

## **Original and Copies – A case for retaining the SNA 1993 treatment**

**By**

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### **Introduction**

1. The Canberra II Group on the treatment of assets in the SNA has submitted a proposal on a new treatment of originals and copies to the Advisory Expert Group. The essence of this proposal is that the creation of a copy of an original should be recognised in the system as capital formation. Of 27 members of the group at the Washington meeting, 25 voted for this proposal. This note points out unresolved issues that this new proposal brings, and suggests that the current 1993 SNA treatment is adequate and appropriate.

### **Canberra Group II proposal**

2. The creation of a copy of an original intangible asset such as a database is capital formation, and purchase of a copy should be recorded in the capital account as acquisition of a produced non-financial asset. The argument is that using an original to produce a copy is essentially the same as using a machine (the capital asset) to produce a new product which is also a capital good. So a truck-making plant (capital) produces a new truck (capital asset) for business. So an original database is used to produce a copy.

3. The proposal also suggests that where the original asset is intangible, then the licence to use a copy of the original, or to access the original, should also be recorded as an asset, and payments for a licence should be seen as the purchase of an asset.

### **Issues**

4. This is a major change to the current SNA – the treatment of artistic originals and copies is set out in paragraph 6.146 and this is reproduced below.

*6.146 The owner [of an asset] may also licence other producers to make use of the original in production. The latter may produce and sell copies, or use copies in other ways; for example, for film or music performances. In these cases, the owner is treated as providing services to the licencees that are recorded as part of their intermediate consumption. The payments made by the licencees may be described in various ways, such as fees, commissions or royalties, but however they are described they are treated as payments for services rendered by the owner. These services are valued by the fees, commissions, royalties etc. received from the licencees.*

5. Selectively choosing text from this SNA 1993 extract, we get

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*these cases, the owner is providing services to the licencees that are recorded as part of their intermediate consumption. The payments made by the licencees may be described as fees, commissions or royalties; treated as payments for services rendered by the owner.*

## **Question I**

6. What is wrong with the current SNA treatment of artistic originals? Where is the flaw in the recommended treatment? The current guidelines are clear and simple in concept to apply. They reflect the fact that payments for access to an original such as a film should be seen as fees, as service payments, and so part of the intermediate consumption of the purchaser. Owning a copy of a film does not represent the acquisition of the underlying asset which is protected by copyright conditions.

## **Question II**

7. It has been agreed by the Canberra Group that databases created for business purposes should be recognised as intellectual property - a knowledge asset. Does the proposed treatment of originals and copies work for databases?

8. Consider an insurance company with a database of prospective clients in East London. The database holds information such as name, address, telephone number, household income, insurance history, financial credit rating, and so on. The data base is used to help salespersons to target prospective clients. Let us call this company A. Now consider company B which shares the same building as company A. It would also like to use the database. It offers company A regular payments for continued access to the database, allowing the staff of company B to use the computer terminals of company A with a password provided to give access to the database.

9. The treatment of the payments depends on the conditions of use. If we assume that the access is very restricted – not allowed to alter the database in any way, not allowed to pass on the information gained to third party, not allowed to tell anyone else the password apart from a limited number of sales staff, not allowed to change the software, etc., then ownership is taken to reside with the legal owner and the payments for access are accepted as being traditional service payments or rentals.

10. Notice that in this case there is no copy of the database made. We simply observe a licence arrangement whereby company B pays money to gain regular and recurring access to the original.

11. Now consider the situation where company B moves across the street, and it is no longer convenient for staff to walk along the corridor to access the database through the shared computer terminals. The companies agree that a copy of the database should be created and sent across the road to run on company B's new computer system. So now the staff of company B can access the copy on their own computer, rather than crossing the road to access the original. Company A undertakes to keep the copy of the database up to date.

12. Is the creation of a copy capital formation? What is different about how company B uses the knowledge of the database to do its business? In creating a copy, have we doubled the knowledge? Or simply doubled the access?

13. What if we allowed company B to access the original database via the internet, rather than access the copy held on their own computer? Is there any essential

difference in the two arrangements, and in the way company B staff use the information held on the database?

14. There seems no essential difference in the two arrangements – using the copy is a different way of accessing the information held on the original. It seems wrong if we say that destroying the copy and changing the access to using the internet results in a reduction in the non-financial capital assets in the economy. This problem is avoided if we characterise the payments for use of the original as rentals, no matter the method of access. The copies are then seen as access devices to an underlying asset, and not capital assets in their own right.

15. The fallacy of treating a copy as a new capital asset is revealed if we compare the situation of company A considering whether to create a new database for West London, to complement its database for East London. It will decide whether this is worthwhile by estimating the value to its own business and any likely payments for other companies using the new original. So the stream of future income from the expected use of the original is factored into how much it is worth to create this new asset. This calculation fully accounts for all the expected rentals of other companies who will want to use the asset. Is this creation of new knowledge for West London equivalent to creating a copy of the existing East London database? Creation of new information for West London seems like capital formation of a new knowledge asset, quite different in nature from creating a further copy of existing information with regard to East London.

16. The creation of a copy of the existing East London database is a way of doubling the access, not doubling the knowledge asset. Creating the new West London database is productive activity resulting in a new capital asset.

17. The current Canberra Group proposal is that the acts of new knowledge creation, and copy creation, result in equivalent capital formation. This just seems wrong.

### **Conclusions**

18. The current treatment of artistic original and copies in the SNA 1993 can be extended to all originals and copies, with no fundamental changes needed.

19. The creation of licences to use originals is not the creation of a non-financial asset, but rather a type of contract between supplier and user. It can attain a financial value if market conditions change, but has no value in its own right as a new non-financial produced asset.

### **Recommendation**

20. Submit the proposal on Originals and Copies to the proposed economic user forum to confirm that users are content with the proposal.