

**OVERVIEW OF
AEG DECISIONS AND COUNTRY COMMENTS ON DECISIONS
OF THE FIRST AEG MEETING AND OTHER CONSULTATIONS
ON ISSUES IDENTIFIED FOR UPDATING THE 1993 SNA**

(For information)

*Prepared for the December 2004
Meeting of the Advisory Expert Group on National Accounts*

UNSD

Background

The United Nations Statistical Commission at its thirty fifth session desired that the global statistical community should be involved in the updating process of the 1993 SNA. The following issues relating to the updating of the 1993 SNA recommended by the Advisory Expert Group (AEG) were, therefore referred to the National Statistical Offices of the member states for their comments, namely:

Item No	Issues
3	Employee Stock Options
5	Measurement of production of non-life insurance services
6 (a)	Measurement of production of the (non-insurance) financial services
6 (b)	Measurement of the output of Central Banks
7	Taxes on holding gains
14	Cost of Ownership transfer of non-financial assets
19	Treatment of Military assets as capital formation
26	Cultivated Assets

(The item nos. refers to the one from the list of issues currently under review for updating 1993 SNA available at <http://unstats.un.org/unsd/sna1993/issues.asp>)

A Majority of the countries¹ have supported the recommendations of the AEG. A brief summary of the issues and the recommendations of the AEG thereon have been presented below:

Item 3 - Employee Stock Options (ESOs)

¹ Forty one countries (Australia, Austria, Belgium, Botswana, Canada, Chile, Columbia, Denmark, Finland, France, Germany, Guyana, Hungary, India, Japan, Jordan, Kazakhstan, Korea, Latvia, Lesotho, Macao, Malaysia, Madagascar, Moldova, Netherlands, New Zealand, Nicaragua, Norway, Poland, Portugal, Russia, Serbia, Slovak Republic, South Africa, Sweden, Switzerland, Syria, Tajikistan, Tanzania, U.K. and USA) have commented on the recommendations of the AEG.

Employee stock options are a common tool used by companies to motivate their employees. Under an standard ESO model a company at the ‘grant date’ grants an employee the right to purchase a set number of shares at a set (‘strike’) price at a particular time in future. The employee has to wait for a certain period of time (known as the ‘vesting period’) before options are available for exercise. This time expires at the ‘vesting date’ and there are generally conditions attached for the ESOs to vest. The employee exercises the option at their discretion on or after the vesting date by purchasing shares at the strike price. These shares can be held or re-sold on the market. The 1993 SNA does not provide guideline for treatment of ESOs which involves issues like: (a) are the ESOs part of wages and salaries? If so, they should be considered as expense to the business (b) the timing of recording of the ESOs i.e. whether on grant date, vesting date, exercise date or spreading its values between two of these points in time, and (c) how should ESOs be valued?

AEG Recommendations: After extensive consultations and detailed discussions the Expert Advisory Group approved to (i) include all ESOs in compensation of employees (wages and salaries in kind), irrespective of whether these will be settled in new or re-purchased stocks, (ii) record the value of the ESOs in the accounts spread between the grant and vesting dates, if possible, (iii) value ESOs at market price, or by using a suitable option pricing model, and (iv) record the ESOs in the financial accounts not as financial derivatives but as an instrument category entitled “financial derivatives and employee stock options,” with the subcategories of (a) financial derivatives and (b) employee stock options.

Item 5: Measurement of production of non-life insurance services

The output of non-life insurance services, estimated at current prices using the 1993 SNA methodology, as balance of premiums to claims (on an accrual basis) could be volatile especially in the event of catastrophic losses. It may be noted that the production of insurance services does not occur when the risk occurs. The concept of insurance service is the service of covering for the risk. As such its measurement should not be affected by the volatilities of the occurrence of the risk. There is a need therefore, to review the present methodology and propose alternative measures of production of insurance services in order to reflect a volume and price movement that corresponds better to this concept.

AEG Recommendations: The issue was deliberated upon by an OECD Taskforce. The AEG after detailed discussions of the recommendations of the Taskforce decided as under: (a) to continue using the formula based on the difference between the premium (plus premium supplements) and claims, but to use adjusted claims and optionally, adjusted premium supplements in this formula in order to correct volatility of observed flows; (b) the adjustment of premium supplements may be optional. The adjusted premium supplement could be estimated either of the three approaches, namely, expectation approach (which uses statistical smoothing of the past data, the accounting approach and the sum of costs + normal profit approach; (c) extension of the SNA definition of provisions for unearned premium, provisions for bonuses and rebates, provisions for claims outstanding the provisions for incurred but not reported incidents

and equalization provisions. These extended technical provisions will be considered assets of policyholders or beneficiaries depending whether they are classified as provisions for unearned premiums or provisions for outstanding claims. All income from these provisions will be considered as premium supplements; (d) decoupling net insurance premiums (D71) and non-life insurance claims incurred (D72) in the distribution accounts. In exceptional cases, such as, catastrophes, part of the difference between D72 and D71 may be treated as capital transfer; (e) changes in the terminology for “technical reserves” to be called “technical provisions” and for “claims due” to be called “claims incurred”: (f) new treatment of reinsurance where all reinsurance flows are treated gross and the same formulae (using adjusted variables) are used as for direct insurance; (g) commissions paid by the reinsurer to the direct insurer and the rebates paid by the direct insurer to the policyholders should be classified as a negative component of the premiums earned. The profit sharing paid by the reinsurer to the direct insurer and the bonuses paid by the direct insurer to the policyholders should be classified as a form of other income transfers.

Item 5 (additional consultation): Measurement of production of non-life insurance services

Members of the AEG were consulted through a questionnaire to decide the following: (i) Should the income from own funds be included in the formula for the calculation of non life insurance output? (ii) If yes, which option to be adopted? (iii) Should commissions and rebates be classified as negative premiums and profit sharing and bonuses as other income transfers? (iv) Should the SNA allow an option permitting the treatment of some catastrophic claims as capital transfers rather than current transfers?

AEG Recommendations: (i) The proposal regarding inclusion of income from own funds in the calculation of the output measure of non life insurance did not find favour with the majority of the AEG members. (ii) In view of (i) above, the question does not arise. (iii) Majority of the AEG members were in favour of classifying commissions and rebates as negative premiums and profit sharing and bonuses as other income transfers, and (iv) Despite its possible impact on the discrepancies of BOPs’ current balances at the international level, the AEG decided by a very large majority the option to treat transfers resulting from exceptional claims as a capital transfer rather than, as in normal cases, a current transfer.

Item 6(a): Measurement of production of the (non-insurance) financial services

This issue is devoted to the measurement of the output of financial intermediation services and portfolio management in the national accounts. The business of financial corporations has undergone a structural transformation towards a rising importance of the portfolio management of financial assets. This generates holding gains and losses, that, typically, national accounts exclude from the production boundary and therefore income. The review will consider whether and how the production boundary can be adapted to this rising activity, and how this could influence income.

AEG Recommendation: The issues involved in the measurement of production of the (non-insurance) financial services were deliberated upon by an OECD Taskforce. The AEG reviewed the provisional recommendations of the Task Force. It was noted that the recommendations should be regarded as work-in-progress. Some of the recommendations of the Task Force like, (a) a new definition of financial corporations, (b) the principle of non-exclusion of own funds in the measurement of output, (c) a reference rate approach for the measurement of financial intermediation services indirectly measured (FISIM), were discussed by the AEG. The recommendations of the Task Force were considered as work-in-progress. The Task Force was requested to continue its work and produce a comprehensive presentation of all the inter-related issues.

Item 6(b): Measurement of the output of Central Banks

The measurement of the outputs of central banks at cost as an alternative to the current measurement has been reviewed. Allocation of the output of central banks has also been discussed.

AEG Recommendation: The AEG reviewed the recommendation made by the ISWGNA in 1995 on the measurement of the output of central banks and agreed that, because of the unique functions that may be performed by central banks, the value of their output obtained by the method recommended by the 1993 SNA (the difference between property income receivable less interest payable) may sometimes be exceptionally large or small or even negative. In such cases the output of central banks or at least part of it could be measured at cost. Further work is needed to clarify these cases. This does not imply reclassifying the central bank to the government sector.

Item 7: Taxes on holding gains

Taxes on capital gains are treated as taxes on income and deducted from income while the tax base (the realized holding gains) is not included in the SNA definition of income. Is this a contradiction that should require alternative treatments or should the 1993 SNA treatment remain the same?

AEG Recommendation: The AEG agreed to continue treating taxes on holding gains as current taxes on income and wealth (D51). As far as possible, taxes on holding gains should be shown as a special sub-category within D51. The AEG considered the possibility of developing alternative concepts of household income but decided however, that this is potentially a big undertaking and is not a priority for the present SNA review.

Item 14: Cost of Ownership transfer of non-financial assets

The principal focus of the review of the treatment of the cost of transfer (COT) has been whether the COT of fixed assets should be treated as current expenditure or capitalized. The scope of the review has since been broadened to include issues such as, (i) if COT is to be capitalized what should be the service life, (ii) how should we treat COT when the underlying asset is sold by the original owner, and by extension, (iii) how should we treat the termination costs of the underlying asset?

AEG Recommendation: It was recommended to preserve the link, in the 1993 SNA, between the value of an asset of an enterprise and the value of the services to be rendered by the asset under reference over the length of time it is held. This implies maintaining COT as capital formation. However, the AEG recommended that rather than depreciating the COT over the lifetime of the underlying asset as recommended by the 1993 SNA, the cost of ownership transfer should be written off over the period during which the acquirer expects to hold the asset. If the expectation is met, this means that the COT will be entirely depreciated when the asset is resold, thus avoiding the overestimation of the net operating surplus.

Item 19: Treatment of Military assets as capital formation

The 1993 SNA divides military assets into those that can be used for civilian purposes and those that can only be used for military purposes. The former are treated as gross capital formation, the latter as intermediate consumption. This treatment does not provide an appropriate accounting system for existing weapons as weapons that have already been expensed can actually be taken out of stock for use or for exports and would have to be balanced by a negative component in government final consumption. Should the line between gross capital formation and intermediate consumption be drawn differently?

AEG Recommendation: Military weapon systems were seen to be used continuously in the process of production of defense services, even if their peacetime use is simply to provide deterrence. As such these meet the same criteria as for other fixed assets, namely, produced assets that are themselves used repeatedly, or continuously, in processes of production for more than one year. In view of this the AEG recommended to include expenditure on military weapon systems as gross capital formation (GCF). This should, however, be presented separately from other types of GCF.

Item 26: Cultivated Assets

During the process of developing the System of Economic and Environmental Accounts, it was noted that the definition of cultivated assets in the 1993 SNA is rather ambiguous. It was suggested to redefine the cultivated assets as follows: “cultivated assets cover livestock for breeding, dairy, draught, etc. and vineyards, orchards and other trees yielding repeat products *whose natural growth and regeneration* is under the direct control, responsibility and management of institutional units”. The words in bold italics replace the words “that are” in the SNA.

AEG Recommendation: The AEG recommended the proposed rewording of the definition of the cultivated assets.

Item 45: Additional issues submitted to the AEG

In consonance with the decision of the Advisory Expert Group (AEG) meeting held during 18-20 February 2004, the following additional issues were received by the ISWGNA Secretariat from the AEG members for possible inclusion in the list of candidate for 1993 SNA updating issues, namely:

- i) Separate chapter for regional accounts

- ii) Additional chapter for multi-country accounts
- iii) Additional chapter for quarterly accounts
- iv) A chapter devoted to financial accounts
- v) Clarification on how to deal with new financial products
- vi) Improve the SNA as a basis for comprehensive productivity analysis
- vii) Integrate policy-oriented variables
- viii) Review SNA terminology for user-friendliness
- ix) Definition of basic prices
- x) Volumes and prices in relation to taxes on products
- xi) Clarification of components of compensation of employees
- xii) Review of classifications
- xiii) Review of purpose and uses of the SNA
- xiv) Review SNA codes

AEG Recommendation: The AEG members were asked to vote and express their views on those additional issues as summarized by the ISWGNA. All additional issues proposed to be included in the list of updating issues were rejected, except for the clarifications that need to be taken into account by the editor when drafting the 1993 Rev. 1. Some of these issues have already been taken up by specialized taskforces and some may be better handled in handbooks.

The result of country consultations have been summarized in the following table:

Item No.*	Issues	AEG Recommendations	Results of country consultation			
			No. of countries			
			In Agreement with AEG	In Disagreement with AEG	No comments	Further research/discussions
3	Employee Stock Options (ESOs)	<ul style="list-style-type: none"> - ESOs are part of the compensation of employees. - The value of ESOs is to be spread between the grant and the vesting dates, if possible. - ESOs should be valued at market prices, or by using a suitable option pricing model. - ESOs should be recorded in the financial accounts as financial derivatives as a separate category. 	34	-	10	2
5	Measurement of production of non-life insurance services	<ul style="list-style-type: none"> - The accounting approach as one solution to estimate output. - The inclusion of technical and other special provisions. - The new treatment of reinsurance. - The treatment of payments in the case of major catastrophes as capital transfers. - The change in terminology. 	32	-	13	1
6(a)	Measurement of	<ul style="list-style-type: none"> - New definition of financial corporations. 	18	1	18	9

	production of the (non-insurance) financial services	<ul style="list-style-type: none"> - Reference rate approach for measurement of FISIM - OECD Taskforce to continue its work 				
6(b)	Measurement of the output of Central Banks	– Measurement of the output of central banks on cost basis.	38	-	5	3
7	Taxes on holding gains	<ul style="list-style-type: none"> - Continue to treat taxes on holding gains as current taxes on income and wealth. - If possible, show taxes on holding gains as a special sub-category. 	34	-	11	1
14	Cost of Ownership transfer of non-financial assets	<ul style="list-style-type: none"> - Continue to treat COT of non-financial assets as fixed capital formation. - COT incurred on the acquisition of an asset should be written off over the period the owner expects to hold the asset (instead of the entire life of the asset). 	25	-	15	6
19	Treatment of Military assets as capital formation	<ul style="list-style-type: none"> - Military weapon systems are to be treated as gross fixed capital formation (instead of intermediate consumption). - Defence GFCF should be presented separately from other types of GFCF. 	18	5	13	10
26	Cultivated assets	More precise definition: Cultivated assets cover , whose natural growth and regeneration is under the direct control, responsibility and management of institutional units.	30	-	16	-

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Summary of the country comments:

The decisions of the AEG were forwarded to the National Statistical Offices (NSO) and the National Banks (NB) of the member countries for their comments which have been summarized in the following table.

Country/Expert		#3	#5	#6(a)	#6(b)	#7	#14	#19	#26
Australia	NSO	A	A (Profit sharing and bonus are adjustments to premiums)	FR	A	A	A	A	A
	NB	A	A	NC	A	A	A	A	A
Austria	NSO	A	NC	NC	A	A	A	A	A
	NB								
Belgium	NSO								
	NB	NC	A	FR	A	A	NC	NC	NC
Botswana	NSO	FR	FR	NC	FR	A	NC	FR	NC
	NB								
Canada	NSO	A	A	A	A	A	A	A	A
	NB								
Chile	NSO								
	NB	A	A	NC	A	A	FR	A	A
Colombia	NSO								
	NB	A	A	A	A	A	A	NC	NC
Denmark	NSO	A	A	FR	A	A	A	FR	A
	NB								
Finland	NSO	A	NC	NC	NC	NC	NC	NC	A
	NB								
France	NSO								
	NB	A	NC	NC	NC	A	NC	FR	NC
Germany	NSO	A (Need not be shown separately)	A (Not in favour of recording expected premium supplement instead of actual premium supplement)	D	A	A	A	D	A
	NB								
Guyana	NSO								
	NB	A	NC	FR	A	FR	A	FR	A
Hungary	NSO	NC	NC	NC	A	NC	NC	NC	NC
	NB								
India	NSO	A	A	A	A	A	A	FR	A
	NB								
Japan	NSO								
	NB	FR	NC	NC	D	NC	NC	NC	NC
Jordan	NSO	A	A	A	A	A	A	FR	A
	NB								
Kazakhstan	NSO	NC	NC	A	NC	NC	NC	NC	NC
	NB								
Korea	NSO								
	NB	A	A	A	A	A	FR	FR	A
Latvia	NSO								
	NB	A	A	A	A	A	A	A	A
Lesotho	NSO								
	NB	A	NC	A	FR	A	A	NC	A
Macao	NSO	A	A	A	A	A	A	A	A
	NB								

Malaysia	NSO	A	A	NC	A	NC	NC	D	NC
	NB								
Madagascar	NSO								
	NB	A	A	A	A	A	A	A	A
Moldova	NSO								
	NB	A	A	NC	A	A	A	A	A
Netherlands	NSO	A	A	FR	FR	A	FR	A	A
	NB	A	NC	NC	A	A	NC	NC	NC
New Zealand	NSO	A	A	NC	A	A	A	A	A
	NB								
Nicaragua	NSO	NC	A	NC	A	NC	FR	A	NC
	NB								
Norway	NSO	A	A	A	A	A	A	A	A
	NB								
Poland	NSO								
	NB	NC	NC	NC	A	A	FR	D	A
Portugal	NSO								
	NB	A	NC	NC	NC	A	NC	A	NC
Russia	NSO								
	NB	NC	A	A	A	NC	NC	NC	NC
Serbia	NSO	NC	NC	NC	A	NC	NC	NC	NC
	NB								
Slovak Rep.	NSO	A	A	FR	A	A	A	A	A
	NB								
South Africa	NSO	A	A	NC	A	A	A	D	A
	NB	A	A	FR	A	A	A	D	A
Sweden	NSO								
	NB	NC	A	NC	NC	NC	NC	NC	NC
Switzerland	NSO								
	NB	NC	A	A	A	NC	NC	NC	NC
Syria	NSO								
	NB	NC	NC	A	A	NC	NC	NC	NC
Tajikistan	NSO								
	NB	A	A	A	A	A	A	A	A
Tanzania	NSO	A	A	A	A	A	A	FR	A
	NB	A	A	A	A	A	A	FR	A
U.K.	NSO	A	A	NC	A	A	A	A	A
	NB								
United States	NSO	A	A	A	A	A	A	A	A
	NB								
European Central Bank		A	A	FR	A	A	FR	FR	A
Total	NSO	A=18 D=0 NC=4 FR= 1	A=16 D=0 NC=5 FR=1	A=8 D=1 NC=10 FR=4	A=19 D=0 NC=2 FR=2	A=17 D=0 NC=6 FR=0	A=15 D=0 NC=6 FR=2	A=10 D=3 NC=4 FR=5	A=17 D=0 NC=6 FR=0
	NB	A=16 D=0 NC=6 FR= 1	A=16 D=0 NC=8 FR=0	A=10 D=0 NC=9 FR=4	A=19 D=0 NC=3 FR=1	A=17 D=0 NC=5 FR=1	A=10 D=0 NC=9 FR=4	A=8 D=2 NC=9 FR=5	A=13 D=0 NC=10 FR=0

A: Agrees with the proposal D: Disagrees with the proposal NC: No Comments FR: Further
Research/discussion required