Greek debt and the Babel-like confusion of tongues

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The discussion about the size and sustainability of the Greek debt is byzantine as it is, but it is compounded because it is spoken in different languages. IPSAS would provide a more realistic picture.

Two accounting languages - or three, actually - are used and politicians and economists who engage in the debate simply seem to choose the language they feel suits them best, or the one their supporters are supposed to hear. Is there no alternative?

The IMF talks about Nominal debt when it discusses debts. The Maastricht Treaty has been prepared in the Face value or principal argot - a type of Nominal Debt “dialect” (nominal debt is principal corrected for discount/premium upon issuance plus any interest in arrears).

Statisticians who draw up the National Accounts of countries, though, express ownership and debt – to the extent they are marketable - in market value. IPSAS (International Public Sector Accounting Standards), a mordern accounting grammar according to which debt - just like IFRS in the business community - is valued at market value wherever possible, likewise prescribe market value or fair value. The majority of EMU countries as yet does not apply this public sector accounting standard.

Exaggerated lament?

Jacob Soll, professor of history and accounting at the University of Southern California, wrote an Op-Ed article in the International New York Times on January 21, 2015, in which he laid bare why the lament about the unbearable Greek debts was actually excessive: the failure to apply IPSAS. Ever since the renegotiations on the terms and conditions of the debt in 2012, when the installments were stretched - some even up to 2054 - and the interest dropped down to less than 2 per cent, the present value of the Greek debt has become much lower. Still, this is not revealed because neither Greece nor the main creditors, with Germany leading, apply the IPSAS rules to determine the current value of the debt.

And, as Soll goes on to state, the Greek accounts are shaky - a fact augmented by a lack of qualified auditors - so the recently resigned government of Antonis Samaras was not in the position to provide reasonable arguments for an improvement of its country’s fiscal position and other economic indicators. Had the government been able to do so, the country would have profited from better credit ratings from credit rating agencies such as Moody's. It would thus have reduced interest payments on non-renegotiated debts.

Actual debt restructuring only concealed by ongoing high nominal value.

Restructuring concealed

Klaus Regling, CEO of the European emergency fund EFSF, which provided Greece with a large package of new low-interest loans, used slightly different words in an interview with Het Financieele Dagblad recently: “If the reforms continue there will be no debt problem in Greece in the years to come.”

As the FD shows in the article, the present value of the total Greek debt of approximately 380 billion euro has dropped by 40 per cent thanks to the more lenient conditions applied by the EFSF. Effectively, it concludes, a debt restructuring has already been implemented and only the ongoing high nominal value conceals it.

Because Germany does not apply IPSAS either, Soll states, the Merkel government can continue to conceal to the general public – which is notoriously skeptical about the idea of their money constantly being used to save Greece – a huge de facto write-down on the receivable whose nominal value is 57 billion euro.

The present value of the Greek debt has fallen considerably. But it is not made visible.

More realistic

If Soll and Regling are right, what refrains the European governments from introducing IPSAS - or EPSAS, an alternative more in line with certain wishes of EU Member States?

Until recently, Frans van Schaik (University of Amsterdam, Deloitte) was a member of the IPSAS Board, the organization advocating the introduction of this IFRS variation for governments: “If the interest rate on loans is below-market, as is the case with the renegotiated loans to Greece, the nominal value indeed does not reflect the economic substance. Any IPSAS financial statements would value such *concessionary loans* at a lower amount than the nominal value. This provides a more realistic picture of the government’s financial position and with the Greek loans this makes a big difference.”

Still, as he likewise reminds, the implementation of IPSAS in itself would not affect the requirements set for the amount of Greek national debt. This would require the Maastricht Treaty to be modernised: “According to one of the EMU standards - laid down in the Maastricht Treaty of 1992 - the national debt may not exceed 60 per cent of the gross domestic product. This standard relates to the nominal debt, the face value of loans, but otherwise disregards other debts such as civil servants’ pension liabilities.”

Grown historically

The Flemish writer Willem Elsschot already wrote: “Laws and practical objections are in the way of dream and action.” The observations by Léonard Haakman, senior researcher at Statistics Netherlands and a member of the European Task Force EPSAS Standards also show this to be the case. He thus basically propagates bidding farewell to the Dutch national government’s practice of the so-called commitments cash accounting, which does not distinguish between costs and investments, and thus does not value investments and their financing at market value.

A historically grown practice, Haakman thinks, is notoriously hard to change: “As many countries still mainly apply cash accounting it is difficult to meet IPSAS and IMF standards. And if you want to make comparisons at a European level you would rather have all countries being able to properly measure debt even if its definition does not quite cover the connotation.”

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Slightly bizarre

Haakman thinks focusing on a single figure would be wrong. Example: “In addition to gross debt the term net debt is relevant, too, because a high debt is less problematic if a gross debt can be set off with sufficient financial assets that may be released.”

He further points out a distorting effect of valuation at market value: “In terms of debt an almost bankrupt country would on paper be relatively better off than a country where things are going well.” And indeed slightly bizarre: “Parallel to a value increase of listed government bonds, the Dutch debt would thus increase strongly.”