Comments on draft SNA chapter:
Chapter 17: Cross-cutting and other special issues
Deadline for comments: 1 September 2007
Send comments to: sna@un.org

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Submission date:	31 August 2007

This three-part template allows you to record your comments on draft chapter 17 easily and, at the same time, makes it easy for us to use your comments in considering revisions to the draft chapter. You may complete any one, any two, or all of the three parts of the template.

There is no file comparing existing text with draft text for this chapter because the draft is all new text.

Save this template and send it as an attachment to the following e-mail address: sna@un.org

Part I: General comments

In the space below, please provide any general comments, such as about the clarity with which the new recommendations were incorporated (30 words or less).

Comment:

In general the new recommendations have been incorporated well.

Part II: Comments on specific draft paragraphs or passages

In your review of draft chapter 17, you may wish to devote particular attention to the passages listed below. For ease of reference, we have identified the relevant paragraphs. For each passage, a Word table is provided for you to use in making your comments. There is a row for general comments at the top of the table. Thereafter please use a separate row for each paragraph on which you wish to make detailed comments.

Chapter 17, Part 1: The treatment of insurance and social insurance other than pensions

Part 1 is based loosely on annex IV of the 1993 SNA, but includes several passages that introduce changes. Some of these are identified below.

1. A refined treatment of non-life insurance is introduced in paragraphs 17.37-17.39 to prevent the variation in claims made each year from affecting output. A different treatment is permissible when the claims are exceptionally large and beyond expectation (17.50). Are these paragraphs clear?

General comment	Different treatment of exceptional claims is sufficiently clear
17.37	Discussion for this section is clear
*	Click here and start typing.
17.50	Click here and start typing.

* Insert rows in this Word table for each paragraph on which you wish to comment.

2. The simplification in the SNA whereby direct insurance and reinsurance transactions were consolidated was seen to be causing errors especially in countries where all reinsurance was carried out with non-resident corporations (as is often the case). Is the description of how and why to treat direct insurance and reinsurance separately sufficiently clear (paragraphs 17.54-17.60)?

General comment	OK
17.54	Click here and start typing.
*	Click here and start typing.

* Insert rows in this Word table for each paragraph on which you wish to comment.

3. A treatment for annuities as a form of life insurance is introduced in Rev. 1. This is desirable in itself and because it is how regular payments in retirement under defined contribution pensions are recorded. Paragraphs 17.90-17.97 describe this treatment. Are the paragraphs clear?

General comment	
17.92	The last sentence is incorrect. The liability of the insurance company should equal the premium received – otherwise what transaction give rise to the difference? Also, any expected revenue to be earned by the insurance company will be built into the annuity price (if the revenue is to be passed onto the annuitant) or retained by the insurance company if the income earned by the annuitant is independent of the return to the insurance company, in which case it represents a gain to the insurance company and not to the annuitant.

17.97	Part (b) – it could be clarified that this amount represents the unwinding of the discount Part (d) – the reduction in liability is also equal to the benefits actually payable, which will be the counterpart to the payment made to the annuitant that will generally be in the form of cash. This could be clarified.

* Insert rows in this Word table for each paragraph on which you wish to comment.

Chapter 17, Part 2: The treatment of loan guarantees in the System

Rev. 1 distinguishes three classes of loan guarantees. The first is composed of those guarantees provided by means of a financial derivative (described in chapter 11). The second is composed of the sorts of guarantees where large numbers of very similar guarantees are issued. Another is described as one-off guarantees, where each guarantee is tailored to specific circumstances.

4. The second class is called standardized loan guarantees. A treatment of such guarantees is introduced in paragraphs 17.106-17.111. It resembles the treatment of insurance in several respects. Is the description clear and comprehensive?

General comment	
17.107	The liability mentioned in this paragraph should also be equal to the guarantee fee less the service charge (in other words, the unearned fee) – this would be a practical way of calculating it and would not require the NPV of expected future calls to be calculated.
*	Click here and start typing.

* Insert rows in this Word table for each paragraph on which you wish to comment.

Chapter 17, Part 3: The treatment of pensions in the System

Part 3 describes the treatment of pensions. It does so in some detail, in part because the means by which pensions are provided to persons in retirement varies considerably from country to country.

5. Rev. 1 incorporates a number of changes in the treatment of defined benefit pension schemes. After distinguishing between defined benefit and defined contribution schemes in paragraphs 17.141-17.146, the text describes the transactions recorded for a defined benefit scheme and provides a numerical example. This text begins in paragraph 17.147 and continues through paragraph 17.166. Is the text clear and comprehensive?

General comment	OK
17.142	There is no convincing reason to justify why any imputation is involved. The employer's expense (and the related employee's income) accrue as

	the employee provides his/her services, based on the (best available) actuarial information. Conceptually, this accrued amount represents the relevant transaction value between the two parties. If the so-called "actual contribution" (meaning presumably the cash amount) differs from this, then it should simply be treated as a payable or a receivable, consistent with the accrual basis that is implicit in the system. Any reference to an imputation is out of place in this and in several subsequent paragraphs -- the transactions are only 'imputed' in the sense that they don't necessarily involve cash
17.148	It would be helpful if the rationale for treatment of both an over-funded and an under-funded scheme was presented in a technically more robust manner. It is not sufficient to simply state that the employer's contribution should be calculated 'regardless of investment income earned by the scheme' without further explanation. It would be helpful to understand the reason why compensation of employees would be considered "understated" and why compensation of employees would be considered "artificially" reduced. Here is a reworked version of the whole paragraph ... "The employer contribution in relation to the pension entitlement earned in the period is calculated using an acturial methodology such that this contribution together with the investment returns of the fund are just sufficient to meet the obligation when it becomes due. As it is by nature a forward-looking calculation based on assumptions, it is inevitable that cases of over or under-funding will occur. In fact, extreme cases have occurred in the past where the investment of the pension entitlements has done so well that the employer has taken a "contribution holiday" and has not made a contribution towards current period entitlements until a balance has been restored. As this current period entitlement is part of the compensation of employees, not including an amount suggests counter intuitively that employees worked for nothing in the period(s) concerned in respect of this aspect of their remuneration. Rather than consider the adequacy or otherwise of the employer's past contribution rate(s) that led to such an over or under-funded situation, the approach taken here is that the contributions by the employer should be calculated regardless of any investment income earned by the scheme in the period concerned or any over-funding of the scheme. As a result, compensation of employees will continue to be recorded even in the event of a contributions holiday and the "benefit" to the employer is to be regarded as a change in liabilities between it and the pension fund. This leaves the net worth of both the same as when contributions are not recorded under a contributions holiday without reducing compensation of employees."
17.150	Refer to comments regarding imputation above. This paragraph could be reworded as follows: "The amount accrued in respect of employment services provided in a particular period is treated as part of the compensation of employees for

	that period in keeping with the accrual principle. The employer may discharge this actuarially determined amount in cash, build up an amount payable or have a mix of the two in the period. The amount is recorded as an outflow by the employer in the generation of income account and an inflow by the employee in the distribution of primary income account."
17.159	In the last sentence, it could be clarified that holding gains/losses attributed to the employer are recorded in the revaluation account.

* Insert rows in this Word table for each paragraph on which you wish to comment.

6. Paragraphs 17.183-17.193 describe the proposed supplementary table that gives flexibility to countries not to include all liabilities for pensions in the main accounts while still providing the information for analysts. Is the table clear?

General comment	OK
17.183	Click here and start typing.
*	Click here and start typing.
Table 17.10	Click here and start typing.

* Insert rows in this Word table for each paragraph on which you wish to comment.

<u>Chapter 17, Part 4: The recording of flows associated with financial assets and liabilities</u>
Part 4 describes the flows associated with financial assets and liabilities more extensively than in annex III of the 1993 SNA text, including the services associated with them.

7. The introduction, paragraphs 17.194-17.204, provides an overview of financial services that is wider than the traditional view of financial intermediation as applied to only deposits and loans. Is this wider perspective on financial services comprehensive and is the material presented in a helpful manner?

General comment	OK
17.194	Click here and start typing.
*	Click here and start typing.

* Insert rows in this Word table for each paragraph on which you wish to comment.

8. A new table summarizing the types of flows that relate to each instrument is given in table 17.11, which is introduced in paragraph 17.205. Is this table helpful?

17.211	The last sentence is inconsistent with the decision to treat the issuance of SDRs as liabilities of the recipient countries etc – see issue #44. Therefore, there is no ‘appearance’ to record in the other changes in assets account.

17.218	This suggests that FISIM can be levied by non-financial institutions such as retailers. I would have thought that when a retailer operates in this capacity a separate institutional unit, allocated to the financial corporations sector, should be created.
17.216	The last two sentences are almost judgmental in nature and could be either reworked to be more value neutral or even dropped.
17.220	It could be pointed out that the reason that there are no nominal holding gains/losses on loans and deposits is that these are always valued at their nominal amounts.
17.225 to 17.227	These paras are labeled "valuing securities" but they are mainly about how interest is calculated. Securities are always valued at market value regardless of whether the creditor or debtor approach is used – this principle does not come clearly through.
17.240	For clarification, "(ie treated as if the security was denominated in a foreign currency)" could be inserted after "by reference to the foreign currency" in the last sentence.
17.252	How should decreases in the value of the option between grant date and vesting date be treated – as negative CoE or as an adjustment to the previously recorded CoE?
Table 17.11	(1) It's not clear what the x's in parentheses mean. (2) It is possible for their to be buy/sell margins associated with financial derivatives.

* Insert rows in this Word table for each paragraph on which you wish to comment.

<u>Chapter 17, Part 5: Contracts, leases and licences</u>

The 1993 SNA did not have a comprehensive, coherent discussion of contracts, leases and licences. Part 5 brings together the material on the subject discussed under several of the 44 agreed Update issues.

9. Paragraphs 17.261-17.269 describes the three kinds of leases, including a description of resource leases, which are introduced in Rev. 1 in paragraph 2.269. Is the description of resource leases clear? Is the greater clarification of the distinction between operating and financial lease clear?

General comment	Generally, this section reads well
17.262	The test of "repair and maintenance" to determine whether a lease is operating or financial is too restrictive and it could lead to leases that are financial in character having "sham" repair and maintenance contracts with the legal owner to avoid them being classified as a financial lease. Other factors, such as the length of the leaser relative to the life of the asset and who is responsible for any residual value of the asset should also be considered.
17.267	It could be that the lessor charges a fee on an annual basis, in which case it would not be built into the value of the liability.
17.268	The issue of how holding gains associated with an asset under a finance lease arrangement should be recorded. Whether these accrue to the lessor or the

	lessee will depend on what arrangements are made for the 'residual' (ie who bears the risk from holding losses or the benefit from holding gains)
17.269	'rental' implies that it is a produced asset, this is inconsistent with the non-produced nature of radio spectra

* Insert rows in this Word table for each paragraph on which you wish to comment.

10. Paragraphs 17.301-17.305 describe how to record in balance sheets the benefits for each party corresponding to a shared asset. Are these paragraphs clear?

General comment	OK
17.301	Click here and start typing.
*	Click here and start typing.

* Insert rows in this Word table for each paragraph on which you wish to comment.

11. Paragraphs 17.306-17.311 describe the treatment of permissions to undertake a specific activity. Is it clear when a permit is to be treated as a tax and when it can simultaneously become an asset?

General comment	OK
17.309	The method of valuing the asset mentioned in the second last sentence would presumably only be adopted when there was no observable market value – perhaps this could be clarified.
*	Click here and start typing.

* Insert rows in this Word table for each paragraph on which you wish to comment.

Part III. Other specific comments

Para 17.5 – "particular" might be preferred to "peculiar" in the first line.

Para 17.6 – in concept, there would exist an unwinding of the discount for unearned premiums, so the premium earned in the second period would be somewhat more than 30. with the difference reflecting imputed income from the insurance company to the policyholder, which is then added to the 'pre-paid' premium.

Para 17.83 – this para states that funded schemes for benefits are not very common, and then states two cases where these might occur. In Australia, there is a third case, which is workers' compensation schemes, which are typically funded schemes operated by third parties.

Table 17.3 -- (a) is the intermediate consumption of households meant to represent the acquisition of insurance services by unincorporated enterprises? If so, it seems large relative to that acquired by corporations (even though it is only an example), (b) it's perhaps unfortunate that the net premiums and claims equal each other. While this could be expected in the long run, it's unlikely to be the case in any particular period.

Para 17.121 – the words "in the future" could be inserted before "benefits" in the second last sentence to clarify

Para 17.125 -- add the words "payable to the employee on retirement" after the word "benefits" in the first sentence - makes the description more consistent with the paragraph that follows.

Para 17.127 -- the expression "as they build up" does not indicate precisely that an accruals basis of recording should be used. Suggest that the sentence:

> "For both types of schemes, pension entitlements of the participants are recorded as they build up."

be changed to read:

> "For both types of schemes, the pension obligations of the employer and the pension entitlements of the participant employees are recorded as they accrue over each employment period."

Para 17.128 -- it is not clear why there is reference to the recording of transactions only - should it not be transactions and stocks or transaction and balances? Comment also applies to the sub-heading in para 17.129

Para 17.137 – the gains that accrue to participants in DC schemes that are attributable to holding gains should be recorded directly as a revaluation flow in the participants'' assets, and not as part of the use of income adjustment for the increase in pension entitlements item. To record the transaction as suggested in the paragraph introduces holding gains directly into the income account.

Para 17.140 -- recommend that the sentence:

> "Thus while there is (in principle) exact information available on the benefits for the participant in the defined contribution pension scheme, the benefits for the participants in a defined benefit pension scheme must be estimated."

be changed to read:

"Thus while there is (in principle) exact information available on the benefits for the participant in the defined contribution pension scheme at all times, the benefits for the participants in a defined benefit pension scheme can only ever be estimates in the periods leading up to exit from the scheme and can only be quantified precisely on actual exit."

It would also be worth noting that the benefit to employees in DC schemes is determined by contributions and investment income PLUS holding gains.

Para 17.169 – there are two other entries that could be made in the other changes in asset accounts that should be mentioned. The first is change the change in the NPV of pension entitlements, which should be treated as a revaluation. The second is the change due to changes in actuarial assumptions, which should be recorded as other changes in volume.

Para 17.171 – we found this paragraph to be unclear.

Para 17.203 – last sentence; notes and coins do not give rise to investment income, either.

Para 17.300 – It's not helpful to lead off saying that the "a full articulation of the balance sheets ... is difficult". Also, the case where royalties are set below the full value of the economic rent should be explained – presumably given that it has been decided that the asset cannot be partitioned the asset will be valued at the NPV of the full economic rent on the owner's balance sheet, and not at the NPV of the of the future royalties; otherwise the total value of the asset would be understated.