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13th Meeting of the Advisory Expert Group on National Accounts,
1-3 October 2019, Washington D.C., USA

Agenda item: 2.2.1

Task Force on the SNA Research Agenda: subgroup on globalization
Issue note on the valuation of imports and exports of goods

<u>Introduction</u>

The guidance on how to value international transactions in goods and treat related transportation and insurance services (i.e CIF/FOB adjustment) has been discussed at the Advisory Expert Group (AEG) on national accounts meetings in 2013 and in 2017. The issue has been put forward by the AEG as a first priority of research in the Task Force on the SNA Research Agenda subgroup on globalization. The attached issue paper authored by Saturo Hagino (Fukuyama University, Japan), member of the subgroup provides an overview of the topic including various options for the valuation of imports and exports. The first draft of the issue paper has not yet benefited from discussion inputs from the entire subgroup. It is now being circulated to the subgroup for consultation.

A paper on: Valuation of imports and exports of goods

<u>Main issues to be discussed</u>

The AEG is invited:

- Express views regarding the options put forward in the issue note.
- Are there any additional options that should be considered by the subgroup that are not addressed in the note?
- Provide input into current country practices with regards to the recording of imports and exports in their country's national accounts.

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Introduction by the co-chairs and secretariat

At the end of 2011, Anne Harrison, Editor of the *2008 System of National Accounts* (2008 SNA) brought to the attention inconsistencies in guidance on how to measure international trade in goods between national and international economic accounts. The issue was first discussed in a 2012 Committee on Balance of Payments Statistics (BOPCOM) paper. At that time, the IMF Statistics Department did not favor introducing any changes to the *Balance of Payments and International Investment Position Manual, 6th edition* (BPM6) to address this apparent inconsistency given that the treatment in the balance of payments is long-established.

The issue was then deferred for clarification by the Intersecretariat Working Group on National Accounts (ISWGNA) and its Advisory Expert Group (AEG). The conclusions of the 2013 AEG meeting, recognized that while both 2008 SNA and *BPM6* recommend recording the imports and exports of goods at free-on-board (FOB) values, the 2008 SNA does not fully reconcile the FOB valuation principle with the principle of output valuation at basic prices. It, therefore, recommended that in the longer term, the agreed change of ownership principle for cross-border transactions should be applied consistently across the SNA, BPM, and International Merchandise Trade Statistics (IMTS).

The issue has recently appeared again in various fora, in particular on the proposal to use the transaction price (i.e. invoice values) by Statistics Netherlands and Germany's Bundesbank. Haan and Hiemstra, Statistics Netherlands, presented a paper at the 2017 AEG. The conclusions of the 2017 AEG meeting recognized that the use of transaction prices for exports and imports of goods is not consistent with the current SNA recommendations, but recommended an assessment of country experiences in CIF/FOB recording by the ISWGNA and to develop a guidance note as part of the research agenda on globalization.

Hence, as part of the Task Force on the SNA Research Agenda, this issue was considered a first priority by the subgroup on globalization. The following issue paper, authored by Saturo Hagino (Fukuyama University, Japan), member of the subgroup provides an overview of the topic including the various options for the valuation of imports and exports. This first draft of the issue paper has not yet benefitted from discussion inputs of the entire subgroup on globalization. It is now being circulated to the subgroup for consultation.

Issue paper on CIF-FOB valuation of imports/exports

By Saturo Hagino, Fukuyama University, Japan

1. Introduction to the issue

The guidance on how to valuate international transactions in goods and treat related transportation and insurance services differs between the national accounts and BOP. Within the national accounts, a variety of different bases are acceptable, depending on agreements reached between individual buyers and sellers, whereas in the BOP, FOB is the uniform valuation basis and the CIF/FOB adjustment is recommended.

This issue cropped up in 1996 in the context of EU trade asymmetries and a technical group was established within the EU to propose a uniform method for estimating merchandise transport. The first report presented in 1999 proposed an invoice approach, i.e. a valuation method based on actually observed transaction values for international transactions of goods and related transportation services. However, this approach was not further pursued due to the inconsistency with the BPM5 recommendations. Recently, Haan and Hiemstra (2018), Dutch national accountants, as well as Walter (2018), German BOP compiler took up this approach in various fora, including the AEG in 2017 and OECD Working Parties in 2018, insisting that the current CIF/FOB recording of merchandise imports and exports in the BOP contrasts economic reality and causes trade asymmetries.

Anne Harrison, editor of 2008 SNA, raised this issue at the 2012 IMF Committee on Balance of Payments Statistics meeting held in 2013. At that time, IMF Statistics Department did not favor introducing any changes to BPM6 to address this apparent inconsistency for the reason that the treatment in the balance of payments is long-established. Thus, this issue remains to be thoroughly discussed by the Committee members.

Nevertheless, the analysis of Anne Harrison revealed two remarkable points. First, the ratios of freight debits to imports FOB are quite stable, which suggests that the CIF/FOB adjustment is based on long-established proportions. Second, the ratio of recorded freight debits to freight credits averages about 140 percent a year over the 17 years and the 40 percent excess represents about one percent of imports FOB. Thus, by eliminating this excess, asymmetries between world exports and imports would be reduced from one to two percent to one percent or less.

2. Existing materials

According to the 2008 SNA, the question of whether the value of goods covers the cost of transportation or not depends on whether the exporter or importer is responsible for transport (2008SNA 14.68). This means that cross-border trade in goods should be recorded at amounts specified between the buyers and sellers. The SNA has revised the treatment of transport costs in the revision of 1993. Before the 1993 SNA, the cost of transporting goods from a supplier to a purchaser was always separately identified and formed part of the difference between the basic price and purchaser's price. 1993 SNA revised this treatment by not recognizing transport cost if the price agreed between the supplier and the purchaser included the cost of delivery to a place of the purchaser's choice. The rationale for this decision is that that the point when change of ownership occurs is different under the different scenarios (2008SNA 14.60).

In contrast, the principle for valuation of general merchandise in BPM6 is the market value of goods at the point of uniform valuation and that is the customs frontier of the economy from which the goods are first exported, that is, FOB (BPM6 10.30). This means that imports and exports of goods are to be valued FOB, even if transaction prices agreed between exporters and importers include varying amounts of distribution costs, including none, some, or all of wholesaling, transport, insurance, and taxes (BPM6 10.31).

SNA recognized that the use of customs declarations is not necessarily ideal for use in the national accounts or BOP (2008SNA 14.69). It can be said that BPM6's requirement of a uniform valuation of imports and exports at the border of the exporting country is a deviation from the true transaction or actually observed price as a general valuation principle in 2008SNA.

It is to be mentioned that, in the BOP, merchanting entries are valued at transaction prices as agreed by the parties, not FOB (BPM6 10.44). To clarify this recommendation, "The treatment of Freight and Insurance Associated to Merchanting and the Geographical Allocation of Net Merchanting" stipulates that, depending on the agreed delivery terms, the freight and insurance costs shall be embedded in the sale value of the good or accounted for separately.

As to the treatment of transportation services, 2008SNA describes cases of identifying non-resident carriers from resident carriers (2008SNA 14.72). If it is the importer that contracts the delivery and if the carrier is not co-resident with the importer, an import of services takes place and, ideally, for the SNA it would be desirable to separate the CIF value into the value of the good only and the value of the transport service. If the importer undertakes delivery itself or contracts with a unit resident in the same economy, there is, in fact, no import of services even though it will appear there when imports of goods are recorded CIF. To counteract this, a fictional export of the same amount of services must be shown to leave the current balance of goods and services correct.

Based on the examples given in Box 10.3 of BPM6, Haan and Hiemstra (2018), as well as Walter (2018), argue that the constructed CIF/FOB values for exports and imports of goods are not consistent with the data collected for the international trade in transport services. They conclude that without information on the residency of the carrier, proper imputations cannot be made and the CIF/FOB adjustment diverging from the actual transaction value will easily lead to mistakes in the trade balance.

Finally, against the background of the development of the global value chain and the containerization, current business practices of the transport industry may be quite different from those established when BPM first recommended the CIF/FOB adjustment as a uniform valuation method. For example, by using containers, most merchandise is sent from exporters to importers seamlessly. It appears that BPM has not regarded the seamless transport as the major practice, but rather assumed that most goods are unloaded at the border of an exporting country and loaded on non-resident cargos. This assumption may have become obsolete.

Anne Harrison put forward four options in improving the consistency between BPM and SNA in the area of the treatment of freight transport (and insurance costs) and the valuation of traded goods.

1. The SNA could change its recommendation on the treatment of domestic transportation back to what it was before the 1993 revision. Under the past treatment, transportation is always treated as a service and never integrated with the value of the good.

2. The SNA recommendation could, if necessary, be changed to be strictly consistent with BPM6 when transactions with non-residents were concerned.

3. The SNA and BPM could stay as they are but with the inconsistencies are explained by a supplementary table showing how imports CIF are converted to imports FOB. Such a table should explain how much of the difference is rerouting and how much is a reclassification from goods to services.

4. It can be considered to amend the BPM guidelines and adopt the valuation on a true transaction or actually observed price basis.

3. Points for discussion

- What are your views on the 4 options put forward by Anne Harrison?
- Do you support the valuation of goods on a true transaction or actually observed price basis for international trade?
- Should we investigate the practical aspects of the true transaction of actually observed price approach such as the availability of source data?

(Reference)
Anne Harrison (2013), "FOB/CIF Issue in Merchandise Trade/Transport of Goods in BPM6 and the 2008 SNA" 25th meeting of the IMF Committee on Balance of Payments statistics.

Mark de Haan and Leo Hiemstra (2018), "CIF/FOB recording of imports and exports in the national accounts and the balance of payments," OECD Joint Meeting of the Working Party on Financial Statistics and the Working Party on National Accounts

Jens Walter (2018) "Measuring merchanting and international freight transportation costs in the Balance of Payments (BOP)," OECD Working Party on International Trade in Goods and Trade in Services Statistics