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Item 3 (f) of the provisional agenda
Items for discussion and decision: National accounts

Background document
Available in English only

The Full Set of Consolidated Recommendations

The Recommendations Made by the Advisory Expert Group for the
Update of the System of National Accounts, 1993

Prepared by the Intersecretariat Working Group on National Accounts

Update of the 1993 SNA

Full set of consolidated recommendations

A list of issues to be considered during the update was prepared by the Intersecretariat Working Group on National Accounts (ISWGNA) and endorsed by the Statistical Commission in 2003. The issues included some that had been on the research agenda included in the 1993 SNA and a number that had arisen since as more detail on new aspects was worked out or in response to emerging phenomena. In all, five main groups of issues can be identified. These are described below.

The second Canberra Group on Non-financial Assets (the Canberra II Group) took forward consideration of “intangible assets”, many of which are associated with the establishment of property rights over knowledge in one form or other. One key issue was the proposed inclusion of research and development expenditure as capital formation. Another was the proposed introduction into the SNA accounts of the link between the stock of non-financial assets used in production and the operating surplus generated. This link stems from the theory of capital services and is fundamental to studies of productivity.

In response to growing analytical interest in the role of the public sector (in contrast to the narrower concept of general government), a Task Force on the Harmonisation of Public Sector Accounts (TFHPSA) was set up. This task force was also charged with liaison with the International Public Sector Accounting Standard Board (IPSASB) to try to develop approaches that users of the GFSM and public sector standards would be comfortable with as well as national accountants. The work focussed on the delineation of the government and public sector from the rest of the economy, the handling of transactions between government and public corporations and with securitisation vehicles to ensure objective recording of items that could significantly affect government debt.

A number of issues concerned financial services. For the most part each issue was dealt with by a special group, often an EDG. The topics included a review of non-life insurance to clarify how exceptional events should be treated; the treatment of employee stock options; the treatment of impaired (non-performing) loans; and a detailed examination of the services provided by financial institutions to ensure these were fully covered in the SNA. The most far-ranging issue under this heading concerns the recording of pension entitlements even when the pension schemes may not be fully funded.

Over recent years, the IMF Committee on Balance of Payments Statistics (BOPCOM) has become increasingly focussed on the international investment position and the treatment of different financial assets covered. Questions arose in particular about instruments linked to foreign currency in one way or another and the aspects of retained and reinvested earnings of direct investment enterprises. Another set of issues raised by BOPCOM concerned the more traditional area of balance of payments accounting. These issues included the treatment of remittances and the recording of goods sent abroad for processing, two issues of increasing attention in the context of globalisation.

Lastly there were some issues that were self contained but no less important for that: clarification of ancillary units and holding companies, and measurement of informal and illegal activities.

The issues were numbered from 1 to 44 as they were added to the list but there is no particular grouping within the numbering system. In the lists below, the issues are first presented in numeric order and then grouped by topic. A presentation of individual issues follows, in numeric order. Each presentation begins with a statement of the issue and then contains the summary recommendations made by the Advisory Expert Group (AEG), either at a formal meeting or in response to an electronic consultation. On five issues, listed below, world-wide consultation has revealed a lack of unanimity with the AEG recommendations.

- 9 Research and development;
- 15 Cost of capital services;
- 16 Government and non-market producers, cost of capital services of own assets;
- 19 Military expenditures;
- 40 Goods for processing.

This document describes only the recommendations made by the AEG as of November 2006. The considerations of the ISWGNA and recommendation to the Statistical Commission are contained in the official report by the ISWGNA to the Statistical Commission (Paper E/CN.3/2007/7).

The papers relevant to each issue are listed following the AEG recommendation. Papers with code numbers of the form SNA/Mx.0y/z were considered at an AEG meeting. Papers presented to the first meeting of the AEG held in Washington in February 2004 contain the code M1.04; those for the second meeting held in New York in December in 2004 contain M2.04; the meetings held in Bangkok in July 2005 and in Frankfurt in February 2006 contain codes M1.05 and M1.06 respectively. The final digit(s) are the number of the paper relative to the meeting in question and are followed by the title of the paper. The follow-up papers all contain codes of the form SNA/F1.06/z. All these papers appear on the part of the UN web site dedicated to SNA update and in particular to the meetings of the AEG at <http://unstats.un.org/unsd/nationalaccount/aeg.htm> .

A postscript concerning clarification items follows the last issue. A general call asked for instances where greater explanation or clarity would be beneficial to the existing text. Most responses were very focussed and involve no change in the SNA. However, in five areas the response involves some degree of change, mostly to move to a greater degree of harmonisation with other systems of statistics. The five items cover the most aggregate level of ISIC to be used in the SNA; clarification with the ILO on labour inputs; clarifications with alternative financial account systems on the sub-sectors to be shown for the financial sector; more flexibility on the valuation of equity; and incorporation of some of the proposals put forward in the Atkinson report on the measurement of non-market output. Each of these is described in the postscript.

A note on terminology

The SNA gives guidance, guidance it is hoped will be followed in order to facilitate international comparison. However, the SNA does not have the power of law and so it is not possible to speak of some items as being “mandatory” in contrast to others that are “optional”. Where there is any question of doubt, the descriptor “standard” is used to indicate items, procedures and tables that the SNA recommends that all countries follow. When the descriptor is “supplementary”, the SNA recognises that it is unlikely that all countries will supply this degree of detail but suggests that those countries that can provide extra detail, and choose to do so, should follow the indications given to ensure comparability even on the basis of a restricted number of countries.

List of acronyms and abbreviations

AEG	Advisory Expert Group on National Accounts
BOP	Balance of Payments
BOPCOM	International Monetary Fund Committee on Balance of Payments Statistics
BOOT	Buy-Own-Operate-Transfer
BPM	Balance of Payments Manual
Canberra II Group	Canberra II Group on Non-Financial Assets
CPC	Central Product Classification
CPI	Consumer Price Index
DBMS	Database Management System
ECB	European Central Bank
EDG	Electronic Discussion Group
e-discussion	electronic (web-based) discussion
ESA95	European System of Accounts 1995
EU	European Union
FISIM	Financial Intermediation Services Indirectly Measured
GDP	Gross Domestic Product
GFSM	Government Finance Statistics Manual
IASB	International Accounting Standards Board
ICLS	International Conference of Labour Statisticians
ICT	Information Communication Technology
ILO	International Labour Organization
IMF	International Monetary Fund
IPSASB	International Public Sector Accounting Standards Board
ISIC	International Standard Industrial Classification of All Economic Activities
ISWGNA	Intersecretariat Working Group on National Accounts
NPLs	Non-Performing Loans
NPISHs	Non-Profit Institutions Serving Households
OECD	Organisation for Economic Cooperation and Development
PFI	Private Finance Initiatives
PPP	Public-Private Partnerships
R&D	Research and Development
Repo	repurchase agreement
SDRs	Special Drawing Rights
SEEA	System of integrated Environmental and Economic Accounting
SNA	System of National Accounts
SPE	Special Purpose Entities
SPV	Special Purpose Vehicles
TFHPSA	Task Force on the Harmonization of Public Sector Accounts
UNECE	United Nations Economic Commission for Europe

List of issues considered in the update of the 1993 SNA

Issues listed in their numeric order (and in order of presentation in this document)

- 1 Repurchase agreements
- 2 Employers' pension schemes
- 3 Employee stock options
- 4a Non-performing loans
- 4b Valuation of loans and deposits; Write-off and interest accrual on impaired loans
- 38c Application of the accrual principle to debt in arrears
- 5 Non-life insurance
- 6a Financial services
- 6b Allocation of the output of central banks
- 7 Taxes on holding gains
- 8 Interest under high inflation
- 9 Research and development (R&D)
- 10 Patented entities
- 11 Originals and copies
- 12 Databases
- 13 Other intangible fixed assets
- 14 Costs of ownership transfer
- 15 Cost of capital services
- 16 Government and non-market producers: cost of capital of own assets
- 17 Mineral exploration
- 18 Right to use/exploit non-produced resources between residents and non-residents
- 19 Military expenditures
- 20 Land improvements
- 21 Contracts, leases and licences
- 22 Goodwill and other non-produced assets
- 23 Obsolescence and consumption of fixed capital
- 24 Public-private partnerships (PPPs) (including buy-own-operate-transfer (BOOT) schemes)
- 25a Ancillary units
- 25b Holding companies, special purpose entities, trusts
- 25c Treatment of multi-territory enterprises
- 25d Non-resident unincorporated units
- 25e Non-resident SPEs controlled by government
- 26 Cultivated assets.
- 27 Classification and terminology of assets
- 28 Amortization of non-produced assets
- 29 Assets boundary for non-produced intangible assets
- 30 Definition of economic assets
- 31 Water as an asset

- 32 Informal sector
- 33 Illegal activities
- 34 Government transactions with public corporations: earnings from equity investment and capital injections
- 35 Tax revenues, uncollectible taxes and tax credits
- 36 Public/private/government sectors delineation
- 37 Granting and activation of loan guarantees
- 38a Change of economic ownership (as term)
- 38b Assets, liabilities and personal effects of individuals changing residence (“migrants’ transfers”)
- 38c Application of accrual principles to debt in arrears
- 39a Meaning of national economy
- 39b Predominant centre of economic interest (as term)
- 39c Residence of entities with little or no physical presence
- 39d Non-permanent workers
- 40 Goods for Processing
- 41 Merchanting
- 42 Retained earnings of mutual funds, insurance companies and pension funds
- 43a Treatment of index-linked debt instruments
- 43b Debt indexed to a foreign currency
- 43c Interest at concessional rates
- 43d Fees payable on securities lending and gold loans
- 44 Financial assets classifications

Issues grouped by topic

Issues concerning non-financial assets (considered by the Canberra II Group)

- 9 Research and development (R&D)
- 10 Patented entities
- 11 Originals and copies
- 12 Databases
- 13 Other intangible fixed assets
- 14 Costs of ownership transfer
- 15 Cost of capital services
- 16 Government and non-market producers: cost of capital of own assets
- 17 Mineral exploration
- 18 Right to use/exploit non-produced resources between residents and non-residents
- 19 Military expenditures
- 20 Land improvements
- 21 Contracts, leases and licences
- 22 Goodwill and other non-produced assets
- 23 Obsolescence and consumption of fixed capital

- 24 Public-private partnerships (PPPs) (including buy-own-operate-transfer (BOOT) schemes)
- 26 Cultivated assets.
- 27 Classification and terminology of assets
- 28 Amortization of non-produced assets
- 29 Assets boundary for non-produced intangible assets
- 30 Definition of economic assets
- 31 Water as an asset

Issues concerning government and the public sector (considered by TFHPSA and others)

- 6b Allocation of the output of central banks
- 7 Taxes on holding gains
- 25e Non-resident SPEs controlled by government
- 34 Government transactions with public corporations: earnings from equity investment and capital injections
- 35 Tax revenues, uncollectible taxes and tax credits
- 36 Public/private/government sectors delineation
- 37 Granting and activation of loan guarantees

Issues concerning financial services (considered by the Task Forces on Pensions, Insurance, Financial Services and others)

- 1 Repurchase agreements
- 2 Employers' pension schemes
- 3 Employee stock options
- 4a Non-performing loans
- 4b Valuation of loans and deposits; Write-off and interest accrual on impaired loans
- 38c Application of the accrual principle to debt in arrears
- 5 Non-life insurance
- 6a Financial services

Issues concerning financial instruments (considered by BOPCOM and others)

- 42 Retained earnings of mutual funds, insurance companies and pension funds
- 43a Treatment of index-linked debt instruments
- 43b Debt indexed to a foreign currency
- 43c Interest at concessional rates
- 43d Fees payable on securities lending and gold loans
- 44 Financial assets classifications

Issues concerning the rest of the world (considered by BOPCOM)

- 25c Treatment of multi-territory enterprises
- 25d Non-resident unincorporated units
- 38a Change of economic ownership (as term)

- 38b Assets, liabilities and personal effects of individuals changing residence (“migrants’ transfers”)
- 39a Meaning of national economy
- 39b Predominant centre of economic interest (as term)
- 39c Residence of entities with little or no physical presence
- 39d Non-permanent workers
- 40 Goods for Processing
- 41 Merchanting

Issues concerning units

- 25a Ancillary units
- 25b Holding companies, special purpose entities, trusts

Issues concerning informal and illegal activities

- 32 Informal sector
- 33 Illegal activities

Other issues

- 8 Interest under high inflation

1	<p>Repurchase agreements</p> <p>A repurchase agreement (repo) involves the sale of securities or other assets with a commitment to repurchase equivalent assets at a specified price. The market for repos has evolved since the SNA guidelines were prepared; in particular, contrary to what the 1993 SNA suggests, the right to on-selling has become almost universal. The treatment of repos in 1993 SNA and the <i>Balance of Payments Manual</i>, fifth edition, is similar to that of a collateralized loan or as other deposits if repos involve liabilities classified under national measures of broad money. Should the 1993 SNA treatment be revised?</p>
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The treatment of repos has been under discussion for some years in a number of fora. The conclusion in 2005 was that there is still insufficient agreement on how to improve the recording of repos and that there should be no fundamental change to the SNA in respect of them. Rather the question of how best to record them should stay on the research agenda. However, some detailed changes are needed in the text.

The first change is that the present text suggests that on-selling of securities that have been repoed is either not allowed or not practised. This situation has now changed and on-selling is common. The text therefore has to explain that this happens and that when it does a negative asset is recorded for the lender to avoid double-counting.

Further, the 1993 SNA text talks only of repos in terms of a cash collateral. This needs to be extended to cover security collateral, gold swaps and gold loans and deposits.

AEG papers: SNA/M2.04/26 Repurchase agreements
 SNA/M1.05/25.1 Reverse transactions
 SNA/M1.05/25.2 Reverse transactions - Report on e-discussion

2	<p>Employers' pension schemes</p> <p>In the 1993 SNA, promises to pay future pension benefits are not recognized as liabilities of social security schemes or unfunded employer schemes. The review will investigate the analytical relevance of recording liabilities for the latter in the national accounts and, if appropriate, formulate recommendations regarding their valuation and measurement. The review should also address the problems of under- and over-funded defined benefit schemes where at present liabilities are recognized only to the extent that reserves have been built up. The implications for the definition of output of pension schemes, compensation of employees and saving as well as measurement issues need to be addressed. The review will also lead to a reconciliation of the recommendations of the 1993 SNA and the IMF <i>Government Finance Statistics Manual</i> regarding the treatment of unfunded employer pension schemes.</p>
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The 1993 SNA makes a distinction between employer pension schemes and social security even though both are part of social insurance schemes. Employer pension schemes are viewed primarily as being a means of redistributing income over time for a single individual. Depending on the conditions of employment, an employee builds up a claim on his employer during his period of employment for income to be paid after retirement. Social security schemes, in contrast, primarily redistribute income among a set of individuals at a single point in time. It is this notion of redistribution between large sections of the population within the current period that leads to the feasibility of basing their funding on a pay-as-you-go-basis.

These characterisations are not exact. Pension schemes include some element of redistribution, for example from people who die early to those who live longer than expected. Increasingly demographic change calls into question the possibility of maintaining both the levels of social protection provided by social security and the pay-as-you-go nature of funding. Nevertheless, the starting point was that there is a fundamental difference in the claim that an employee will have in future on the pension scheme organised by his employer and that on the government through social security. Investigation soon showed that this presumption is not true for all countries. In some, the distinction between the pension schemes offered by government to its employees is very hard to distinguish from social security. The initial review, therefore, can be seen as comprising two separate elements.

1. What changes need to be made to have a comprehensive recording of pension liabilities and coherent recording of all transactions associated with the functioning of employer pension schemes run by private employers?
2. Can a distinction always be drawn between the benefits due to a government employee under a pension schemes from those due under social security?

Agreement has been reached on how to improve the recording of private employer pension schemes. This is described below. Although discussion continues on how to make the distinction in 2 and, what the further implications may be for the recording of social security schemes in the SNA, agreement has been reached on a promising approach. This too is described below.

Private pension schemes

The 1993 SNA states that the actual social contributions by employer and employee in a period should be the amount actually paid into a pension fund. For a defined contribution scheme (hereafter to be designated a money purchase scheme), this is correct and complete since the

eventual payment depends only on the amounts set aside in a pension fund. For a defined benefit plan, there is no guarantee that the amounts set aside will exactly match the liability of the employer to the employee. In consequence a number of changes to the 1993 SNA in the case of defined benefit plans are proposed.

The level of the employer's contribution should be determined by assessing the increase in the net present value of the pension entitlement the employee has earned in the period in question, adding any costs charged by the pension fund for operating the scheme and deducting the amount of any contribution the employee makes.

This amount must be determined actuarially, taking into account only the life expectancy of the employee and not any future earnings or the impact of any future pay increases on the ultimate pension benefit. While these estimates cannot be made accurately for any individual, robust estimates can be, and are, made for cohorts of employees.

To explain the steady increase in the net present value of future pension payments as retirement gets closer, it is appropriate to record property income payable to the employee and returned to the pension fund as a social insurance contribution supplement. This should be estimated by applying the discount rate used in the actuarial calculations to the pension liability accrued up to the beginning of the period.

An explicit liability of the pension fund to the employee is to be shown in the financial account and balance sheet. The assets of the fund are then to be regarded as belonging to the fund and not (as stated in the 1993 SNA) as belonging to the employee. Depending on the relationship between the fund and the employer, any excess of the liabilities over the available assets may represent a claim of the pension fund on the employer (and any excess of the assets over the liabilities a claim by the employer on the pension fund). In some countries, though, any such shortfall may be covered by an insurance arrangement between the employer and the pension fund. In such a case the insurance related transactions between the employer and the pension fund are to be determined separately from the transactions relating to the provision of pension to the employee.

The use of an actuarial basis for the determination of the amount of the employer's liability has consequences for the items affecting both the other changes in volume of assets account and the revaluation account.

There is a cost to administering any pension scheme and even for a non-autonomous scheme. In principle, there should be a value of output of the fund. This is to be determined on the basis of the sum of costs, and by convention is deemed to be payable by the current employees. The imputed level of the employer's contribution must be large enough to ensure this cost is met.

When an obligation to pay pensions passes from one unit to another, this should be recorded as a transaction in pension liabilities even if neither unit has previously recorded such liabilities.

Government employer schemes

Considerable discussion focussed on how to portray the pension entitlements of scheme for government employees, given the diversity of funding arrangement across countries. In order to make a recommendation that can be widely accepted, it is proposed that a standard table should be prepared in conjunction with the regular accounts showing the pension entitlements accruing to households for all pension schemes, regardless of the means of funding or the category of the unit bearing the responsibility to meet the obligations of the pension scheme. Countries will have flexibility about whether all of these schemes should be carried forward to the "core accounts" (that

is, whether the full increase in the entitlements will be shown as income and saving of households), but in cases where particular schemes are not carried forward, a reasoned explanation for why this is not done will be required. Internationally agreed criteria for when a scheme might not be carried forward should be developed but this might not be possible before the proposed adoption of the updated SNA text in March 2008. In this case, the search for the necessary criteria will form part of the research agenda.

Social security schemes

As part of the work to define precisely the format of the pensions table, consideration will be given to the desirability and feasibility of including information for social security scheme in the same or a similar table.

AEG papers:	SNA/M1.04/13	Treatment of employer retirement pension schemes
	SNA/M2.04/29	Treatment of employer retirement pension schemes
	SNA/M1.05/28	Employer pension schemes
	SNA/M1.06/03.1	The treatment of employer pension schemes and other defined benefit pension schemes
	SNA/M1.06/03.2	Pension schemes
Follow-up papers:	SNA/F1.06/12	Possible compromise on the treatment of pension scheme in the 1993 SNA Rev 1.
	SNA/F1.06/13	Outcome of the AEG consultation

3	<p>Employee stock options</p> <p>Employee stock options are a common tool used by companies to motivate their employees. Given that the 1993 SNA does not provide guidance on their treatment, the question is whether stock options should be considered as compensation of employees and therefore as a cost to employers. Doing so would permit further harmonization with international business accounting standards.</p>
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It is proposed to include the value of employee stock options as a form of compensation of employees in kind. This will slightly modify the coverage of wages and salaries in kind since at present they are restricted to goods and services, and the value of interest foregone when an employer provides cheap loans to staff.

Typically an employer informs his employees of the decision to make a stock option available at a given price (the strike price or exercise price) after a certain time under certain conditions (for example, that the employee is still in the enterprise's employ, or conditional on the performance of the enterprise) The time of recording of the employee stock option in the national accounts has to be carefully specified. The "grant date" is when the option is provided to the employee, the "vesting" date is the earliest date when the option can be exercised, the "exercise" date is when the option is actually exercised (or lapses). In some countries the permissible length of time between vesting and exercise date is quite long; in others it is very short.

IASB accounting recommendations are that the enterprise derives a fair value for the options at grant date by taking the strike price of the shares at that time multiplied by the number of options expected to be exercisable at vesting date divided by the number of service years expected to be provided until the vesting date. This fair value is applied to the number of service years provided in each year to derive the cost to the firm in the year. The fair value per service year is adjusted if the assumptions about the number of options to be exercised alters.

The proposal for the SNA is that the valuation of the options may be estimated using a stock options pricing model or as the difference between the market price and strike price at the vesting date. (If the market price is lower than the strike price, the option has zero value as it would not be exercised.) The time of recording should be spread over the period between the grant date and vesting date, if possible. If this is not possible, the value of the option should be recorded at vesting date. Any change in value between the vesting date and exercise date is not treated as compensation of employees but as a holding gain or loss. During this period, an increase in value of the share price is a holding gain for the employee and a holding loss for the employer and vice versa.

Before the option is exercised, the arrangement between the employer and employee has the nature of a financial derivative and is shown as such in the financial accounts of both parties. It is sometimes possible for these options to be traded or the employer may buy back the option for cash instead of issuing shares. The present item in the financial accounts "financial derivatives" will be changed to "financial derivatives and employee stock options" with a breakdown into the two components.

It is possible that multi-national corporations may offer employees in one economy options on shares of their parent company in another country. The implications for this in respect of foreign direct investment have to be worked out with those responsible for the BPM revision.

There are two consequences of the treatment of employee stock options to be incorporated into the accounts on the grounds of consistency. One relates to other means of rewarding employees that are related to shares in the company. The other relates to the use of stock options to meet expenses other than compensation of employees.

The first consequence is for variations on the basic employee stock option model. A firm may contribute its own shares to the pension fund. This variation is usually called an employee share plan or a stock ownership plan. Under the 1993 SNA, these shares would not have been recognised as claims by households because such funding was not “arm’s length”. With the change to recording pension entitlements rather than the existing assets to meet them, this objection to recording in the same manner as the IASB recommends disappears and should be followed.

Another variation on the use of stock option to reward employees is the offer to employees to purchase shares at advantageous rates under an employee share (stock) purchase plan. Employees are not obliged to accept the offer, but if they do the discount in the share value should be treated as part of compensation of employment. Similarly, if employees receive a benefit relating to the change in a company’s shares but not shares themselves, this payment should be treated as part of compensation of employees.

The second consequence is the possibility that the enterprise pays for goods and services by means of stock options as well as offering these as part of the compensation package to employees. When this happens, the value of the stock option should be estimated if at all possible by the value of goods and services received in exchange. If this is not possible, then similar valuation methods should be used as in the case of employee stock options. The options should be recorded as a form of trade credit between the issuers and the supplier of the goods and services in the financial account. Such arrangements are usually referred to as share (stock) appreciation rights.

AEG paper:	SNA/M1.04/11	Treatment of employee stock options
Follow-up paper:	SNA./F1.06/15	Stock options and employee share ownership plans

4a	<p>Non-performing loans</p> <p>The financial crises of the 1990s led to renewed interest in the statistical treatment of non-performing loans. The purpose of the review is to determine what criteria should be applied in the SNA to the writing-off of non-performing loans and to make sure that they are consistent with the other major macroeconomic statistical systems (balance of payments, government finance statistics, and monetary and financial statistics).</p>
4b	<p>Valuation of loans and deposits; Write-off and interest accrual on impaired loans</p> <p>The valuation of loan positions and deposits are subject to alternative perspectives. Nominal or face value valuation might be misleading because of the risk of default and/or changes in interest rates. This difference becomes apparent when the loans are traded. However, these valuation issues are equally applicable to non-traded loans. Business accounting standards are considering using the concept of “fair value” for the valuation of loans as if they were traded. Should the SNA introduce a valuation other than nominal for deposits and loans?</p>
38c	<p>Application of the accrual principle to debt in arrears</p> <p>The different statistical manuals do not use the same approach to the time of recording for scheduled debt repayments. <i>Balance of Payments Manual</i>, fifth edition, the <i>External Debt Guide</i>, and <i>Government Finance Statistics Manual</i> use the due-for-payment date basis involving imputation of transactions that the liability has been repaid and replaced by a short term debt. The 1993 SNA uses an accrual basis involving no imputation of transactions but continuing to show arrears in the same instrument until the liability is extinguished. If the accrual basis is followed, sub-headings or memorandum items for all or selected arrears might be introduced.</p>

It is proposed to continue to record loans at nominal values in the main accounts and to show interest accruing until a loan is repaid or cancelled by mutual agreement. However, it is proposed that the asset side of balance sheets also show two memorandum items in respect of loans. The first is the nominal value of loans deemed to be non-performing. The second should be the “fair” value of non-performing loans (NPLs), or, if this is not available, their nominal value less expected losses. In addition, interest receivable on NPLs should be shown as an “of which” item. These items would be standard for the government and financial sectors and supplementary for other sectors and for loans with the rest of the world.

There is an agreed definition of what constitutes a non-performing loan and a table will be shown to illustrate how the extra items feature in an accounting of the differences between the levels in the opening balance sheet and those in the closing balance sheet. With this information, supplementary analyses concerning the impact of NPLs will be possible. Investigation of the way in which unpaid FISIM on any sort of loan should be recorded led to the proposal that it should be accumulated to principal outstanding in the same way as (SNA) interest accruing but unpaid.

The outcome of the reflections of the BOP Committee on the application of the accrual principle to debt in arrears is that the BPM should change to follow the 1993 SNA procedure. The *Monetary and Financial Statistics Manual* is already consistent with the 1993 SNA

AEG papers: SNA/M2.04/07 Non-performing loans
 SNA/M2.04/19 Application of accrual principles to debt arrears
 SNA/M1.05/21 Non-performing loans

SNA/M1.06/25.1
SNA/M1.06/25.2

Non-performing loans impact on FISIM
Non-performing loans impact on FISIM - Report on
e-discussion

Follow-up paper: SNA/F1.06/03

Consideration by the ISWGNA on non-performing
loans

5	<p>Non-life insurance</p> <p>Several instances of massive insurance claims, notably those from the 11 September terrorist attack, focused attention on the measurement of non-life insurance services when catastrophic losses occur. This necessarily involves considering the treatment of reinsurance also. The output of insurance services as calculated using the 1993 SNA algorithm depends on the balance of premiums and claims (on an accrual basis). Output can therefore be extremely volatile (even negative) following major catastrophes, and this volatility impacts on GDP and balance of payments (reinsurance). The objective of the review is to propose measures that would be more consistent with the perception of production in this activity. In particular, medium- to long-term aspects of non-life insurance are to be taken into consideration. The issue will also cover the measurement of production of non-life insurance services in volume terms.</p>
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The focus of the update issue was initially on non-life insurance, because of the impact of exceptionally large insurance claims in the recent past. However, the requirement to treat life and non-life insurance consistently means that the recommendations formulated have been considered for both types of insurance.

A number of recommendations have been made to improve the recording of output of insurance, most importantly using adjusted (which in certain conditions is equivalent to expected) claims and adjusted premiums supplements in the algorithm to calculate output, which will avoid most of the undesirable and counter-intuitive volatility resulting from the 1993 SNA algorithm. A consequence of this is that net premiums receivable and adjusted claims due will no longer be necessarily equal period by period.

It is also proposed that for exceptionally large claims, the payment of the claim might be recorded as a capital transfer rather than, as normal, a current transfer.

Reinsurance should in future be treated in exactly the same way as direct insurance and not, as now, netted against direct insurance. This is particularly important for transactions with the rest of the world.

Detailed changes are recommended for the measurement and terminology used concerning the reserves or provisions held by insurance companies and the treatment of payments to agents to bring the SNA treatment more into line with accounting standards.

Explicit guidance has been developed for the calculation of volume estimates of insurance output.

AEG papers:	SNA/M1.04/10	Measurement of the production of non-life insurance Recommendations of the AEG on non-life insurance
	SNA/M2.04/28	Non-life insurance services
	SNA/M1.06/04	The production of financial corporations and price volume measurement of financial services and non-life insurance services

6a	<p>Financial services</p> <p>The business of financial corporations has undergone a structural transformation towards an increasing importance of portfolio management of financial assets with the aim of generating holding gains and a decreasing importance in simple intermediation. The definition of financial corporations and of financial services needs examining to ensure all the activities of financial corporations are adequately captured in the SNA. The review will also cover the measurement of production of financial services in volume terms.</p>
6b	<p>Allocation of the output of central banks</p> <p>The 1993 SNA recommends that the services of central banks be measured on the basis of receipts from fees, commissions, and financial intermediation services indirectly measured (FISIM). This method sometimes results in unusually large positive or negative estimates of output. In 1995, the ISWGNA therefore decided to allow countries to measure the output of central banks, as a second best, at cost. However, the ISWGNA did not provide further guidance on the implications of this method. The review seeks to clarify the impact of the different roles that central banks perform on the nature of their output and the appropriate valuation and allocation to associate with the output of central banks.</p>

Financial services

The definition of a financial corporation is expanded to give due weight to the increase in services other than intermediation, specifically risk management and liquidity transformation. Further, the inclusion of margins on foreign exchange dealing and dealing in securities should be more prominent in the description of explicit fees for financial services.

By convention, while non-financial corporations can provide financial services against a fee, they will not be treated as undertaking FISIM. However, units lending their own funds will be considered financial corporations providing financial services against a fee if they provide loans to a range of clients and incur the financial risk of the debtor defaulting.

Units producing financial services for only one unit or a group of units are to be considered as financial corporations if they keep a complete set of accounts and are capable of acquiring assets and incurring liabilities on their own account.

The recommendation in the 1993 SNA on how to calculate FISIM, as the difference between property income received and interest paid on intermediated funds only is to be changed. FISIM should be calculated on loans (y_L^t) and deposits (y_D^t), only. Assuming that these loans and deposits attract interest rates of r_L^t and r_D^t respectively, FISIM should be calculated according to the formula

$$(r_L^t - rr^t)y_L^t + (rr^t - r_D^t)y_D^t$$

which implies the use of a reference rate (rr). This implies several changes to the 1993 SNA formula. For financial intermediaries, all loans and deposits will be included, not just those made from intermediated funds. Other property income receivable on intermediated funds is excluded. A reference rate is to be used in determining the level of services on loans and deposits separately. Different reference rates may be used for domestic and foreign transactions.

The possibility not to allocate FISIM to users is to be withdrawn.

Specific guidance on deriving a volume measure of output has been developed.

The output of central banks

Separate establishments should be established for units of the Central Bank undertaking market and non-market production when the difference is significant for the accounts as a whole. The non-market activities are to be regarded as acquisition of collective services by general government with a matching transfer from the Central Bank to the Government, so there is no net cost to the Government for these services. Market output is provided on an individual basis to all sectors of the economy against payment for the services.

When the interest rate set by the Central Bank is so high or so low as to imply the inclusion of an implicit tax or subsidy, these should be explicitly recorded as such if they are significant. These taxes or subsidies will be shown as receivable by and payable by government but with a matching transfer from the government to the Central Bank in the case of a tax and a transfer from the Central Bank to government in the case of a subsidy.

AEG papers:	SNA/M1.04/15	Measurement of financial intermediation services and portfolio management
	SNA/M1.04/16	Measurement of the production of central banks
	SNA/M1.05/26	Financial services
	SNA/M1.06/04	The production of financial corporations and price/volume measurement of financial services and non-life insurance services
	SNA/M1.06/05	Output of Central Banks

7	<p>Taxes on holding gains</p> <p>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 suggest alternative treatments or should the SNA treatment remain the same?</p>
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Taxes on holding gains will continue to be shown as current taxes on income and wealth. Where possible and relevant, they should be shown as a separate sub-category.

AEG paper: SNA/M1.04/08 Treatment of taxes on holding gains

8	<p>Interest under high inflation</p> <p>The treatment of nominal holding gains and interest on financial assets under conditions of high inflation was described in the 1993 SNA (Chapter XIX, Annex B) and subsequently in the OECD publication <i>A Manual on Inflation Accounting</i>. These two publications take different approaches, however. What should appear in the 1993 SNA Rev. 1?</p>
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The problem of compiling accounts under conditions of high inflation is much more pervasive than simply deciding how to measure interest. As well as Annex B, section G of Chapter XIX (Application of the integrated framework to various circumstances and needs) deals with the question of compiling accounts under inflation. This section will be re-written drawing on material in chapters 1-6 of *A Manual on Inflation Accounting*, which deal with the problems caused by inflation in the goods and services accounts. The redrafted section will be summary, making reference to that manual.

The item of measuring interest under inflation will remain on the research agenda.

AEG papers:	SNA/M1.04/14	Accounting for interest under high inflation
	SNA/M1.06/34	Interest under high inflation

9	<p>Research and development (R&D)</p> <p>The 1993 SNA does not recognize the output of R&D as capital formation, despite the fact it is thought to be a major contributor to future economic growth. If the SNA were to be changed, should all expenditure on R&D, or only some, be recorded as capital formation? Can all the practical difficulties of deriving satisfactory estimates be overcome, for example by using expenditure data collected in accordance with the Frascati Manual, and obtaining appropriate deflators and service lives?</p>
10	<p>Patented entities</p> <p>In the 1993 SNA, patented entities are treated as non-produced intangible assets. However, payments received from patent users are by convention recorded as payments for services (similar to rentals from an operating lease of fixed assets). This is contrary to the SNA accounting rules, which treat payments for the use of non-produced assets as property income. If R&D is not treated as capital formation, should the payment for use of patented entities continue to be treated as a payment for services?</p>

Research and development should be treated as gross fixed capital formation in the SNA. It should be defined as in the Frascati manual, namely as “research and experimental development comprises creative work undertaken on a systematic basis in order to increase the stock of knowledge, including the knowledge of man, culture and society and use of this stock of knowledge to devise new applications.” This definition should not be interpreted as including human capital as capital formation within the SNA.

By convention, since much R&D is carried out on own account, it should be valued at cost. In practice, the information collected in accordance with the Frascati manual will provide estimates of R&D expenditure; discussion is ongoing to make adjustments to the Frascati framework to meet the needs of the SNA more closely. It is recognised that a detailed guide to implementation will be desirable to assist implementation of this recommendation.

All R&D expenditure that is sold or is expected to bring a benefit in the future to its owner (including for the public in the case of R&D undertaken by government) is included within the asset boundary. Only R&D that brings no economic benefit discernable at the time of its completion is excluded.

With the inclusion of R&D in the asset boundary, patented entities will no longer be separately identified as such in the system, but they will be subsumed into R&D assets.

AEG paper: SNA/M1.05/20 Research and development

Follow-up paper: SNA/F1.06/02 Consideration by the ISWGNA on research and development

Please note: this was the recommendation of the AEG. For later developments, please refer to the main report E/CN.3/2007/7

11	<p>Originals and copies</p> <p>Following the 1993 SNA’s introduction of computer software as capital formation, it became more evident that the SNA does not provide guidance on the treatment of originals and copies as distinct products. Should expenditures on originals and copies both be recorded as expenditure (on new goods) on the basis that originals are distinct from copies, or should originals be considered as being analogous to a ‘stock’ of copies, and so expenditure on a copy partly (or mostly) reflects a sale of an existing good? How should the transactions in copies be recorded?</p>
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The case of software is taken as a paradigm that applies to originals and copies generally.

The act of creating an original leads to the acquisition of a fixed asset if the original satisfies the conditions of an asset, that is it can be a source of economic benefits to the owner over a period of years. These benefits derive from allowing other units to use the content of the original by means of issuing licences for a fee. (These benefits are in addition to any benefits that the owner of the original receives from using the original himself.)

Licences may be issued for use by one or a specified number of users or may be issued with permission to reproduce copies. These are referred to as “licences to use” and “licences to reproduce” respectively.

Licences to use

The generation of copies for issue as licences to use gives rise to production.

A copy of a licence to use purchased with a single payment for use over a multi-year period may be treated as gross fixed capital formation if it is to be used in production for more than one year.

If a copy of a licence to use is purchased with annual payments over a multi-year contract, and if the licensee assumes all the risks and rewards associated with economic ownership of the copy, this may be regarded as the acquisition of an asset under a financial lease.

If annual payments are made for a licence to use without a long term contract, the payments are treated as payments for a service under an operating lease.

If there is a large initial payment followed by a series of smaller payments in succeeding years, the initial payment is recorded as gross fixed capital formation and the succeeding payments as payments for a service.

Licences to reproduce

If the terms under which a unit is given permission to reproduce copies resemble an operating lease, then payments to the holder of the original are recorded as payments for a service.

If the holder of the original divests itself of part or all of the responsibility to issue and service copies under licences to use, this constitutes the sale of part or all of the asset represented by the original.

AEG papers:	SNA/M2.04/06	Originals and copies
	SNA/M1.05/18.1	Originals and copies
	SNA/M1.05/18.2	Originals and copies - Report on e-discussion

12	<p>Databases</p> <p>The 1993 SNA recommends that large databases should be capitalized. Should the SNA provide a clearer definition of databases to be capitalized covering characteristics such as size and marketability of the data as well as the database itself, or should all databases be capitalized? How should the value of a database be determined?</p>
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The non-financial asset category “computer software” is to be changed to “computer software and databases” with a subsequent breakdown between software and databases.

All databases holding data with a useful life of more than one year are fixed assets. Both databases created on own account and those for sale are included if they meet this criterion. However, they are valued differently.

Valuation of databases created on own account

In the absence of a more satisfactory alternative, the value of a database should be estimated on a sum-of-costs basis. The value of the software component of databases, the database management system (DBMS), is to be recorded elsewhere as a software asset.

The remaining value of the database should only include the costs involved in converting the data from one medium/format to that required by the DBMS, including the application costs (setting up the structure of the database, loading metadata, etc.) but excluding the costs of acquiring the data themselves.

All updating costs for a database should be recorded as capital formation rather than maintenance.

Valuation of databases for sale

Databases for sale should be valued at their market price, which includes the value of the information content. If the value of a software component is available separately, it should be recorded as the sale of software.

AEG papers:	SNA/M2.04/04	Databases
	SNA/M1.05/19.1	Databases
	SNA/M1.05/19.2	Databases - Report on e-discussion

13	<p>Other intangible fixed assets</p> <p>In the Annex of Chapter XIII, the 1993 SNA describes this item as consisting of “new information, specialized knowledge, etc. not elsewhere classified” items, whose use in production is restricted to the units that have established ownership rights over them or to other units licensed by the latter”. No specific examples of items to be included have yet emerged. Should this category be retained or removed?</p>
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The category will be retained but will be renamed as “other intellectual property products”.

AEG paper: SNA/M1.06/06 Asset boundary for intangible non-produced assets/Other intangible fixed assets

14	<p>Costs of ownership transfer</p> <p>The cost of transferring ownership of financial assets is treated as current expenditure while that for non-financial assets is treated as capital expenditure. The initial question was whether costs of ownership transfer on non-financial assets should continue to be treated as capital expenditure or be treated as current expenditure. The review was expanded to cover the treatment of costs of ownership transfer on disposal of an asset, including terminal costs, and the period over which costs of ownership transfer should be written off via consumption of fixed capital.</p>
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Costs of ownership transfer should continue to be treated as fixed capital formation.

Costs of ownership transfer on acquisition of an asset should be written off over the period the asset is expected to be held by the purchaser rather than over the whole life of the asset. Costs of ownership transfer on the disposal of an asset, and also terminal costs (for example dismantling costs) should also be written off over the period the asset is held but recorded when they are actually incurred. When this recommendation on terminal costs cannot be followed for lack of adequate data, these costs should still be recorded as gross fixed capital formation but written off as consumption of fixed capital in the year of acquisition.

Installation and de-installation costs should be included in the costs of ownership transfer when they are separately invoiced and in the purchaser's price of the asset otherwise.

AEG papers: SNA/M1.04/12 Costs of ownership transfer on non-financial assets
 SNA/M2.04/10 Cost of ownership transfers - part II

15	<p>Cost of capital services</p> <p>Capital services provided by non-financial assets to the production process are not explicitly defined by the 1993 SNA. The OECD manual <i>Measuring Capital</i> defines capital inputs as the actual or estimated pure economic rent payable; that is, by the sum of consumption of fixed capital, expected holding gains/losses and the capital, or interest, costs. The rental, paid by the user of a rented non-financial asset to the owner, covers both the costs incurred by the owner in providing the service and the capital services rendered by the asset to the owner. For non-financial assets used by the owner, capital services appear implicitly as part of the gross operating surplus. How should the concept of capital services be articulated in the SNA?</p>
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Capital services for assets used in market production are implicitly included within the 1993 SNA but are not separately identified. Given the importance of identifying them for productivity measurement and other analysis, a new chapter will be added to the 1993 SNA Rev 1 explaining the role and appearance of capital services in the system and stressing the desirability of calculating capital services, capital stock and consumption of fixed capital in an integrated and consistent manner. No changes will be made to standard entries in the accounts to show capital services but an explanation will be provided of how optional, supplementary items or tables could be derived and presented.

AEG papers:	SNA/M2.04/15	Cost of capital services in the production account
	SNA/M1.05/04	Cost of capital services

Please note: this was the recommendation of the AEG. For later developments, please refer to the main report E/CN.3/2007/7

16	<p>Government and non-market producers: cost of capital of own assets</p> <p>When summing costs to measure non-market output, the 1993 SNA recommends that the value of the services provided by a producer's own non-financial assets should be measured as consumption of fixed capital. This means that neither a return on capital to these assets nor, equivalently, an opportunity cost of capital is recognized. This leads to an inconsistency with the rental that would have to be paid if the assets were rented. Should the SNA recommendation be changed and the cost of consumption of fixed capital be replaced with capital services (consumption of fixed capital, expected holding gains/ losses and the capital or interest costs)?</p>
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After extensive discussion, reflection and wide consultation, it is proposed that a return to fixed capital owned and used by non-market producers should be included in the estimation of the output of those producers in addition to estimates of consumption of fixed capital. The restriction to fixed assets is a compromise between what might be conceptually desirable and what is likely to be implementable in practice. For the rate of return, it is suggested to use the expected real rate on government bonds if necessary supplemented by other indicators of the cost of borrowing to government.

AEG papers:	SNA/M2.04/08	Government owned assets - cost of capital services
	SNA/M1.05/05	Government and other non-market producers: cost of capital of own assets
	SNA/M1.05/05.1	Result of Global Consultation on Government and other non-market producers
	SNA/M1.06/07	Government and other non-market producers' owned assets - Cost of capital services

Please note: this was the recommendation of the AEG. For later developments, please refer to the main report E/CN.3/2007/7

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17	<p>Mineral exploration</p> <p>Expenditures on mineral exploration are classified in the 1993 SNA as gross fixed capital formation. The rationale is that mineral exploration creates a stock of knowledge about the reserves that is used as input in future production activities. The question has been raised as to whether this knowledge should be seen as independent of the stock of economically exploitable reserves or whether this leads to double accounting when both discovered stocks of resources and stock of exploration are capitalized.</p>
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It is recommended that a distinction will continue to be maintained between the act of exploring for mineral deposits (treated as a produced asset) and the mineral deposits themselves (treated as non-produced assets). The terminology for exploration will be changed to “mineral exploration and evaluation” to match the term used in the International Accounting Standards and the definition of the terms will also be brought into line with the IASB definition.

Clarification of the existing text will be added to make it clear that the item is valued at market prices if purchased or at the sum of costs plus an appropriate mark-up if undertaken on own account.

As well as clarifying the treatment of mineral exploration, the AEG also clarified some aspects of the accounting for mineral deposits.

Because a market price is seldom available for mineral deposits, the default valuation is the present value of future receipts of resource rent.

Payments by the extractor to the owner of the deposits corresponding to a share of the resource rent should continue to be shown as property income even if they are described as taxes and treated as such in government’s own accounts.

It is recommended that when the legal owner of a mineral deposit contracts with another unit to undertake extraction, in principle the value of the stocks to be extracted under the contract should be included in the balance sheet of the extractor with a financial lease arrangement with the legal owner. However, the value of the stock is liable to alter frequently in response to technical discoveries, changes in the rate of extraction and changes in the price of the mineral. These changes all affect the terms of the financial lease, both the amount of the loan and how payments due under it are recorded. Therefore as a matter of practice, the deposit may continue to be shown on the balance sheet of the legal owner with payments by the extractor to the owner being entered as property income (rent).

AEG paper:

SNA/M2.04/05

Mineral exploration

18	<p>Right to use/exploit non-produced resources between residents and non-residents</p> <p>Except for land, transactions between residents and non-residents relating to the right to use or exploit non-produced resources have not been fully elaborated in the 1993 SNA. For land, a notional resident unit is created that is deemed to purchase the land while the non-resident is deemed to purchase a financial asset (equity) of the notional unit. Should the treatment of land be extended to other non-produced resources such as water, fish, etc. or should there be alternative treatments?</p>
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Notional resident units are to be created when a non-resident unit:

is the legal owner of land,

has a financial lease on a building or other immovable structure

has a licence to extract natural resources over a number of years.

It is probable that the holder of a licence to use the radio spectrum of a country is resident except for geographically small countries where cover is provided by facilities in neighbouring countries.

Extraction of static or land-based natural resources on a short-term basis does not lead to the creation of a notional unit. In these cases, a fee for one-time extraction represents the sale of an asset. Illegal extraction should be recorded as an uncompensated seizure.

A fishing vessel becomes resident only if the operator establishes a base in the country in question, otherwise the residence of the vessel remains that of the operator, regardless of the area in which it is fishing. In principle, illegal fishing should be recorded as uncompensated seizure.

Fish quotas are to be treated as licences to undertake specific activities as described under issue 21.

AEG papers:	SNA/M1.06/26.1	The right to use/exploit non-produced resources between residents and non residents
	SNA/M1.06/26.2	The right to use/exploit non-produced resources between residents and non residents - Report on e-discussion

19	<p>Military expenditures</p> <p>The 1993 SNA divides military acquisitions into offensive weapons and their means of delivery, and all other. The former are excluded from capital formation regardless of their life length. This treatment implies that “defence” is not a service provided by government using military hardware as associated assets. Further, 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?</p>
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In future, all expenditure by the military that meets the definition of being used in production over a period in excess of one year will be treated as capital formation, regardless of the nature of the expenditure or the purpose intended for it. All equipment will be treated as fixed capital formation except for consumables, which will be treated as inventories. Separate items will identify weapons systems within fixed capital formation and military inventories apart from other inventories. (Strategic inventories will no longer be separated from other inventories of the same type of products.)

AEG paper: SNA/M1.04/09 Treatment of military weapon system as fixed assets

Please note: this was the recommendation of the AEG. For later developments, please refer to the main report E/CN.3/2007/7

20	<p>Land improvements</p> <p>The 1993 SNA records improvements to land as gross fixed capital formation, but in the balance sheet such improvements are included with land itself – a non-produced asset. Should land be split into two, with one part recorded as a fixed asset and the other part recorded as a non-produced asset? If so, how should the separation be made? One option is to distinguish between land that is in, or nearly in, its natural state as a non-produced asset and the remainder as a fixed asset. Another option is to separate land from the improvements made to it, and record the former as a non-produced asset and the latter as a fixed asset.</p>
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In future land improvements will be shown not only as gross fixed capital formation but as a produced asset distinct from natural land. Costs of ownership transfer on land should be treated as fixed assets and included with land improvements. The total value of a plot of land is to be considered as the sum of the land improvements on the plot (if any) plus the value of the plot in its unimproved state. The latter is described simply as “land”.

Where it is not possible to partition the value of land between land improvement and natural land components, the whole value should be allocated to one or the other category depending on which is assumed to represent the greater part of the value.

Clarification is also provided about when construction activity is to be regarded as land improvement and when it is to be treated as structures. Activities such as land clearance, land contouring, creation of wells and watering holes that are integral to the land in question and that are carried out by the landowner are to be treated as part of land improvements. Activities such as the creation of sea walls, dykes, dams and major irrigation systems that are in the vicinity of the land but not integral to it, often affect land belonging to several owners and which are often carried out by government, are to be classified as structures.

AEG papers:	SNA/M1.05/22.1	Land improvements and structures
	SNA/M1.05/22.2	Land improvements and structures - Report on e-discussion
	SNA/M2.04/09	Treatment of land

21	<p>Contracts, leases and licences</p> <p>The 1993 SNA refers to contracts, leases and licences in a number of contexts but there is no overview that sets out the principles of the appropriate treatment of all such arrangements. Further, clarification is desirable concerning several specific points:</p> <ol style="list-style-type: none"> 1. the definition and treatment of operating and financial leases on fixed assets, 2. when legal constructs should be recognized as assets, 3. whether tradable government permits should be treated as assets, 4. can sub-contracting lead to the creation of an asset, 5. can a difference between a contract price and the corresponding prevailing price affect the treatment of existing leases.
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Extended discussion on the five points listed in the issue description led to the following recommendations:

1. The definition of operating and financial leases will be clarified. In particular it will be clear that a lease may be a financial lease even if it is not for the whole of the life on a fixed asset.

A new form of lease, a resource lease, will be introduced to cope with the case where all the benefits from using a natural resource in production fall to the lessee but the resource remains on the balance sheet of the legal owner.

2 and 4. Most contracts do not represent assets but two cases exist when they may. The first case applies to contracts where one party agrees to provide goods or services to the second party in the future at a stated price or to permit the second party to use non-financial assets belonging to the first party on agreed terms. A contract may represent an asset when a price difference appears between the price specified in the contract and the market price for a comparable product or rental of a non-financial asset, and the second party to the contract is legally and practically able to take advantage of this difference by transferring the delivery of the product or the rental to a third party. The second case is when contracts (permits) that allow the second party to undertake some activity for which permission is a necessary requirement allow that party to obtain some degree of monopoly profits in the exercise of the sanctioned activity.

3. Government permits to undertake specific activities, even when these are limited in number and may be competed for by auction or similar competitive application, are to be recorded as taxes. If the permit covers multiple periods, the tax should be recorded on an accrual basis if government

has an obligation to refund the value of the unused part in the case of a revocation or surrender. If government has no such obligation, the whole of the payment is recorded as a tax when paid. In addition the acquisition of an asset is recorded. As with transferable contracts just described, whether or not an asset is recorded in respect of a permit, if the initial holder of the permit can legally and practically sell the permit than its current value, this is also regarded as an asset.

5. The value of an asset is to be determined taking account of the returns to the asset payable under the terms of the lease and not on the basis of returns that might be received in the absence of such a lease.

Discussion also clarified that when the benefits of a natural resource are shared between the lessee and the lessor, a financial lease should be construed to exist between the two parties.

AEG papers:	SNA/M1.06/08	Contracts and leases: Government permits
	SNA/M1.06/09.1	Leases and licences (part 1)
	SNA/M1.06/09.2	Leases and licences (part 2)

22	<p>Goodwill and other non-produced assets</p> <p>The 1993 SNA records goodwill (as purchased goodwill) only when an enterprise is sold, and it treats purchased goodwill for corporations and unincorporated enterprises differently. Should goodwill continue to be recognized only when purchased or should internally generated goodwill be recognized? Should purchased goodwill be treated the same way for corporate and unincorporated enterprises? Should the balance sheet recognize assets such as brand names, trademarks, franchises, etc.?</p>
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Because it is usually not possible to separate goodwill from other entities such as customer lists, franchise arrangements, mastheads, logos etc. that add value to an enterprise, the category of “purchased goodwill” will be changed to “purchased goodwill and marketing assets”. Entries will continue to be recorded only when the value of such entities is evidenced by a sale but the possibility of a marketing asset being sold independently of the sale of the entire enterprise is noted.

For all enterprises, whether incorporated or quasi-corporate, the value of purchased goodwill and marketing assets will be valued as the takeover value of the enterprise less the value of other assets and liabilities identified in the SNA for the enterprise. This represents a change for incorporated enterprises and makes their treatment consistent with quasi-corporate enterprises.

Although some of the value of purchased goodwill and marketing assets is due to productive activity, they will continue to appear under the heading of non-produced assets, though at a higher level in the hierarchy than previously, specifically at the same level as natural assets, and contracts, leases and licences.

Amortisation of these assets should be in accordance with international accounting guidance on impairment tests for the remaining value.

AEG papers:	SNA/M1.05/24.1	Purchased goodwill and marketing assets
	SNA/M1.05/24.2	Purchased goodwill and marketing assets - Report on e-discussion

23	<p>Obsolescence and consumption of fixed capital</p> <p>Consumption of fixed capital is defined in the 1993 SNA in general terms as the decline, during the course of the accounting period, in the current value of the stock of fixed assets owned and used by a producer as a result of physical deterioration, normal obsolescence or normal accidental damage. This decline is expressed in the average prices of the period, but the 1993 SNA does not give guidance about whether the prices to be used should relate to the general price level or whether they should be asset specific.</p>
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It is agreed that the prices in question should be the prices of an asset of constant quality. The text of the 1993 SNA is to be expanded to describe the consequences of this clarification.

AEG papers: SNA/M1.05/06 Obsolescence and depreciation

24	<p>Public-private partnerships (PPPs) (including buy-own-operate-transfer (BOOT) schemes)</p> <p>Public-Private Partnerships (PPPs) are complex legal arrangements designed to share the control and the risks and rewards of a set of fixed assets between a private enterprise and a public unit, normally a unit of the general government sector. In most PPPs, the assets are legally owned and used by the private enterprise to produce a specified category of services for several years, and then the government gains operational control and legal ownership of the assets, often without payment. The 1993 SNA treatment of operating and financial leases are not sufficient to derive an appropriate accounting treatment for PPPs and there are no other guidelines given about PPPs. There are two major issues to be resolved. The first is to decide whether the private enterprise or the government is the economic owner of the fixed assets. The second is to decide the appropriate recording for transactions between the private enterprise and the public unit during the period covered by the PPP arrangement.</p>
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Public-Private Partnerships (PPPs) or Private Finance Initiatives (PFIs) are relatively new ways of government seeking to work with private enterprises to provide assets and services for public use without the government incurring all of the costs at the inception of the project. The terms of such agreements are still evolving and the International Public Sector Accounting Standards (IPSAS) has yet to conclude exactly how these schemes should be recorded in accounting terms.

The recommendation is that indicative guidance on the characteristics to be examined to determine whether the private or public partner is the economic (as opposed to legal) owner of the assets in question should be provided in an annex in the SNA Rev.1. Placing the material there will allow the annex to be updated separately from a generalised update if and when more specific guidance emerges from IPSAS or for any other reason, it is decided that a more specific set of guidelines for how PFIs are to be recorded within the SNA is appropriate.

AEG paper: SNA/M1.06/10 Public-private partnerships

25a	<p>Ancillary units</p> <p>The 1993 SNA specifies that units conducting only a specified list of activities designated as “ancillary” should not be treated as separate units but their costs should be consolidated with the units they serve. This means that when accounts for a region are compiled, head offices and other ancillary units located there are excluded if the units they serve are located outside the region. This results in a difference between ancillary units located abroad, which are treated as separate units, and those that are resident but distant from their related enterprises. Should the principle of not treating ancillary units as separate units be changed and what are the consequences throughout the accounts?</p>
25b	<p>Holding companies, special purpose entities, trusts</p> <p>As part of the innovation in financial markets and asset management over the last decade, several forms of separate entities have come into existence that only hold assets or liabilities but do not engage in production. Such entities are separate new or existing legal structures assigned for specific purposes such as specialized portfolio management of assets and debts, restructuring agencies, special purpose entities, shell companies, limited liability partnerships or trusts. Should these entities be treated as ancillary and merged with their related enterprises, or should they be treated as separate units? If they are separate units, to which sector should they be allocated?</p>
25c	<p>Treatment of multi-territory enterprises</p> <p>The 1993 SNA follows the <i>Balance of Payments Manual</i> in allowing for a single enterprise run as a seamless entity with substantial operations in two or more economic territories to be regarded as having a centre of economic interest in each of the countries where it is recognized by the tax and licensing authorities, but only when the activity is operating mobile equipment such as ships, aircraft and railways. In these cases, the possibility is for all the enterprise’s transactions to be allocated to the countries of registry in proportion to the financial capital that the countries have contributed or their share of equity in the enterprise. Should this treatment be extended to other activities, for example hydro-electric schemes on border rivers and pipelines? Should reference be made to joint sovereignty zones and zones of joint jurisdiction?</p>
25d	<p>Non-resident unincorporated units</p> <p>The <i>Balance of Payments Manual (BPM)</i> indicates that establishments of enterprises located in a country different from the country of residence of the parent should be treated as notional units, resident in the country where located under certain conditions. The SNA discusses non-resident unincorporated enterprises rather than establishments. Should the SNA and <i>BPM</i> be more closely aligned?</p>
25e	<p>Non-resident SPEs controlled by government</p> <p>Is special treatment required for non-resident units established abroad by government for fiscal purposes?</p>

25a. Ancillary units

Ancillary activities

A productive activity is described as “ancillary” when the resulting product is of a type common to all or most enterprises and is used for intermediate consumption within the same enterprise. The scope of ancillary activities is limited; it does not apply to all production that is consumed solely by the parent enterprise. In particular while payroll activities may be treated as ancillary, portfolio management is not because it is usually only larger enterprises, or specialized financial enterprises,

that may manage their own portfolios. There is no change to this concept and the following recommendations are built around it.

Ancillary establishments

If an establishment undertaking purely ancillary activities is statistically observable, in that separate accounts for the production it undertakes are readily available, or if it is in a geographically different location from the establishments it serves, it may be desirable and useful to consider it as a separate unit and allocate it to the industrial classification corresponding to its principal activity. However, it is recommended that statisticians do not make extraordinary efforts to create separate establishments for these activities artificially in the absence of suitable basic data being available.

When such a unit is recognized, its output should be derived on a sum-of-costs basis, including the costs of the capital used in the unit. The output will be deemed to be market output when the parent enterprise is a market enterprise and non-market otherwise. The output of the ancillary unit is treated as intermediate consumption of the establishments it serves and should be allocated using an appropriate indicator such as the output, value added or employment of these establishments.

Ancillary corporations

The original rationale for the treatment of ancillary corporations as integral to the units they serve was when they represent artificial units created for legal or tax reasons. In these circumstances, the 1993 SNA treatment should stand; an institutional unit will continue to be separately identified when it is non-resident.

25c Multi-territory enterprises

This question arose in the context of the BPM revision. It is agreed that the SNA and BPM will stay aligned in this as in other areas. The treatment of multi-territory enterprises will be extended to cover activities such as those mentioned in the issue description. The transactions of multi-territory enterprises operating in zones of joint sovereignty or joint jurisdiction will be prorated to the territories concerned using criteria to be specified in the BPM.

25d Non-resident unincorporated units

The BPM5 criteria for identifying a notional resident unit is that the unit should

- Engage in significant production of goods and services,
- Plan to operate the business indefinitely or for a long period of time,
- Have a substantial physical presence,
- Maintain a complete and separate set of accounts of local activities
- Pay income tax to the host country
- Receive “funds for enterprise work for the enterprise account”.

The 1993 SNA simply states that an unincorporated enterprise owned by a non-resident institutional unit should be treated as a notional resident unit in the country where it is located.

It is agreed that physical presence is not necessary; units involved in financial intermediation and operating leasing are examples where physical presence is not essential. The requirement to have a full set of accounts is too restrictive; if a unit engages in production it should be treated as a notional resident unit in the host country. Being subject to the income tax laws of the host country rather than necessarily paying income tax is a preferred criterion.

The list of criteria should be taken to be indicative and a unit may be treated as a notional resident unit even if not all criteria are met.

25b Holding companies, SPEs, trust funds

Holding companies are not ancillary units; the functions they perform to control and direct subsidiary companies are not ancillary activities. The 1993 SNA classifies them as non-financial or financial corporations depending on the classification of their subsidiary companies. In future, holding companies will all be treated as “other financial institutions”.

Special Purpose Entities (SPEs)

Resident SPEs will not be treated as separate institutional units unless they satisfy the criteria for qualifying as institutional units. Their output should be valued at cost if no market valuation is available. Non-resident SPEs are always to be classified as separate institutional units.

SPEs are to be classified by sector and industry according to the principal activity of the SPE.

Investment funds

Investment funds that are created as legal entities, even without employment, should be treated as institutional units. Their output should be valued at cost if no market valuation of their output is available. These units are to be classified as “other financial institutions”.

Restructuring agencies

If the restructuring agency acts only to implement pre-specified government policy and bears no risk in the transformation of financial instruments connected with the restructuring, the agency is regarded as a non-market unit and part of the general government sector.

If the restructuring agency puts itself at risk in the transformation of the assets and liabilities of the units in difficulty and if it can determine the costs it can charge for the restructuring activity, it is treated as a financial corporation. Whether it is publicly controlled or a private financial corporation is determined using the usual criteria.

When government uses a restructuring unit to channel funds to a unit in financial difficulties and the restructuring unit derives its main resources from activities other than acting as an agent of government, these funds should be shown as payable and receivable by the government and unit concerned directly and not routed via the restructuring agency.

25e Non-resident SPEs controlled by government

The term “securitization vehicle” is reserved for units that only undertake securitization of assets. These are to be classified as “other financial institutions”. Securitization based on a future flow of revenue is not the sale of an asset but borrowing. If a non-resident SPE borrows, the economic substance is best reflected by imputing a borrowing by the resident parent from the SPE at the same time as the SPE incurs a liability to a foreign creditor. Although this principle has general validity, it will be applied only for non-resident SPEs created by government for fiscal purposes.

AEG papers:	SNA/M1.06/11	Units in the 1993 SNA
	SNA/M1.06/42	Globalization
	SNA/M1.05/27.1	Multi-territory enterprises

SNA/M1.05/27.2 Multi-territory enterprises - Report on consultation
SNA/M1.05/31 Non-resident SPEs linked to general government
SNA/M2.04/21 Treatment of multi-territory enterprises
SNA/M2.04/22 Holding companies, special purpose entities, and trusts
SNA/M2.04/23 Recognition of unincorporated branches

Follow-up paper: SNA/F1.06/01 Consideration by ISWGNA on head offices and holding companies

26	<p data-bbox="311 241 507 271">Cultivated assets</p> <p data-bbox="311 309 1369 488">During discussions about the System of Economic and Environmental Accounts, it was noted that the present definition of cultivated assets in the SNA is ambiguous. Should the definition in the SNA be tightened as follows: “cultivated assets cover livestock for breeding, dairy, draught, etc. and vineyards, orchards and other trees yielding repeat products <i>whose natural growth and regeneration are</i> under the direct control, responsibility and management of institutional units”? The words in bold italics replace the words “that are” in the 1993 SNA.</p>
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This change to the definition of cultivated assets is agreed. It brings symmetry with the definition of uncultivated assets.

27	<p>Classification and terminology of assets</p> <p>Should the classification of non-financial assets be revised in light of the review of a wide range of non-financial assets? Is the tangible/intangible dichotomy still of primary importance in the classification?</p>
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Bringing together the recommendations arising from other issues on the categorization and the terminology for non-financial assets results in the table below to replace the classification of non-financial assets in the 1993 SNA. In addition to the assets themselves, it is proposed to change the items appearing in the other changes in assets account to give a more structured listing of possible causes for changes in assets other than transactions and price changes.

AEG papers: SNA/M1.06/12 Classification and terminology of non-financial assets

Proposed revised classification of non-financial assets

Non-financial assets

Produced assets

Fixed assets

Dwellings

Other buildings and structures

Non-residential buildings

Other structures

Land improvements

Machinery and equipment

Transport equipment

ICT equipment

Other machinery and equipment

Weapons systems

Cultivated biological resources

Animal resources yielding repeat products.

Tree, crop and plant resources yielding repeat products

Costs of ownership transfer on non-produced assets

Intellectual property products

Research and development

Mineral exploration and evaluation

Computer software and databases

Computer software

Databases

Entertainment, literary or artistic originals

Other intellectual property products

Inventories

Materials and supplies

Work in progress

Work in progress on cultivated biological resources

Other work in progress

Finished goods

Military inventories

Goods for resale

Valuables

Precious metals and stones

Antiques and other art objects

Other valuables

Non-produced assets

Natural resources

Land

Mineral and energy reserves

Non-cultivated biological resources

Water resources

Other natural resources

Radio spectra

Other

Contracts, leases and licences

Third party property rights

Marketable operating leases

Permissions to use natural resources

Permission to undertake specific activities

Entitlement to future goods and services on an exclusive basis

Of nominated legal persons

Of future production

Goodwill and marketing assets

The classification is designed to be consistent with that used in the SEEA for natural resources. The SEEA contains a further level of standard headings under each of the headings shown in the SNA. If more detail is held to be desirable in SNA tables, it is recommended that the supplementary items should follow the detail of the SEEA.

Proposed entries in the “Other changes in volume of assets account”

Entries applying to a restricted number of assets

Economic recognition of produced assets (K4)

Public monuments

Valuables

Increase in the value of natural resources

Discoveries and upwards reappraisals of sub-soil resources (K3)

Natural growth of uncultivated biological resources (K5)

Transfers of other natural resources to economic activity

Quality changes in natural resources due to changes in economic uses

Decrease in the value of natural resources

Extractions and downwards reappraisals of sub-soil resources (K61)¹

Harvesting of uncultivated biological resources

Transfers of other natural resources out of economic activity

Quality changes in natural resources due to changes in economic uses

Initiation of contract, leases and licences (K3)

Relating to third party property rights

Marketable operating leases

Permissions to use natural resources

Relating to the entitlement to future goods and services

Termination of contracts, leases and licences (K62)

Relating to third party property rights

Marketable operating leases

Permissions to use natural resources

Relating to the entitlement to future goods and services

Changes in the value of goodwill and marketing assets (K62)

Appearance and disappearance of financial assets and liabilities

Debt operations

Creation and exhaustion of financial derivatives

Entries applying to all classes of assets

Catastrophic losses (K7)

Uncompensated seizures (K8)

Other volume change (K9 and K10)

Changes in sector classification and structure

Changes in the classification of assets and liabilities

Code numbers in brackets are the code numbers of the 1993 SNA. Items without code numbers are new or a breakdown of existing items.

28	<p>Amortization of non-produced assets</p> <p>The final report of the ISWGNA in 2001 on mobile phone licenses includes a brief discussion of the issue of the amortization of intangible non-produced assets. Can a way be found to show the impact on net worth of the decline in the value of non-produced assets due to production via transactions rather than as other changes in the volume of assets?</p>
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Despite the theoretical attractions of showing the decline in value of non-produced assets as a cost of production, as yet no satisfactory method of doing so has been agreed. As a result, the present treatment of showing the decline in the value of non-produced assets in the other changes in assets account will be maintained.

AEG papers: SNA/M1.06/13

Amortisation of intangible non-produced assets

29	<p>Assets boundary for non-produced intangible assets</p> <p>The category “other non-produced intangible assets” in the 1993 SNA was a placeholder intended to accommodate any new assets of similar type to those in the general category which did not fall in the more specific headings. However, this heading has been used in some instances to cover the securitization of future receipts of government. Should the heading continue to be included in the classification hierarchy and if so, what sort of items should be included in it?</p>
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The use of SPEs controlled by government as securitisation vehicles was covered as part of the discussion of issue 25 concerning units. It was agreed that a future stream of revenue is not regarded in the System as an asset. Securitisation based on such a stream should therefore be recorded as borrowing.

It is proposed that the category of assets “other intangible non-produced assets” should be dropped.

AEG paper: SNA/M1.06/06 Asset boundary for intangible non-produced
assets/Other intangible fixed assets

30	<p>Definition of economic assets</p> <p>The SNA should provide a clear definition of what constitutes an asset that is consistent with where the asset boundary falls in respect of currently known entities, as well as providing guidance for determining whether entities that appear in the future fall within the asset boundary. It should be accompanied by guidance on how assets should be valued. Does the definition in the 1993 SNA need further elaboration?</p>
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Expanded text building on the existing definition of an asset will cover issues such as the responsibility for risk in relation to determining ownership, demonstrable value and contingent obligations.

AEG paper: SNA/M1.06/14 Definition of economic assets

31	<p>Water as an asset</p> <p>When water is no longer free, how should the charge for it be treated? Although a large share of the charges represents distribution costs, is there an element that should be treated as giving rise to rent in a similar way to land or mineral resources? How should the use of water as a sink for waste be treated?</p>
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In recognition that water is becoming scarce in some places and at some times, it is proposed that the SNA include guidance that allows water to be treated in a way more similar to mineral resources, that is with an inherent value (resource rent) and with the delivery of water being the delivery of a product and not just a transportation service. The specific proposals follow. Water resources should be extended to include rivers, lakes, artificial reservoirs and other surface catchments in addition to underground aquifers and other groundwater resources, always assuming the enforcement of ownership rights and some measure of economic control as for other natural resources considered as assets.

In principle, water bodies treated as assets should be valued in a manner similar to that of valuing mineral resources but in practice more pragmatic alternatives may be necessary such as estimates based on access fees.

It is recognized that surface water may be associated with land under cultivation. In all cases where water and land co-exist and separate valuations are difficult, the combined asset should be allocated to either land or water depending on which is thought to have the greater share of the value.

Carrying water is recognized as production in the 1993 SNA. This is consistent with the concept that water as delivered represents a product (whether in the form of bottled water, water from a tap or in an open container) and not just the provision of a service of transporting water.

When fees are charged to discharge dirty water or other liquids into water bodies, these should be recorded in the accounts in a manner consistent with other such charges. (See issue 21, contracts, leases and licences).

AEG papers:	SNA/M1.05/23.1	Water as an asset
	SNA/M1.05/23.2	Water as an asset - Report on e-discussion
	SNA/M1.06/27.1	Water
	SNA/M1.06/27.2	Water - Report on e-discussion

32	<p>Informal sector</p> <p>An extract from the resolution on statistics of employment in the informal sector adopted by the Fifteenth International Conference of Labour Statisticians (January 1993) is reproduced as an annex to chapter IV in the 1993 SNA. The resolution, among other things, provides an international statistical definition of the informal sector. However, the SNA does not amplify on the definition or provide guidance on its application in a national accounting context. Given that the informal sector accounts for a substantial portion of production in many countries, such guidance has often been requested. The review should consider whether the updated SNA can provide guidance drawing on work by the Delhi Group on Informal Sector Statistics and by ILO, UNECE, IMF, the Commonwealth of Independent States, and OECD in preparing <i>Measuring the Non-observed Economy: A Handbook</i>.</p>
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The role of the informal sector and how to achieve better economic understanding and statistical coverage of it was one of the items placed on the research agenda at the time the 1993 SNA was finalized. The importance of the issue has grown rather than diminished since but there are now several statistical initiatives and sources that allow a more specific treatment in the updated SNA.

It is proposed to include a chapter on the informal sector, which will discuss the conceptual basis of an informal sector, informal production, and informal employment. It is important to recognize the use of these terms by other organizations, especially the ILO, and relate them to SNA counterparts, explaining clearly that the same words are sometimes used in different statistical systems with somewhat different meanings and coverage. The goal of the chapter is to allow an articulation between the comprehensiveness of all economic activity in the SNA and the subset of activity in the household sector that is of particular policy interest in the “informal sector” context.

A group including some members of the AEG is working on developing such a chapter in collaboration with others interested in the field including at the ILO and in the Delhi group.

AEG papers:	SNA/M2.04/12	Informal sector
	SNA/M1.06/15	The Informal Sector in the <i>1993 SNA, Rev. 1</i>

33	<p>Illegal activities</p> <p>Since the publication of the 1993 SNA, the handbook <i>Measuring the Non-observed Economy</i> has considered in detail and provided recommendations on the recording of illegal activities such as bribery, extortion and money laundering in addition to theft and fencing. The review should consider to what extent the recommendations included in the <i>Handbook</i> on the recording of production and redistribution of income from such activities should be included in the updated SNA.</p>
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The 1993 SNA makes clear that the fact that an activity is illegal is not in itself a reason to exclude it from the SNA accounts. The publication of the *Non-observed Economy* handbook provides welcome advice about how in practice reasonable estimates might be made for some of the more important illegal activities. This handbook will be referred to and some examples quoted in the updated SNA. However, the recommendations in the handbook that theft and bribery should be included in output are felt to be inconsistent with the SNA production boundary and these activities will not be treated as production. The only exception is when production has previously taken place, the output has been placed in inventories and there is subsequently an exceptional loss from inventories. In this case the loss is recorded as an other change in the volume of assets and no change in the level of output in either the current or a past period is made. Regular losses from inventories are treated as increasing the value of intermediate consumption or reducing the value of output; pilfering from current production is also not recorded as output.

AEG papers:	SNA/M1.06/28.1	Illegal activities in the 1993 SNA
	SNA/M1.06/28.2	Illegal activities in the 1993 SNA - Report on e-discussion

34	<p>Government transactions with public corporations: earnings from equity investment and capital injections</p> <p>The 1993 SNA treatment of withdrawals from quasi-corporations differs from that of payment of dividends from corporations. Dividends are always assumed to be from current earnings, but withdrawals from quasi-corporations may not be. Public corporations are often quasi-corporations and the treatment accorded quasi-corporations allows government to manage the pattern of withdrawals from one year to another for political reasons. Should the SNA be amended to limit this possibility and if so which of two possibilities is recommended?</p> <p>The first option is to bring the treatment for quasi-corporations more into line with that for corporations in respect of large and exceptional payments (like super-dividends) as well as of capital injections made by the government as the owner.</p> <p>The second option would be to adopt an approach for public corporations similar to that for direct investment enterprises and show redistributed earnings (or losses) of public corporations as accruing in the government accounts and then reinvested in (or withdrawn from) the equity of the corporation .</p>
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The 1993 SNA specifies that regular payments from public corporations to government are recorded as dividends and that payments from quasi-corporations are recorded as withdrawals from entrepreneurial income. Exceptional payments from a public corporation are recorded, as are regular payments, as dividends. Exceptional payments from public quasi-corporations are recorded as withdrawals from equity, recognising that the payment is not made from current entrepreneurial income but from accumulated reserves or sales of assets. It is recommended that the treatment of exceptional payments from public corporations should be changed and also recorded as withdrawals from equity because these also must be made from accumulated reserves or sales of assets. Therefore, only regular distributions from the entrepreneurial income of corporations are to be recorded as dividends.

In the 1993 SNA, exceptional payments from government to public corporations are recorded as capital transfers. By contrast, exceptional payments from government to public quasi-corporations are recorded as additions to equity. It is recommended that in the updated SNA, such payments should be treated as capital transfers for both public corporations and quasi-corporations.

Exceptional payments made by government units to public corporations and quasi-corporations are most frequently intended to cover accumulated losses and should be recorded as a capital transfer since the characterisation of payments to corporations making regular losses as additions to equity is inappropriate. However, to the extent that the government is acting in the same way as a private shareholder in a commercial context, that is, it has a valid expectation of a return in the form of a property income, the payment should be recorded for both types of corporation as additions to equity.

The option to follow the same principle for public bodies as for non-resident units in recording reinvested earnings exactly matching current entrepreneurial income is not being proposed for adoption at the present time but is recommended as an item for the research agenda.

AEG papers:	SNA/M1.05/29	Government transactions with public corporations: Super-dividends, capital injections, reinvested earnings
	SNA/M1.06/16	Government dividends and capital transactions with public corporations in the updated SNA

35	<p>Tax revenues, uncollectible taxes and tax credits</p> <p>(a) <i>Definition and coverage of taxes</i></p> <p>Is it necessary to clarify the definition of taxes in the 1993 SNA and the distinction between the payment of taxes and payments for services?</p> <p>(b) <i>Accrual recording of taxes</i></p> <p>The 1993 SNA describes the conceptual basis on which taxes should be assessed as accruing. Some practical flexibility is allowed in order to ensure that uncollectible taxes are not shown as accruing. Should greater precision be given about the degree of flexibility that is acceptable in relation to (i) the time when accrual is deemed to take place and (ii) the amounts to be shown as accruing?</p> <p>(c) <i>Tax credits</i></p> <p>The 1993 SNA does not give guidance on the treatment of tax credits although the <i>Government Finance Statistics Manual</i> does. In order to correct this omission, a choice has to be made between recording these as a reduction in government tax receipts and recording some or all as government expenditure. Which alternative should the SNA adopt?</p>
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Definition and coverage of taxes

Taxes are usually described as unrequited because, in most cases, the government provides nothing directly in exchange to the individual unit making the payment or nothing commensurate. However, there are cases where the government provides something to the individual unit against the payment in the form of the direct granting of a permit or authorisation. An issue of concern is how to treat payments to government for permission to use certain natural assets or to undertake certain activities when the number of permits is limited and the fees are much higher than the administrative cost of issuing the permits.

The outcome of this part of the discussion under Contracts, Leases and Licences was as follows:

Government permits to undertake specific activities, even when these are limited in number and may be competed for by auction or similar competitive application, are to be recorded as taxes. If the permit covers multiple periods, the tax should be recorded on an accrual basis if government has an obligation to refund the value of the unused part in the case of a revocation or surrender. If government has no such obligation, the whole of the payment is recorded as a tax when paid. In addition the acquisition of an asset is recorded. As with transferable contracts just described, whether or not an asset is recorded in respect of a permit, if the initial holder of the permit can legally and practically sell the permit than its current value, this is also regarded as an asset.

Accrual recording of taxes

In general taxes are to be recorded as accruing when the taxable event to which the tax relates occurs. Some flexibility is allowed in two cases. One of these relates to taxes on income and provides for the time of recording to be when the tax liability is assessed with some measure of certainty. The other refers to taxes arising from activities in the “parallel” economy when the timing of the taxable event is unlikely to be known. In this case also the time of recording will be the time of assessment.

In assessing the amount of taxes accruing, care must be taken not to include tax unlikely ever to be collected. Three methods of ensuring this is not so are recommended. The first method is the “time-adjusted cash basis” under which the amounts are initially recorded when paid and then adjusted to the time the liability to pay tax was incurred. The other two methods assess from the outset the amounts likely to be collected. The second method (net recording of taxes) adjusts the initial estimate of tax accruing by a coefficient reflecting the degree of non-collection in the recent past. The third method (gross recording of taxes) records realistic estimates of total taxes accruing but records the difference between the accruals estimate and actual receipts as a capital transfer in favour of the defaulting payers.

Tax credits

Some subsidies or social benefits are made available via the tax system in the form of tax credits, and the incidence of linking payment systems with the tax collection system is increasing. Tax credits represent tax relief and so reduce the tax liability of the beneficiary. If the relief is greater than the liability, and the beneficiary actually receives the excess, these are described as payable (sometimes non-wasteable) tax credits. It is recommended that the whole amount of the payable tax credit be recorded as government expenditure as well as noting the amount of the payable tax credit drawn back in tax paid. This would then allow comparison to be made with presentations on a net basis, where only the excess of the payable tax credit over the tax liability is shown.

AEG papers: SNA/M1.05/07 Taxes, revenues, uncollectible taxes and tax credits

36	<p>Public/private/government sectors delineation</p> <p>According to the 1993 SNA, two factors determine whether a corporation or non-profit institution is controlled by government and thus falls into the public sector. One factor is the degree of control exercised by government. Concern has been expressed about the “mainly financed” phrase cited in respect of non-profit institutions. The determination of control in respect of special purpose vehicles (SPVs), notably created in the context of public private partnerships (PPPs) or securitization, is not always clear cut. The second factor is about “economically significant prices.” Concern has also been expressed over possible ambiguity in this concept. Is it possible to give greater content to the description without going so far as to prescribe a fixed proportion of costs to be covered by sales?</p>
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To further clarify the delineation between government and private control of units in the economy, the Task Force on the Harmonisation of the Public Sector Accounts has developed extended guidelines amplify the meaning of “control” and “economically significant prices”. For control, a set of eight indicators useful for corporations and a set of five for non-profit institutions are put forward. None of these indicators is determining of control taken in isolation and not all the indicators have to be satisfied but together they give an enhanced view of what is meant by control. There are some general guidelines given on “economically significant prices” and some more detailed guidance on when a unit supplying products to government should be regarded as a market producer.

A decision tree showing the delineation between the government, public and private sectors will be included in the updated text.

It is proposed that these details be added to the SNA text. (They are available in detail in the AEG paper SNA/M1.06/17)

AEG papers:	SNA/M1.05/09.1 SNA/M1.06/17	Public/private/government sectors delineation Government/public sector/private sector delineation issues
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37	<p>Granting and activation of loan guarantees</p> <p>Loan guarantees have a significant impact on economic behaviour, especially when issued by government. The 1993 SNA treats guarantees as contingent liabilities and thus has no record of the existence of the guarantee until it is activated. Further, the treatment of flows arising at the activation is not explicit. Should obligations arising from guarantees be recognized when guarantees are granted, particularly regarding those guarantees for which it is possible to make reasonable estimates of expected future claims?</p>
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It is proposed that three classes of guarantees be recognized.

The first of these is composed of those guarantees provided by means of a financial derivative, such as a credit default swap. These derivatives are actively traded on financial market. The derivative is based on the risk of default of a reference instrument and so not actually linked to an individual loan or bond. Incorporating the transactions connected with establishing this sort of financial derivative presents no new features for the SNA.

The second class of guarantees, standardized guarantees, is composed of the sorts of guarantees that are issued in large numbers, usually for fairly small amounts, along identical lines. There are three parties involved in these arrangements; the borrower, the lender and the guarantor. Either the borrower or lender may contract with the guarantor to repay the lender if the borrower defaults. The classic examples are export credit guarantees and student loan guarantees. Here, although it is not possible to establish the likelihood of any one loan defaulting, it is not only possible but standard practice to estimate how many out of a batch of similar loans will default. If the guarantor is working on purely commercial lines, he will expect all the fees paid, plus the property income earned on the fees, to cover the expected defaults. This is exactly the same paradigm as operates for non-life insurance and it is proposed that a similar treatment be adopted for these guarantees, to be described as “standardized guarantees”. This will involve including transactions and balance sheet items parallel to those for non-life insurance, including the generation of output and payments of a fee supplement and a service fee by those taking out the guarantees. If the guarantor is part of general government and deliberately sets the fees below the level of expected defaults, a subsidy is to be imputed to the guarantee holders.

The third class of guarantees, described as one-off guarantees, consists of those where the loan or the security is so particular that it is not possible for the degree of risk associated with the loan to be calculated with any degree of accuracy. In most cases, the granting of a one-off guarantee is considered a contingency and is not recorded as a financial asset/liability. (As an exception, one-off guarantees granted by governments to corporations in certain well-defined financially distressed situations and with a very high likelihood to be called might be treated as if these guarantees were called at inception.) Otherwise, no change is proposed for recording these in the accounts. If a fee is charged, this is recorded as a payment of a service at the time of payment. If a call is made under a guarantee, a capital transfer is recorded from the guarantor to the guarantee holder at the time of default or, in cases where the guarantor obtains an effective claim on the guarantee holder, a financial transaction (including increases in equity participation).

AEG papers:	SNA/M1.05/08	Granting of guarantees
	SNA/M1.06/18	Granting and activation of guarantees in an updated SNA
Follow-up papers:	SNA/M2.04/25	Treatment of activation of guarantees
	SNA/F1.06/10	Questionnaire for consultation by the AEG
	SNA/F1.06/11	Outcome of the AEG consultation

38a	<p>Change of economic ownership (as term)</p> <p>The principle of ownership is central to the determination of the timing of recording of transactions in financial and non-financial assets (including transaction in goods). However, the 1993 SNA does not explicitly define ownership. Does the term “economic ownership” better reflect the underlying economic reality by reflecting risks and rewards of ownership? Should the SNA draw a distinction between legal, physical, and economic ownership?</p>
38b	<p>Assets, liabilities and personal effects of individuals changing residence (“migrant transfers”)</p> <p>The flows of goods and changes in the financial account arising from a change in residence of individuals are treated as imputed transactions in the <i>Balance of Payments Manual</i>. These flows are offset in the capital account by capital transfers called migrants’ transfers. The 1993 SNA is not explicit on the treatment of these flows. Since no change in ownership occur. Should the changes in financial claims and liabilities due to change in residence of individuals be treated as reclassification in other changes in volume account?</p>
38c	<p>Application of accrual principles to debt in arrears</p> <p><i>This item is described and dealt with in conjunction with issue 4, Non-performing loans</i></p>

Concepts of ownership

The updated SNA is to give guidance on the difference between legal ownership and economic ownership and recommend that assets be recorded on the balance sheets of the economic rather than the legal owner. For a non-financial asset, the user and not the legal owner may assume economic ownership if the legal owner agrees that the user is entitled to the benefits deriving from using the asset in production in return for assuming the risks involved. Similarly when products change hands, it is the unit who assumes the risks in the case of destruction, theft, etc. who is the economic owner. Ownership is also associated with assuming risk in the case of financial assets. Physical custody alone is seldom if ever a sufficient criterion for attributing ownership in the SNA. When the time of recording depends on change of ownership, it is in general the change of economic ownership that is intended but this is to be clarified in a case-by-case basis.

For some non-financial assets and some financial assets, some of the benefits may be shared between two or more units. In most cases, the ownership of the whole asset will be recorded on the balance sheet of one of the parties with a financial lease conveying benefits to the others. However, there are some cases where this is not a satisfactory solution (for example with unincorporated joint ventures) and these will be described on a case-by-case basis.

Individuals changing residence

The updates to the SNA and to the BPM will confirm that when an individual changes his country of residence, there is no change of ownership of the non-financial assets, and financial assets and liabilities owned by that person. All that is required is a reclassification of the appropriate country of residence of the (economic) owner of these items. As such, it is more appropriate that the changes be recorded in the other changes in the volume of assets account than as capital transfers. Consumer durables appear only as a memorandum item in the balance sheets. They may feature as a memorandum item in the other change in volume of assets account but should not appear as trade in goods.

AEG papers:	SNA/M1.05/13.1	Migrants' transfers
	SNA/M1.05/13.2	Migrants' transfers - Report on e-discussion
	SNA/M2.04/18	"Change of economic ownership" as term

39a	<p>Meaning of national economy</p> <p>In the 1993 SNA, the concept of the national economy is discussed in terms of “economic territory of a country” for which two contradicting criteria are used: “administered by a government” and “free circulation of persons, goods and capital”. The criteria need to be clarified. Clarification is also needed between domestic and national economy.</p>
39b	<p>Predominant center of economic interest (as term)</p> <p>With globalization, there are an increasing number of institutional units with connections to two or more economies. The concept of “predominant” center of economic interest has been put forward to address this issue.</p>
39c	<p>Residence of entities with little or no physical presence</p> <p>For enterprises and other entities with little or no physical presence, the criteria of production and location that are used in the 1993 SNA to help determine residence are not very relevant. Should the jurisdiction that allows the creation of and regulates the entity be considered as the determining the entity’s predominant centre of interest?</p>
39d	<p>Non-permanent workers</p> <p>The number of non-permanent workers with connections to two or more territories has grown substantially in recent years. Would it be useful to prepare supplementary presentations for countries where the number of non-permanent resident persons is significant, bringing together relevant components of contract services, compensation of employees, workers’ remittances and migrants’ transfers with the numbers of short-term non-resident workers? Can the residence concept be more closely harmonized with demographic, tourism, and migration statistics and any remaining differences spelt out?</p>

National economy

It is agreed that greater precision is needed for the definition of “national economy” and care taken in the use of the word ‘domestic, especially given the time-sanctioned use of gross domestic product as a measure of activity within the national economy.

Predominant centre of economic interest

In order to associate only one economy with a unit (or individual) that has connections with two or more economies, it is agreed to identify the most significant of these connections and to refer to this as the country where there is a predominant centre of economic interest.

Entities with little or no physical presence

Consistent with the recommendations under issue 25d, it is accepted that a unit may be established in an economy even though it may have little if any physical presence.

Non-permanent workers

There is growing analytical interest in the number of people resident in one economy and working in another or having strong association with a country other than that of their current residence. In

order to meet this interest, changes are proposed to the way transfers affecting households are to be shown in the BPM and the SNA.

A new term of “personal transfers” will be introduced. The previous item of “workers’ remittances” will be part of this and may be shown as an “of which” item to preserve continuity with past data series. Personal transfers will cover all transfers between resident and non-resident households whether or not the source of the transfer was income from employment and whether or not individuals in the sending and receiving households were related.

A term “personal remittances” will be introduced as a supplementary item consisting on the receipts side, of personal transfers, as just defined, plus compensation of employees earned abroad, less expenditure abroad by those employees.

“Total remittances” will consist of personal remittances plus social benefits including private pensions received from abroad.

A final term, “total remittances plus transfers to NPISHs” will consist of total remittances plus funds and resources provided from abroad to local NPISHs.

Two other cases relating to residence have been clarified. One of these was to confirm that the present exceptions to the residence of individuals in the case of ships’ crews, students and patients. Students and patients remain residents of their home country regardless of the length of study or treatment (respectively). Ships’ crews are resident in the country where they spend most time other than on board ship.

The other case related to the “migration “ of a company. Usually, what appears to be a migration is in reality either a transaction between two enterprises or disinvestment and exports from one country and imports and capital formation in another. However, there is provision under EU law for a company to migrate and the SNA and BPM must make clear the circumstances under which this is possible.

AEG papers:	SNA/M1.05/15.1	Residence of households: Non-permanent workers
	SNA/M1.05/15.2	Residence of households: Non-permanent workers - Report on e-discussion
	SNA/M1.05/15.3	Residence of households: Ships' crew and patients
	SNA/M1.05/15.4	Residence of households: Ships' crew and patients - Report on e-discussion
	SNA/M2.04/20	"Predominant center of economic interest" as term

40	<p>Goods for Processing</p> <p>The 1993 SNA and the <i>Balance of Payments Manual</i> treat the goods sent abroad for processing differently. The 1993 SNA only records gross flows in the case of substantial processing (reclassification of the good at three-digit CPC). The <i>Balance of Payments Manual</i>, as a practical matter, suggests a convention that all processing be assumed substantial and therefore gross flows are recorded. Can a distinction be made between the different levels of processing? Further, the position is that when goods are sent abroad for processing, no change in ownership takes place and thus there are no actual transactions. It is mentioned that the current treatment of goods for processing in the 1993 SNA was to facilitate input-output analysis. Is this still a valid reason to record goods for processing on a gross basis or does the advent of globalization and the increasing amount of goods processed abroad suggest a change in practice would be appropriate?</p>
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The recommendations on goods for processing in the 1993 SNA and in BPM5 are complex and not well understood. This is demonstrated in the form the question was posed in the description of the issue. During investigation of the issue, it proved that the fundamental question to be addressed was not the degree of processing involved but whether recording of imports and exports should follow a change of ownership recording or that of physical movement. The recommendation is for the former, that is for recording on a change of ownership basis. This is a change from the 1993 SNA, affecting the recording of transactions within the national economy as well as international transactions. This has implications for the input-output tables, which on the proposed basis will reflect the economic basis of production (what does each unit contribute to the production process) rather than the physical technology as heretofore.

This recommendation and that on merchanting (issue 41) recognise that many goods move from one country to another without entailing a consequential payment from the recipient country to the sending country. For economic analysis, the financial consequences take precedence over the physical movements, though it is recognised that there may be some interest in this also. For this reason, and to assist in controlling the accuracy of data available for a range of statistics, the recommendations have implications for the way in which the physical movement of goods, captured in merchandise trade statistics, is reconciled with the international flows to be recorded in the BOP and SNA. This is being addressed in conjunction with trade statisticians.

AEG papers:	SNA/M1.05/16	Goods sent abroad for processing
	SNA/M2.04/24	Goods sent abroad for processing

Please note: this was the recommendation of the AEG. For later developments, please refer to the main report E/CN.3/2007/7

41	<p>Merchandising</p> <p>Merchandising is defined in the <i>Balance of Payments Manual</i> as the purchase of a good by a resident (of the compiling economy) from a non-resident and the subsequent resale of the good to another non-resident, without the good entering the merchant's economy. The SNA does not cover the topic. The existing definition of merchandising may capture activity that is part of the production process in an increasingly globalized and inter-connected world, which is not the intent behind the definition of merchandising activity. Therefore, there is a need for a clear and precise definition of merchandising; arising out of this there needs to be clear guidance on whether merchandising (when redefined) should be recorded on a net or a gross basis and under goods or services.</p>
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Merchandising does not appear by name in the text of the SNA; there is one passing reference to it in the chapter on the rest of the world account. This activity is of increasing importance and comprehensive guidance should be included in 1993 SNA Rev 1. The activities concerned are global manufacturing, global wholesaling and retailing and commodity dealing. Most commodity dealing is undertaken by means of transactions in financial derivatives. Only when actual settlement in terms of the nominated commodity takes place would transactions considered here take place.

The case is the reverse one to that of goods for processing; there is a change of ownership and consequences for financial flows but the goods purchased do not enter the country where the purchaser is resident. Including all goods bought and sold by retailers and wholesalers (or by manufacturers) in both imports and exports would inflate those figures by including goods never present in the economy. It is recommended, therefore, that goods acquired by global manufactures, wholesalers and retailers and those cases of commodity dealing being settled in the commodity should be recorded as negative exports on acquisition and positive exports on disposal. The difference between the two appears in exports of goods (consistent with the goal of a zero global balance on goods) but appears as the production of a service in the merchant's economy, consistent with margins applied to domestically produced goods. In the case where goods are acquired in one period and not disposed of until a subsequent period, they will appear in changes in inventories of the merchant even though these inventories are held abroad.

The same requirement for improved recording of merchandise trade applies to merchandising as applies to goods for processing.

AEG papers:	SNA/M1.05/14	Merchandising
	SNA/M1.06/19	Merchandising

42	<p>Retained earnings of mutual funds, insurance companies and pension funds</p> <p>In the 1993 SNA, retained earnings of an entity are generally treated as the income and saving of the entity, rather than the owner. However, exceptions are made for life insurance companies, pension funds and foreign direct investment companies, where there is an imputed outflow to the policyholders, beneficiaries, or owners (respectively), with an equal financial account inflow from them. The <i>ESA 95</i> introduces a similar treatment for mutual funds by imputing a distribution of retained earnings to the investors and a subsequent reinvestment in the fund. Should the SNA follow this treatment to have a more consistent treatment of various forms of collective investment schemes?</p>
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It is recommended that the SNA adopt the concept of an “investment fund”, which would include mutual funds and money market funds but not pension funds. For investment funds there would be a distribution of property income to the shareholders in the fund with subsequent reinvestment in the fund. New categories of property income payable and receivable would be introduced, distinguishing dividends distributed to, and retained earnings attributed to, investment fund shareholders. In addition, a new financial asset category, “investment fund shares” will be introduced and will cover the reinvestment of the distributed income (as well as purchases and sales of mutual fund shares).

As a follow up to this item, a separate consultation took place to decide how far redistributed property income may include holding gains and losses. Although the SNA excludes this from production, payments of interest and dividends are recorded as stated by the paying institutions even though the source of some of the items may be holding gains. Further, when the amount accruing to pension fund liabilities due to the fact that retirement is one year nearer is estimated on the basis of a rate of return times the liability outstanding at the beginning of the year (the actuarial basis) the source of this income is again irrelevant. It is recommended that when the amount distributed is known to the recipient, for example because it is determined by application of an agreed formula or if the recipient is notified of the amount of the distribution, this is to be recorded as property income regardless of the source of financing.

AEG papers:	SNA/M1.05/17.1	Retained earnings on mutual funds and other collective investment schemes
	SNA/M1.05/17.2	Retained earnings on mutual funds and other collective investment schemes
	SNA/M1.06/29.1	Retained earnings on mutual funds, insurance corporations and pension funds
	SNA/M1.06/29.2	Retained earnings on mutual funds, insurance corporations and pension funds - Report on e-discussion

43a	<p>Treatment of index-linked debt instruments</p> <p>The guidance in the 1993 SNA about how transactions relating to index-linked debt instrument are recorded is not precise. When the principal is indexed, the redemption value is not known until maturity; as a result, interest flows are not known before maturity. What should be recorded for interest and principal repayment in the period before maturity? Further, for some instruments, the indexation may lead to valuation gains. How should these be recorded?</p>
43b	<p>Debt indexed to a foreign currency</p> <p>For debt instruments with both principal and coupons indexed to a foreign currency, the currency of account is important for distinguishing transactions from holding gains and losses. The results may be different from an assessment made on the basis of the currency of settlement. Does this mean that debt indexed to foreign currency should be treated in the same way as foreign currency debt, that is as if denominated in foreign currency?</p>
43c	<p>Interest at concessional rates</p> <p>Loans with concessional interest rates could be seen as providing a transfer from lender to borrower. Should such transfers be recognized in the SNA? Although there is no clear definition of what is a concessional loan, the guidance in the <i>External Debt Guide</i> suggests features such as an intention to convey a benefit and occurrence in a non-commercial setting (usually government-to-government). If concessional loans are not recognized in the core accounts, should the concessional amounts be considered as supplementary information where they are significant?</p>
43d	<p>Fees payable on securities lending and gold loans</p> <p>Neither the 1993 SNA nor the <i>Balance of Payments Manual</i> discusses the issue of fees payable on securities lending and gold loans. The fee for securities lending is for putting a financial instrument at the disposal of another unit, but it does not fit with the definition of interest when the legal ownership is transferred but the economic risks and rewards of the ownership remain with the original owner. The fee payable on gold loans appears to be a payment for services as gold in this instance is non-monetary gold.</p>

Index linked debt instruments

The guidance in the 1993 SNA is that interest on a loan where the principal is index-linked, is determined as the difference between the eventual redemption price and the issue price. Because the final redemption price is not known before redemption, the amount of interest payable in a year can only be approximated until redemption. For an instrument indexed to a broad-based measure of inflation such as the CPI, this presents little difficulty but instruments linked to volatile indices such as commodity prices or a stock market index present serious problems.

If no revisions to prior years are accepted, the path of interest payables can be highly volatile and even include negative amounts. Revising the path of interest payable for every year to date throughout the life of the instrument or making a single set of revisions at redemption date give very different paths of interest payments though the total over the life of the instrument is the same in both cases.

It is recommended that the principle underlying the calculation of interest in the case where an instrument is linked to a potentially volatile index should be changed. In this case, the amount of interest due each period should be calculated by reference to the expected redemption value of the

instrument and not subsequently revised. At redemption, the sum of interest recorded over the life of the instrument will not necessarily be equal to the redemption value less the issue value. Any difference will be recorded as a holding gain or loss. This treatment was held to be preferable to the alternative.

For an instrument indexed to a broad-based index, the interest due each period should be calculated by reference to the movement of the index to date. This series would not be subject to revision due to subsequent movements in the index.

Debt indexed to a foreign currency

When a debt instrument has both the principal and coupons indexed to a foreign currency, the debt instrument transactions relating to both principal and coupon should be calculated by reference to the foreign currency, even if the currency of settlement is different. However, these debt instruments do not necessarily constitute foreign debt just because they are denominated in a foreign currency. It is important distinguish clearly between the currency of account and of settlement.

Interest at concessional rates

The question of how to recognize the consequences of concessional debt is very important, especially for developing countries. However, the means of incorporating the impacts within the SNA are still not agreed, although several suggestions have been advanced. Most of these involve some degree of variation from the normal SNA rules. The recommendation is that this item be added to the research agenda and pending resolution the impacts of concessional loans should be shown in supplementary tables.

Fees payable on securities lending and gold loans

It is proposed that all fees payable to the owners of securities used for securities lending and to the owners of gold used for gold loans (whether from allocated or non-allocated gold accounts) be recorded by convention as interest.

AEG papers:	SNA/M1.05/11.1	Interest on index-linked debt instruments
	SNA/M1.05/11.2	Debt instruments linked to a foreign currency
	SNA/M1.05/12	Fees on securities lending and reversible gold transactions
	SNA/M1.06/20	Debt Concessional
	SNA/M1.06/35	Debt reorganization
	SNA/M2.04/27	Treatment of debt instruments linked to foreign currency

44	<p>Financial assets classifications</p> <p>Continued innovation in financial markets since the 1993 SNA was written means a review of the classification used for financial instruments is appropriate. Suggestions for change arise for most of the present categories.</p> <p><i>Monetary gold and SDRs</i></p> <p>(a) Should monetary gold be treated as a financial asset rather than as a valuable?</p> <p>(b) The 1993 SNA classifies Special Drawing Rights (SDRs) as assets without corresponding liabilities arguing that IMF members do not have an unconditional liability to repay their SDR allocations. However, SDR allocations have attributes of liabilities because interest is payable on them and a country terminating IMF membership would be required to repay its obligations including any SDR allocations. Also, the IMF <i>Monetary and Financial Statistics Manual</i> recommends that the value of allocated SDRs be shown both on the assets and liabilities side of the balance sheets of central banks, which is in accordance with the IMF's SDR Department's guidance to member countries. Should SDR allocations be considered liabilities in the SNA?</p> <p><i>Deposits and loans</i></p> <p>(c) The criteria to make the distinction between deposits and loans are not clear. Recent financial innovations raise questions about the continuing analytical usefulness of the distinction. A particular problem is when a position between two parties, especially financial institutions, is seen as a deposit by one party and a loan by the other. Should the SNA maintain a distinction between loans and deposits?</p> <p>(d) When and under what circumstances do loans that are traded become securities? This is important because virtually all loans are tradable and trading has increased. It also affects market valuation since securities are valued at market price in the SNA and loans at nominal values.</p> <p><i>Securities other than shares</i></p> <p>(e) With financial derivatives treated as a separate instrument in the 1993 SNA, it would be appropriate to introduce the term "debt securities" to replace "securities other than shares".</p> <p><i>Financial derivatives</i></p> <p>(f) Should there be a distinction between different types of financial derivatives, for example between forwards and options as well as the inclusion of employee stock options (see issue 3) in this category?</p>
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Monetary gold and SDRs

It is proposed to treat SDRs as being a liability of countries receiving the allocations and to record allocation and cancellation of SDRs as transactions. The asset and liability aspects of SDRs will be recorded separately.

As a result of the changed treatment of SDRs, it is proposed to show monetary gold and SDRS as separate sub-items under the previous combined heading

Other gold as a financial asset

Enquiries have revealed a difference in accounting for “allocated gold accounts” and “unallocated gold accounts” and similar distinctions for other precious metals. An allocated gold account gives the holder outright ownership of identifiable physical gold and is equivalent to a custody record of title. An unallocated gold accounts provides a claim by the holder against the account provider which is denominated in gold. In effect, the account is denominated in gold. It is proposed that unallocated gold accounts should be treated as financial assets and liabilities and classified with deposits in foreign currency. Allocated gold accounts would continue to be treated as valuables or inventories as at present. Unallocated accounts in other precious metals should be treated similarly to unallocated gold. If the treatment extends to other commodities, a review would be necessary to consider if the treatment should be extended further.

Deposits and loans

The distinction between deposits and loans will be maintained. In a full “from whom to whom” analysis of the holdings of loans and deposits, there should be no problem in distinguishing loans from deposits. However, when this full detail is not available, it may not always be possible to identify loans from deposits when both parties to the transaction are banks. Therefore it is proposed to introduce a category “interbank deposits” to covert this ambiguity.

It is not proposed to change the guidance on traded loans. A loan should be reclassified as a security only if there is evidence of a market for the loan and market quotations are available. A one-off sale of a loan does not make it a security. No separation of loans into traded and non-traded categories is proposed.

Securities other than shares

It is proposed to change the terminology of this item to “debt securities”.

Financial derivatives

It is proposed to make a distinction between options and forwards and to show employee stock options separately (see issue 3). Further breakdowns might be presented at the discretion of an individual country but the SNA will not suggest any further breakdown either as standard or supplementary items.

Further consequences for the classification of financial assets

Discussions of other items have consequences for the classification of financial asset. Arising from issue 42 on the treatment of mutual funds, it is proposed to change the heading and breakdown of equity to show investment funds shares separately and within investment funds to show money market funds separately.

It is proposed to change from the use of “quoted” shares to “listed” shares.

The consequence of issue 37 on guarantees is to introduce more detail in to the category on insurance technical reserves and under issue 5 a change in terminology was proposed regarding the use of the term “provision”.

Taken together, the present proposals for the classification of financial instrument are as in the following table.

Financial assets and liabilities

Monetary gold and SDRs

Monetary gold

SDRs

Currency and deposits

Currency

Transferable deposits

Interbank positions

Other transferable deposits

Other deposits

Debt securities

Short-term

Long-term

Loans

Short-term

Long-term

Equity and investment fund shares

Equity

Listed shares

Unlisted shares

Other equity

Investment fund shares/units

Money market fund share/.units

Other investment fund share\units

Insurance, pension and standardised guarantee schemes

Non-life insurance technical provisions

Life insurance and annuity entitlements

Pension entitlements

Provisions for calls under standardised guarantees

Financial derivatives and employee stock options

Financial derivatives

Options

Forwards

Employee stock options

Other accounts receivable/payable

Trade credit and advances

Other accounts receivable/payable

Memorandum items: Direct foreign investment

Equity

Loans

Debt securities

Trade credit

Other

AEG papers:	SNA/M1.05/10.1	Classification of financial instruments
	SNA/M1.05/10.2	Distinction between loans and deposits
	SNA/M1.05/10.3	Traded loans (Borderline between securities and other financial instruments)
	SNA/M1.06/21	Classification and terminology of financial assets and liabilities in the updated SNA
	SNA/M1.06/22	Liability Aspects of SDRs
	SNA/M1.06/30.1	Non-monetary gold
	SNA/M1.06/30.2	Non-monetary gold - Report on e-discussion
Follow-up papers:	SNA/M1.06/36	International reserves
	SNA/F1.06/8	Questionnaire for the world-wide consultation carried out by the ECB's Directorate General Statistics
	SNA/F1.06/9	Consideration by the ISWGNA

Postscript: Clarification items having implications for the existing SNA

As mentioned above, five items raised as clarifications have implications for the existing text of the SNA. These five are:

1. the most aggregate level of ISIC to be used in the SNA;
2. clarification with the ILO on labour inputs;
3. clarifications with alternative financial account systems on the sub-sectors to be shown for the financial sector;
4. more flexibility on the valuation of equity, and
5. incorporation of some of the proposals put forward in the Atkinson report on the measurement of non-market output.

Each of these is discussed in turn below.

The most aggregate level of ISIC (Rev 4) to be used in the SNA

A revised version of ISIC, revision 4, was adopted by the Statistical Commission in 2006. A number of ISIC headings are used in the SNA, especially in the context of supply and use and input-output tables. In order to have a standard set of headings available for these tables, consistent with ISIC (rev 4), new aggregations levels have been agreed with the classifications experts. The section headings have been further aggregated to 10/11 headings (ten are pure aggregations; the eleventh covers manufacturing). The divisions have been aggregated to 38 headings.

Clarification with the ILO on hours worked and employment

In 1962, the international conference of labour statisticians (ICLS) passed a resolution on hours worked. Consultations in progress are expected to lead to a proposed revision to this resolution in 2008. The changes to be proposed concern the definition of hours worked and improved methods for measurement in the light of the increased incidence of alternative working time arrangements. On the basis of these consultations, it is proposed to make some small modifications to the relevant sections of the chapter on population and labour force to maintain consistency with ILO concepts.

Harmonisation with alternative financial account systems of the sub-sectors to be shown for the financial sector

The sub-sectors of the financial sector of the SNA are introduced only in the context of compiling flow of funds accounts. These accounts provide the link to the monetary and financial statistics system of the IMF and the corresponding system of the ECB. However, neither of these systems uses exactly the same breakdown as that shown in the SNA. In consultation with the staff responsible for these systems, it is proposed to introduce slightly more detail in the SNA to allow more flexible cross-walks to these alternative systems.

Two follow up papers are available on this subject; SNA/F1.06/04 and SNA/F1.06/07.

More flexibility on the valuation of equity

Not all equity is listed and quoted on stock exchanges. The SNA gives rather restricted advice on how to value unlisted equity. Financial statisticians have, since 1993, developed alternative measures of valuation that produce more realistic estimates in some circumstances. It is proposed that these extra options be added to the SNA recommendations.

Incorporation of some of the proposals put forward in the Atkinson report on the measurement of non-market output.

The question of how to measure productivity in government is one of great interest at present. A recent report by Sir Tony Atkinson for the United Kingdom's National Statistics Office addressed in some detail how more satisfactory measurement of the output of the non-market services of government might be achieved. Some of these suggestions are still undergoing trials but in recognition of the initiative in this area, it is proposed that the section in the SNA on the measurement of the volume of non-market output include references to this report and the follow up work.