SNA/M1.20/6.4

14th Meeting of the Advisory Expert Group on National Accounts,
5-9 October 2020, Virtual Meeting

Agenda item: 6.4

Treatment of Emissions Permits: The Atmosphere as an Asset?

Introduction

1. To slow the increase in GHG emissions or eliminate them altogether, countries around the world have introduced or are introducing various polices aimed at reducing GHG emissions. In general, these policies apply a price to a broad set of emissions sources and are aimed at encouraging businesses and individuals to innovate and change their behavior and therefore reduce the level of GHG emissions. For example, it is rational to conclude that carbon pricing will encourage investment in cleaner energy sources and help countries meet their carbon emissions reduction targets as set out by the Kyoto protocol, Clean Air Act and other initiatives and later in the Paris agreement.

2. As countries adopt various carbon pricing strategies, it is important that the associated transactions (non-financial and financial) and stocks across all sectors are properly accounted in the System of National Accounts (SNA). Extensive discussions regarding the environment had taken place prior to when the *2008 SNA* was developed and adopted, as reflected in section Q of chapter 17. However, the notion of nature being considered as a capital good had not been fully developed. Additionally, emissions trading schemes were in their infancy. This short note proposes recommended updates to the SNA to clarify the treatment of emissions trading schemes.

Documentation:

A note on the Treatment of Emissions Permits: The Atmosphere as an Asset?

Main issues to be discussed

The AEG is requested to provide feedback as to whether the Task Team should consider the atmosphere as an asset when forming its recommendations related to the treatment and recording of emissions permits.

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Treatment of Emissions Permits: The Atmosphere as an Asset?

Background

1. Economic activity is having an increasingly negative impact on the environment. Rising levels of greenhouse gas (GHG) emissions are directly linked to climate change which is beginning to have far reaching and often permanent impacts on the environment. Given the environment can be viewed as a ‘free’ good, GHG emissions will be excessive, because there is little incentive for firms and households to change their behavior to reduce emissions. To slow the increase in GHG emissions or eliminate them altogether, countries around the world have introduced or are introducing various polices aimed at reducing GHG emissions. In general, these policies apply a price to a broad set of emissions sources and are aimed at encouraging businesses and individuals to innovate and change their behavior and therefore reduce the level of GHG emissions. For example, it is rational to conclude that carbon pricing will encourage investment in cleaner energy sources and help countries meet their carbon emissions reduction targets as set out by the Kyoto protocol, Clean Air Act and other initiatives and later in the Paris agreement.

2. As countries adopt various carbon pricing strategies, it is important that the associated transactions (non-financial and financial) and stocks across all sectors are properly accounted in the System of National Accounts (SNA). Extensive discussions regarding the environment had taken place prior to when the *2008 SNA* was developed and adopted, as reflected in section Q of chapter 17. However the notion of nature being considered as a capital good had not been fully developed. Additionally, emissions trading schemes were in their infancy. This short note proposes recommended updates to the SNA to clarify the treatment of emissions trading schemes.

Should the SNA the atmosphere as an asset?

3. The *2008 SNA* recommends that payments for permits relating to emissions into the atmosphere should be recorded as taxes because “*governments are increasingly turning to the issuing of emission permits as a means of controlling total emissions. These permits do not involve the use of a natural asset (there is no value placed on the atmosphere so it cannot be considered to be an economic asset) and are therefore classified as taxes even though the permitted “activity” is one of creating an externality. It is inherent in the concept that the permits will be tradable and that there will be an active market in them. The permits therefore constitute assets and should be valued at the market price for which they can be sold.*” (Paragraph 17.363).

4. Recognizing that the proposed treatment in the *2008 SNA* does not fully articulate all the dimensions of tradeable emission permits, further guidance was requested by the ISWGNA[1]. A task force (TF) was established in 2009, which examined the issue and produced a final report "OECD/Eurostat Task Force on the Treatment of Emission Allowances and Emission Permits in the National Accounts Final Report October 2010"[2]

5. The TF took as its starting point the recommendations found in the *2008 SNA* manual, which stipulates that the atmosphere should not be considered as an economic asset. Although, some TF members argued against this view, the discussions were framed within this context. **The guidance note being developed by the Task Team on Well-being and Sustainability is reopening this issue and is considering recommending that the recording of emissions permits starts with the perspective that the atmosphere is an asset.**

6. According to the *2008 SNA*, the system defines an asset as "a store of value representing a benefit or series of benefits accruing to the economic owner by holding or using the entity over a period of time." (Paragraph 3.5). An asset, therefore, must have a life greater than one year. However, there are some exceptions to the one-year rule – inventories, short-term assets (commercial paper, trade receivable). Personal attributes that are normally referred to as assets, such as individual skills and abilities, are not considered as economic assets and are excluded from the national accounts' asset boundary. Economic assets are either non-financial or financial.

7. Non-financial assets can be further decomposed as produced or non-produced. Assets that are created from a production process, are classified as produced non-financial assets (AN1), whereas economic assets that do not originate from a production process are classified as non-produced non-financial assets (AN2).

8. Non-produced non-financial assets are further decomposed into the following subcomponents:

- Natural resources (AN21) such as land and mineral resources;
- Contracts, leases, licenses (AN22) which are assets that have been created through government regulation, legislation or any other legal constructs. They consist of various non-produced assets: operating leases; licenses to undertake certain economic activities such as taxi licenses; permits to use natural resources (resource leases) and other government and legal constructs; and
- Goodwill and marketing assets (AN23), a special type of asset that represents the difference between the acquisition price of a company and the fair value of the assets less liabilities (excluding equity).

9. In the case of contracts, leases and licenses, the *2008 SNA* stipulates, in paragraph 10.186, that in order to be classified as non-produced assets the following two criteria must be satisfied:

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[1] The following points are summaries of the discussions from "The Recording of Emission Permits Issued under Cap and Trade Schemes in the National Accounts", SNA News and Notes, Number 30/31 (February 2011), and number 32/33 (March 2012).

[2] The report may be found at http://unstats.un.org/unsd/nationalaccount/criList.asp

- "The terms of the contract, lease or license specify a price for the use of an asset or provision of a service that differs from the price that would prevail in the absence of the contract, lease or license"; and
- "One party to the contract must be able legally and practically to realize this price difference."

10. Through these definitions the question that arises is whether the atmosphere is an asset and whether emission permits satisfy the conditions of the use of an asset? The *SNA* states that the atmosphere is not an asset because there is no value placed on it. While that may be the case, the fact that governments are able to issue emissions permits means that they are exercising ownership rights over the atmosphere and restricting/regulating its use, suggesting that it is an asset. Furthermore, the right to use the asset, as embodied in the emissions permit provides a benefit to the economic owner, either in terms of being able to continue to operate or as a potential financial investment. The emission permits are marketable, can be readily sold and for which market prices can be established. Emission permits are designed to have a finite time period but will exist for longer than a year, the holder of the permit bears all the risks and rewards and they are transferable. As such, emissions permits satisfy the conditions of an economic asset with the exception that currently the atmosphere is not recognized as an asset in the SNA.

Question for the AEG:

11. The Task Team on Well-being and Sustainability is considering a proposal which recognizes the atmosphere as an asset (but makes no attempt to value it), so that emissions permits can be treated as a non-produced non-financial asset and recorded as such in the SNA. The AEG is requested to provide feedback as to whether the Task Team should consider the atmosphere as an asset when forming its recommendations related to the treatment and recording of emissions permits.