPIs: The Value Creation Ratio KPI, and the Return on Asset KPI. The next step in this process was to develop EU aggregated member states financial number estimates. These estimates are in row one titled EU Current (estimate). The next step was to identify a credible benchmark proxy. The proxy selected was a combination of the better performing countries in the group of eight benchmarks. The performance gap is the difference between the EU current numbers and the benchmark. Using the Value Creation Ratio KPI, the performance gap is an additional GDP of 516 billion euros. Using the Return on Assets KPI, the performance gap is an additional 454 billion euros. The numbers are close at around 3% to 4% of GDP.

## Proposed Sovereign Index

Total Ranking: 0-20 (Poor), 20-30 (Fair), 30-40 (Good), 40+ (High)

	Weighting	Ranking
<b>Qualitative Factors</b>	50%	
<i>Rankings: 0 (Worst), 1 (Poor), 2 (Fair), 3 (Good), 4 (Best)</i>		
1.1 Accounting Principles	7%	
1.2 Audit	7%	
1.3 Budget	7%	
1.4 Financial Statements	7%	
1.5 Fiscal Management	7%	
1.6 Fiscal Oversight	7%	
1.7 Human Capital	7%	
<b>Quantitative Factors</b>	50%	
<i>Quartile Rankings: 1 (Bottom), 2 (Second), 3 (Third), 4 (Top)</i>		
2.1 Net Worth Value Creation Ratio	7%	
2.2 Net Worth Return on Asset Ratio	7%	
2.3 Net Worth % of GDP - Latest	7%	
2.4 Net Worth Annual % Change	7%	
2.5 Total Liabilities Value Creation Ratio	7%	
2.6 GDP Change to Debt Change Ratio	7%	
2.7 Net Debt % of GDP - Latest	7%	
<b>Total:</b>	100%	

One last point to make regarding the Task Force is its work in developing a government financial management index to be included into the credit rating agency sovereign rating frameworks. The Task Forces has and continues to carefully study the sovereign government rating frameworks of the four majors rating agencies: Moody's, S&P, Fitch, and DBRS. Using existing framework precedents, the Task Force has a first draft proposed Sovereign Index to be included as a significantly weighted component of the main rating framework, which has dozens of other factors. As you can see, there are two parts, qualitative factors and quantitative factors. Within each, there are seven component factors. As a preliminary start, all factors have been given equal weighting. We have recommended that this index be given a 20% weighting. In order for this index to become operational, a database on at least 40 sovereign governments will be necessary.

## Best - Worst Practices Performance Gap: Illustrative Balance Sheet Line Items (1 of 2)

	Best Practice	Worst Practice
	<b>Financial Assets:</b>	
1.	Internal cost of capital allocation.	Ignore existence of working capital and its cost.
2.	Benchmarking to achieve top quartile performance.	Bottom quartile performance or no benchmarking or management of financial assets.
3.	Better returns and minimized risk exposure on politically influenced loans.	Opacity and large losses on politically influenced loans.
4.	Full disclosure of financial assistance to and returns on SOEs.	Hidden SOE economic burden and risk.
	<b>Non-Financial Assets:</b>	
5.	Optimal re-investment in and use of real estate assets.	Chronic mismanagement of potentially high value commercial real estate assets.
6.	Low and declining single digit percentage fraud in accounts receivable.	Double digit percentage fraud in accounts receivable payments.
7.	Projects built based on lowest cost to financial metrics.	Public private partnerships with private party has required double digit rate of return, including sale-and-leasebacks.
8.	Concessions that both maximize long term value creation and improve value for the money in delivery of services.	Front-end load inflows to fund exiting (or even worse, new promises) annually recurring operating expenditures.
9.	Asset depreciable lives that encourage high ROI program maintenance.	Unrealistically long depreciation lives that short change program maintenance and create larger replacement costs in the future.
10.	Measure and report real estate tax basis appreciation in areas surrounding government infrastructure investments.	Ignore reporting and accountability for impact of infrastructure investments.
11.	Annual impairment reviews of tangible and intangible assets create discipline to protect asset value.	No balance sheet and/or no proper annual review hides asset value destruction.

As part of its education role, the Task Force has developed a database on best practices and worst practices.

The practices are filed into four groups: financial assets, non-financial assets, financial liabilities, and non-financial liabilities.

### (2 of 2)

	Best Practice	Worst Practice
	<b>Financial Liabilities:</b>	
12.	International standards and audits.	Incorrectly calculating balance sheet debt.
13.	Report pro-forma impact on financial statements.	Ignoring quantification of debt relief impact on net worth.
14.	Use all three tools to understand economic impact of liability management exercises.	Liability management without consideration of financial statement impact.
	<b>Non-Financial Liabilities:</b>	
15.	Payables paid on exact date due.	Incur and not report interest penalties on arrears.
16.	Disclose impact on financial statements of change in government employee pension terms.	Non-quantification of balance sheet impact of change in government employee pension terms.
17.	Quantifies and proactively manages litigation risk.	Ad hoc post-event handling.



## Appendix 1: The Facts on Greek Government Financial Sustainability and Stability (Part 1 of 4)

- 1. Greek Government Received Massive EZ Debt Relief:** The southern axis countries have given Greece €128 billion in highly concessional loans with an opportunity cost to southern axis taxpayers of €8 billion per year. Since 2010, Greece has received €354 billion in debt relief, which is 17 times more than the EZ programme country average. The 3<sup>rd</sup> programme has already provided €23 billion in debt relief. Additionally, Greece receives on average €6.6 billion per year in EU funds which is 251% of comparable size Portugal and Ireland.
- 2. Greek Government Significant Debt Competitive Advantage:** The Greek government has been given a significant debt competitive advantage, with a debt burden of about 50% of investment grade EZ member state peers, but earns worse ratings and higher borrowing costs. Greece 2015 YE Balance Sheet Net Debt, correctly calculated in accordance with international accounting or statistics rules is 41% and 58% of GDP, respectively. Greece will save €10 billion from a lower cash interest burden compared to the southern axis from 2016 to 2020. Greece debt service is 50% of EZ peers versus a gross financing needs of 123%. Greece floating rate debt is only 17% of total debt, not the 69% reported.
- 3. Greek Government High Capital Spending:** The Greek government spent on average €364 million per week on capital spending from 2013 to 2015, which is 297% of comparable size Portugal and Ireland.
- 4. Greek Government Total Balance Sheet of ½ Trillion Euros:** At year-end 2015, the Greek government had over ½ trillion euros in assets and liabilities to manage or mismanage, which is €48,060 per citizen.
- 5. Greek Government €69 Billion Asset Value Lost:** Analysis indicates that €69 billion, or on average €625 million per week, of Greek government asset value was lost from 2014 to August 2016. From 2001 to 2015, Greece added only 10 cents in GDP for each additional euro of debt, compared to EZ peer average 45 cents.
- 6. Greek Government Little Progress in Financial Transparency:** Little progress on Greek government financial transparency and accountability processes to win the trust and confidence of taxpayers. No opening balance sheet. No senior level ministers with professional turnaround, financial, or accounting experience.

## Appendix 2: IMF and Greece: 12 Helpful Facts to Better Understand Greece Government Debt Sustainability (Part 2 of 4)

On 23 September 2016, the IMF released a Greece Article IV Mission Staff Concluding Statement, a useful complement to its May 2016 Debt Sustainability Analyses. The headline message is that Greece government debt is unsustainable, further debt relief is required, and debt continued to rise reflecting shortfalls between economic outcomes and Greece's ambitious targets. (Article IV, page 3)

The following are 12 Helpful Facts to Better Understand Greece Government Debt Sustainability:

- 1. Trust and confidence:** Contrary to the IMF's long-standing tradition, the Statement does not acknowledge building trust and confidence as a cornerstone of government responsibility and omits from its recommendations a most important reform for Greece, which is transparency and accountability of financial information. Despite IMF advocating IPSAS for transparency and accountability of government financials, especially balance sheets, in numerous publications, the Statement makes no mention of these reforms for Greece exposing the IMF to criticism for showing creditor bias in not wanting to report the correct value of Greece government 2015 net debt/GDP of 41%, thereby advancing the IMF's economic interests. Of note, the IMF uses similar rules (IFRS) for its own balance sheet.
- 2. Debt relief:** The DSA acknowledges the "very large NPV (net present value) relief" provided by the EU to Greece, but does not report the impact on Greek balance sheet debt. (DSA May 2016, page 1)
- 3. DSA on PV:** Although the IMF's guidelines for highly concessional loans recommend the present value of debt be reported in debt sustainability analyses, present value is not reported for Greece. (Public Debt Limits June 2015, page 27) Using the IMF guidelines and public information, Greece 2015 gross debt/GDP was 116% and net debt was 104%.
- 4. Debt/GDP:** The IMF states clearly that Greece's "debt/GDP ratio is not a very meaningful proxy for the forward-looking debt burden", but continues to make it a headline target for decision-making. (Preliminary DSA June 26, 2015, page 11)
- 5. Concessional debt:** Replacing debt that matures at face value with highly concessional debt with a present value as low as 20% of future face value is recorded as no change in Greece government debt by the IMF rather than reflecting the economic reality that debt actually declined by up to 80%. Recording restructured debt at present value, also known as initial recognition value, is a global best practice for independently developed international rules, such as IPSAS, IFRS, 2008 SNA, and ESA 2010.

## Appendix 3: Additional Readings

- "Greece's New Agreement with Europe: This Time Different?" *Intereconomics*. September/October 2015. **Pelagidis, Theodore and Kazarian, Paul B.**
- "Greece's Debt: Sustainable?" Harvard Business School Case Study. June 2015. **Serafeim, George**
- "The Curious Case of the Rules for Calculating Debt Relief: A Technical Note on EU Accounting for Debt, Especially Restructured and Concessional Debt." September 2015. **Ball, Ian**
- "Greece Needs to Be Honest About the Numbers." Harvard Business Review. September 2016. **Jacobides, Michael**
- "Greece's Bailout Package: Missing IPSAS?" *The Accountant*. September 2015. **Tornero, Carlos**
- "What if Greece got massive debt relief but no one admitted it? (Part 2)" *Financial Times*. 9 June 2016. **Klein, Matthew C.**

Appendix 1 and 2 are part of a Japonica Partners' campaign aimed at educating Greece key stakeholders globally to better understand Greece government debt sustainability. To that end, Japonica Partners arranged in October a 14 full-page multimedia buy in the *Financial Times*, the *International New York Times*, and the *New York Times*. The campaign was announced at *The Accountant & International Accounting Bulletin's* conference, ahead of its publication.

Japonica Partners stated: "The uneducated recalcitrants who continue to cite incorrect Greek government debt numbers will be taught the international debt measurement rules and the benefits of correctly calculating Greek government balance sheet numbers."

"To illustrate the importance of balance sheet numbers prepared in accordance with international frameworks designed to best reflect economic reality, Greece has a significant debt competitive advantage with correctly calculated government net debt of €72 billion (41% of GDP) at year-end 2015. The oft-cited future face value of €311 billion (177% of GDP) does not reflect economic reality and is being misused in assessing Greece debt sustainability."

"The correct Greece government balance sheet net debt number was calculated by a multi-disciplinary global team of 100 plus professionals under the direction of Japonica Partners over the past four years."

- 6. Restructured debt:** The IMF GFSM guidelines are the only internationally applied rules that do not seek to report the economic reality that rescheduled debt is extinguished and recorded at fair value on the date of rescheduling. Sections A3.12-13 are superficially harmonized with the international consensus saying that "rescheduled debt is considered repaid and replaced with a new debt instrument created with new terms and conditions" and recorded at the "value of the new debt". However, inserted parentheses directly undermine the harmonized text and defy economic reality by adding, "which, under a debt rescheduling, is the same value as the value of the old debt". Furthermore, the GFSM again favors creditors by diverging from international standards and economic reality in section A3.15 requiring debt refinancing in the replacement of existing debt to be recorded at the value of the new instrument by inserting the text, "except for nonmarketable debt (e.g., a loan) owed to official creditors".
- 7. Use of proceeds:** Incurring highly concessional debt to invest in financial assets is reported as a debt increase by the IMF. In economic reality, receiving highly concessional loans and investing in financial assets decreases Greece government net debt as the asset value exceeds the initial value of debt.
- 8. Interest rates:** There is an irreconcilable *non sequitur* between the Statement concluding that the debt stock number is not "meaningful" and using that same number to project interest rates in the DSA.
- 9. Asset losses:** The Statement does not mention the tens of billions of euros in Greece government asset value lost as the main cause for the increase in Greece net debt, a key metric used in other DSAs. Our estimate of government asset value lost is €69 billion or €625 million per week.
- 10. GFN:** Gross financing needs should not replace debt service as a key metric, as about 75% of projected GFN components are not conventional debt service but IMF discretionary assumptions. Conventional debt service for Greece would be approximately 50% of peers.
- 11. Projections:** Half-century projections are not credible. Assumptions for Greece on growth, interest rates, and fiscal balances if applied to many EU member states would show similarly unsustainable debt metrics.
- 12. Loan profitability:** Greece has paid over €3.5 billion in interest payments and fees to the IMF, averaging 37% of IMF total net income, and covering 79% of IMF total administrative expenses. Over the past five years, the IMF had an average operating margin of 63%, a multiple of major banks.

(continued from page 2)

calculated numbers are essential for good decision-making. As the well-known words of wisdom say, “you can manage better what you measure accurately”. And, as the ancient proverb says with regards to the importance of experienced professionals: just because you are a good shoemaker doesn’t mean you can play the fiddle.

**Q.4 - Audience member:** You calculated the Greek government debt according to all the international standards, which must have been an enormous effort. How difficult is it to educate those who have vested interests in defending a future face value number that is both highly destructive and does not reflect economic reality?

**Paul B. Kazarian:** It is super hard to change those that benefit economically and politically from using the fake debt number. It starts with educating those who have a good faith interest in obtaining the facts and not perpetuating the biggest lie of the century. Greek politicians continue to cry wolf about a future face value of debt, when in fact the Greek government debt is among the lowest in the Eurozone at either 41% or 58% of GDP depending on which international standard you use (IPSAS/IFRS or ESA 2010/2008 SNA). And, yes I did say that Greek net debt calculated correctly under ESA 2010 was 58% of GDP at year-end 2015 based on publicly available data. The Greek government has received over €350 billion in debt relief, 17 times more than peers, and the political elite will not admit to one cent of this debt relief to its citizens. In fact, the current government formed an Orwellian-named Truth in Debt Committee, which concluded that the government should not honor any of its debt because it was all odious. The government continues to deny that the 3rd Programme has debt relief built into each extraordinarily concessional loan with about 40 year maturities, grace periods, and interest below one percent. They have this Byzantine, not classic Greek, logic in that they would prefer to go down in failure rather than admit that prior governments reduced debt with debt relief. Combine the crying wolf with the fake debt mountain and the denial of 3rd Programme debt relief, Greece will go down in history as creating and perpetuating one of the biggest lies of this century.

**Q.5 - Audience member:** I have a question for Paul Kazarian. I found your presentation very enlightening and very interesting. I had no idea, like many of us here in this room on the real debt and debt relief numbers that you just discussed. Another figure that stood out was the €625 million of assets that are destroyed every week. Can you elaborate what do you mean by that? I mean, is it financial assets?

**Paul B. Kazarian:** There’s a detailed backup on the website, so you can see it there, because we thought it helpful to disclose this informa-

tion, partly for the government. I’m going to give you the first couple of major categories. First, they put around €37 billion of money they borrowed into their banking system in 2013. They bought a large percentage of the four system banks. They owned around 86% of some of the systemic banks. These equity stakes are now greatly diluted and the value of that €37 billion is around €500 million. That’s real money.

We were fortunate enough to have a reporter ask the Greek finance minister this question about the €30 billion. As is typical protocol during an interview with many members of the press present, his response was on tape. The minister gave a defense by saying that they had lost no money on the bank investments because that’s not the way an economist looks at it. You can hear the audio with subtitles on *MostImportantReform.info*.

Second, you may remember that slide I put up about the rebates of principal and interest. Under the second bailout agreement, there

was an agreement with the EZ that Greece would get rebated around €13 billion of interest and portions of principal (because they had bought their Greek bonds when they were below par) paid to the ECB and NCBs. It worked out to around €13 billion. Because they violated the agreement so repeatedly, they breached the contract and lost the present value of €8 billion in those rebates. There may be the opportunity to recover these funds, but it will take a super credible

and professional team from Greece.

This year alone, Greece lost €1.3 billion in rebates. This loss is on €90 billion of spending. Meanwhile the government is trying to get a primary balance of 0.5% of GDP, which is about €800 million. So, you are talking about almost double the primary balance target. The Greek government just lost €1.3 billion in rebates because they breached the contract. And when this loss was brought up in a recent Greek Parliament debate, the government provided no response. None.

I can go down the list, category by category, fire selling assets: because you have cap rates on your real estate that are 14% compared to the countries that are 4% to 5%, and because the Greek political elite continue to cry wolf about the fake debt mountain and tout that the country is bankrupt, assets are going at prices 40% to 50% of normalized value.

Furthermore, the Greek government put a committee together to implement IPSAS. By way of background, this is the seventh time since 1995 that the government has committed to international accounting standards. The committee has a massive 28 people. And how many of them are CPAs with experience in implementing IPSAS? None. In fact, only one person is a CPA. And, he is 85 years old and has been retired for years. The Greece government does not have a balance sheet. The money that procures assets is booked as an expense and the assets effectively disappear until the government



Paul Druckman (IIIRC), Amy Askew (Menzies/HLB), Paul Kazarian (Japonica Partners), Anders Heede (BDO), Mark Koziel (AICPA) and David Chitty (Crowe Horwath)

need some so-called “free money” to buy votes. They can sell the asset and spend on vote buying consumption and there is no recorded loss on the asset.

**Q.6 - Audience member:** What actually inspired your work? And what keeps you actually carrying on with the work? Is there an upside to this type of work? I’m just intrigued to understand really what is the background to the inspiration for your firm to continue doing the work on Greece.

**Paul B. Kazarian:** The simple answer is two-fold. One, we’re one of the largest private investors in Greek government bonds, which we were fortunate to have bought back in 2012 when the bonds were as low as 11 to 12 cents per 100 face value. And two, we have a fairly large foundation, the Charles & Agnes Kazarian Foundation, which gets much of our firm’s profit. And government accounting and financial reporting mission is a perfect fit for our foundation.

**Q.7 - Audience member:** I agree with Paul, a balance sheet is absolutely core. You have to start with the balance sheet and then you can move on. So in Greece, I understand. But why are governments not preparing and publishing balance sheets? And, what about the prospects for integrated financial statements?

**Paul B. Kazarian:** I don’t know how many governments there are in the world that have proper balance sheets. We found eight. Maybe there are 10, but we found eight that had proper balance sheets. If someone can find more, I’m happy to sit down with them and review the financial statements. As for integrated reporting, I’m in total support, but the government sector doesn’t even have basic balance sheets. They use complexity to try to avoid putting a balance sheet together. So in order to advance, get your first homework done. Otherwise, you’re going to get tied into a cycle and you’ll continue to be stuck there.

**Q.8 - Audience member:** How has the current Greek government responded to your calls to publish net debt figures that “reflect economic reality”? Why haven’t they followed your advice? Have international policymakers/analysts been more responsive?

**Paul B. Kazarian:** There has been considerable progress in educating the most enlightened current and former Greek government officials. The light bulb has yet to burn brightly with the more insular politically populist individuals. This will change, as such individuals have very short political longevity of their own making. The European and international rules are very clear that debt should be reported at today’s value and not the amount paid as far out as almost 50 years in the future. The European government debt measurement rules, known as ESA 2010, are clear that debt is a present value not future face value. Demosthenes taught Greeks the time value of money, so there is little excuse for those who claim that Greeks cannot understand that debt not due for 50 years and with very little interest payments is more like a gift than debt. Furthermore, even the Excessive Debt Procedure (EDP) has a Table 4 that requires the present value debt number, but currently the number is left blank.

**Q.9 - Audience member:** Given your view about Greece’s true debt

burden, how do you view the centrality of the debt issue both in the interminable negotiations between Greece and the troika that led to the referendum of 2015, and in the acrimonious debate between the IMF and the Eurozone in the context of the 3rd Programme?

**Paul B. Kazarian:** Debt is not the issue. The Greece debt burden is 50% of EU peers anyway you look at it if correctly calculated. In fact, Greece floating rate debt is only 17% of total debt, not 69%. Greece has been given €354 million in debt relief, 17 times the other EZ programme countries. There has been more than €23 billion of debt relief on the 3rd Programme, which has yet to be reported. Greece receives €6.6 billion annually in EU net funds, which is 251% of comparable size Ireland and Portugal. Greece debt service is 50% of EZ peers versus a gross financing needs of 123%.

**Q.10 - Audience member:** Under EU accounting standards, what is the Greece government debt number when correctly calculated?

**Paul B. Kazarian:** The EU accounting rules are ESA 2010. Debt is measured differently depending on the type of debt. In sum, almost all government debt throughout Europe is valued at market value; Greece government net debt as a percentage of GDP at year-end 2015 was 58% and gross debt was 88%. Specifically, government debt securities are measured at current “market value” (Section 7.67). Government “restructured debt is considered to be extinguished and replaced by a new debt instrument with the new terms and conditions” (Section 20.236) and such debt operations (Section 20.221) are valued at “market value” at the time of transaction as if taken for purely commercial consideration (Sections 5.20-21). Section 20.236 is a very important section and appears to have been neglected in the government reported calculation. Other debt such as non-restructured loans is at nominal value (Section 7.70). To calculate net debt, which is debt less financial assets, most assets are valued at market values. The market value rules do not have a material impact on other EZ government debt numbers, as they do not have restructured debt.

**Q.11 - Audience member:** Do the EU treaties allow or require the Greek government to report the present value (today’s value) of its debt?

**Paul B. Kazarian:** EU treaties have several rules for measuring debt, including ESA 2010 (described above), Excessive Deficit Procedures, and the EDP semi-annual form. EDP requires debt to be reported at future face value with the well-known 60% of GDP ratio maximum; however, this maximum has long ago been passed by many nations and has effectively become political window dressing. EDP semi-annual form Table 4, Item 4 requires disclosure of a government present value of debt when different from future face value. This is an excellent opportunity for Greece to comply with the rules and tell the world the present value number; however, the government continues to refuse to provide a number in the space provided. The government apparently is aware of the importance of the present value of debt as a non-paper submitted to the EU working group calls the often reported future face value of Greece government debt a “misunderstanding” and attempts to calculate a very rough estimate of present value. ■