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Please find enclosed some comments on

Chapter 22 : The general government and public sectors

Best regards

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CH22

The general government and public sectors

As a whole, the chapter reads well, and is quite complete about the issues raised by the treatment of the general government sector in a SNA context. The discussion on the public sector and on the GFS presentation is adequate.

The only general reservation refers to the way the government units and sector are presented. In short, it is illogical to start from the public/not public nature of units, and it is reducing to build a classification of units on the basis of the market/non market nature of their production:

- it is illogical because it is necessary to have classified at least some entities as being government units in order to be able to assess that some other units are public;
- institutional units, especially those which are liable to belong to the government sector, cannot be reduced to their production function.

To summarise, it is irrelevant to define the general government as "*the collection of all public institutional units that are non-market producers*". This is also non pedagogical.

The points are dealt with according to the order of the sections of the chapter:

- A. Introduction
- B. Defining the general government and public sectors
- C. The government finance presentation of statistics
- D. Accounting issues particular to the general government and public sectors

A. Introduction

1. General remark about the section

Inside the section, there is a sub-section consisting in only two § - §§ 22.11-22.12 -, that is curiously titled “Data sources”.

In addition to the fact that it is odd to have a first sub-section that is not followed by a second one, the title does not really fit the content. There are actually two different topics under respectively § 22.11 and 22.12:

- § 22.11 deals actually with the method used by national accountants for compiling the government accounts, which is closer to an accountant’s work than a statistician’s work: this specificity is certainly due to the nature of data, however it is strange to refer to it as an issue of “data source”;
- § 22.12 deals with consolidation

2. Detailed remarks about §§

§ 22.1 To aggregate or to disaggregate ? that would thus be the question ?

First, although it is conceptually possible, it is not frequent to compile accounts for individual units. Then, what does “chosen intermediate levels” refer to ? something between individual units and sectors ? isn’t that sub-sectors?

What does mean to “aggregate the accounts in different ways” ? does it refer to the ability to aggregate units belonging to different sectors of the central framework, as it is the case for the public sector ? or does it refer to the aggregation of parts of the sequence of accounts ?

In both cases, why coming back afterwards to the usual sectors and sub-sectors - of the central framework, presumably ?

§ 22.2 There are some problems of wording in this paragraph. Either these paragraphs are considered as being purely introductory - i.e. as a kind of gossip -, and they should be shorter. Or they are thought to include substance, in which case precision is needed.

3rd sentence:

“They are able to redistribute income and wealth by means of taxes and social benefits”

It is not right to limit the redistribution of income to the reference to taxes and to social benefits. In many countries, compulsory social contributions are as important as taxes in amount. Furthermore, all current transfers are in general means of redistribution of income: for instance, non-market education services, provided through social transfers in kind of a type that do not belong to social benefits, have always a redistribution dimension; subsidies are redistributive transactions, too. Capital transfers - investment grants, compensation payments - are also involved. A more general wording, referring to “other transfers” should be more neutral, although it is necessary to quote taxation, that is unavoidable.

Proposal: *“They redistribute income and wealth by means of taxation and other transfers”*

4th sentence:

“The accounts for the general government sector show how the revenues raised are used to provide goods and services to the community as a whole or to individual households”

From a pure wording point of view, it is strange to refer to accounts here, since we are only dealing with functions, not with their transcription into accounts.

In addition, this is not right in accounting terms. National accounting is typically a “by nature accounting”. To see how revenues are allocated to the provision of goods and services would require a “by function accounting”. This also means that, contrary to the sentence, revenues are also used to make transfers.

Last sentence:

“The range of goods and services government provides and the prices charged are based on political and social considerations rather than on the profit-maximisation objective of private corporations”

It should be relevant in this sentence to quote the “public goods” expression.

It is probably too much to refer to private corporations. “Profit maximisation” should be enough. In addition, this wording is only oriented to the production aspect of the so-called public goods. The point of view of the consumers should also be addressed, through the use of an expression such as “private satisfaction”, for instance.

§ 22.3 It is not clear to understand the purpose of this paragraph. If its purpose is to introduce the relevance of the public sector, which implies to refer to public corporations in addition to government, it would be better to mention only the quasi-fiscal activities, as they are described in the last four sentences. It is actually usual to describe that as quasi-fiscal activities.

Instead, it would be necessary to check whether it is accepted terminology to describe as “quasi-fiscal operations” what is dealt with in the beginning of the paragraph. First, it is not relevant to enter into a discussion about budgetary procedures at this stage, where only the functions of the government and of the public sector are at stake. It is no more relevant to discuss privatisations, restructuring operations and securitisations, and to mention special purpose entities ¹ and restructuring units.

Furthermore, it is likely that flows relating to privatisations and to securitisations are reported in the budget. In national accounts, restructuring units and also securitisation units will frequently be classified in the government sector, and are not public corporations. In national accounting, operations relating to privatisations, and many times to securitisations, will be reflected in the government accounts (there is no need of the public sector notion for that). Finally, when properly accounted for, privatisations, restructuring operations and securitisations ² have no impact on government revenue, and little impact on expenditure.

§ 22.6 Same remark as for § 22.2. It is allowed to quote examples, under the condition to refer to them explicitly as examples. However, when concepts are mentioned, they should be defined with precision.

Thus, total revenue does not limit to taxes, user fees and grants from other governments. Once again, social contributions are involved. Other revenue include not only user fees - for which it would be better to refer to sale of goods and services -, but also property income received and a lot of other types of revenues.

What is important to tell here is that, in this alternative presentation, a heading - total revenue, for instance - may group transactions that are recorded in several parts of the SNA sequence of accounts. It is doubtful that the reader will be in a position to understand that from the present text.

1. “including those abroad”, good heavens !

2. When considered as a sale, the securitisation of non financial assets has however no impact on revenue, since it does not increase net worth. It impacts only the net lending/borrowing of government.

B. Defining the general government and public sectors

The main concern is this section relates to the logic of the presentation that starts from the distinction between public and not public, and then takes decisions on the only basis of the market/non-market nature of the production undertaken by the concerned entities.

Instead, the definition of “public” needs that at least some government units have been defined first, without quite any consideration about their productive function, and no test about their market/non-market nature.

1. An anti-pedagogical definition of government

§ 22.15 defines the general government as “*the collection of all public institutional units that are non-market producers*” ! This is typically irrelevant and anti-pedagogical. Furthermore, as it is worded, this statement is illogical and non operational.

Can anyone think of, say, the federal government of the USA as being characterised to be a non-market producer ? Is it necessary to check its non-market nature, as a producer, in order to classifying it as a government unit ? Is it even necessary to refer to it as a producer for this classification purpose ?

The right definition of government units as “*unique legal entities established by political processes*”, that is recalled in § 22.17, puts this very feature in the first position. Even thought of as economic agents, it is recalled that governments are responsible for the only provision of some types of goods and services, without any obligation to produce them themselves. In this respect, they are consumers before being producers. Moreover, the (re-)distributive functions of governments are at least as important as their productive function: for instance, in the numerical example provided in the SNA, the production costs of the government sector represent far less than 50 % of its total resources, which means that other expenditures make up the majority. Finally, the financial function of government is important, too.

It is not because a production is attributed to quite all agents in national accounts, that all institutional units and sectors are primarily characterised by their production.

Most of the time, it is not necessary to check the non-market productive nature of government units to characterise them as government.

The productive function of units belonging to the general government sector is mainly relevant for units engaged in the provision of individual services. It is only in a limited number of cases that it is necessary to check their non market nature. This has however to be done sometimes.

In addition, there is some illogism behind that. To define units belonging to the general government as being, first, public units implies a circular reasoning. How is defined the “public” feature of a unit ? By the fact that it is controlled by a government unit. However, how can we know that the controlling unit is a government unit ? by its public feature !

In other words, it is necessary to decide first that some institutional units are genuine government units. This is precisely the relevance of the notion of government units, that constitute the core of the government sector.

§ 22.13 Following the above remarks, it is also irrelevant to say that “*the definition of what is meant by control is fundamental to identifying the units falling within the public sector*”.

That is not right. For most of the public sector, that is for the government sector, the public feature is self-evident. The notion of control is necessary for the, few, NPIs that are part of the government sector.

Instead, it is only fundamental for deciding that some corporations are public.

§ 22.14 The above remarks about market and non market apply also to this paragraph.

In fact, all what is indicated in these 3 paragraphs is an evidence of an upside down approach:

- the right approach consists in identifying, first, government units, which enables to define the public control; it is only after that step that, for some units, it is possible to decide if they belong to government; for some corporations, the existence of a public control leads to classify them into the public sector;
- instead, in the approach favoured in these paragraphs, the first decision relates to the public nature of a unit that, in addition, is supposed to be an institutional unit, which is not an obvious issue³: as indicated above, this is logically impossible.

Such an illogical approach looks like defining rain as an event that occurs when - and because ! - people have umbrellas open in the street.

§ 22.16 *"It is helpful to begin by ... the definition of government units"*

No, this is not helpful, this is fundamental, and not what is referred to as fundamental in § 22.13.

2. Detailed comments: government units

As a whole, this text is clear and relevant. One may note that reference to production is scarce in this text.

§ 22.24 This paragraph raises a small concern.

Although the recommendation is wise, it is formally in contradiction with the definition of financial intermediation which is provided in SNA08 (chapter 4). There is no longer reference, in this definition, to the fact that a financial intermediary places itself at risk. Many units, whether established or not by financial institutions, are usually considered as financial intermediaries without being themselves at risk: mutual funds, partly life insurance companies, some pension funds, etc.

Perhaps, the issue can be solved by making reference to the fact that units engaged in financial activities should be classified inside the government sector when their main purpose is to serve government units, or to act on behalf of them.

3. Detailed comments: NPIs controlled by government

The definition of NPIs classified inside the general government sector has been changed. In SNA93, the NPIs that are classified in the general government sector are the *NPIs that are controlled and mainly financed by government units*. This terminology is superseded in SNA08 by the following: NPIs that are classified in the general government sector are the *non market NPIs that are controlled by government units*. GFSM, as for it, retains the same terminology as SNA93, using however sometimes the ecumenical expression: *non market NPIs that are controlled and mainly financed by government units* (GFSM §§ 2.28-2.29).

This change is unhappy. The main concern with NPIs that are liable to be classified in the general government sector deals with the control issue, not the market/non market issue. Quite all such NPIs are non market producers. More precisely, as for most government units, their productive function is secondary.

The concern is that, among the indicators of control, there is the degree of financing. This means that, if a NPI is largely financed by government, it may be deemed to be controlled by government, and thus classified inside government. This is a bit in contradiction with the handbook on NPIs. There exist many NPIs that have large public financial support, and are fully independent: this is especially the case of NGOs operating abroad. This is also the case of NPIs engaged in the so-called IFFIm⁴, promoted by the UK government.

3. Following the approach that is proposed in chapter 4, except for households, it is quite impossible to decide that an entity is an institutional unit without, in the same time, deciding that it is either a government unit, a NPI or a corporation. Then, the precise classification of NPIs and corporations has to be decided upon.

4. IFFIm = International Finance Facility for immunisation.

It may be useful to state that there are NPIs controlled by government that are market producers. They are then classified in a corporations sector, in a sub-sector of public corporations. This is frequently the case for saving banks.

4. Detailed comments: Corporations controlled by government

§ 22.27 Some wording issues.

“To be classified as a public corporation, an institutional unit must not only be controlled by another public unit, but it also must sell most of its output for economically significant prices.”

Normally, it is not enough for an institutional unit to sell its output at economically significant prices in order to be a corporation. It must also be recognised at law as a separate legal entity, and be a source of profit/financial gain for its owners.

5. Detailed comments: Economically significant prices

1. General

The general orientation of this part is right and relevant. However, it is likely that some ones will consider it as being too much prescriptive: this is a strategic issue that is no longer dealt with in the following.

Apart from that, there is a need for modifying slightly this part. In fact, the present wording is too much oriented to the case of public producers facing a market situation, but that receive so much financial, or other, support from government that the prices they charge are non significant. In this case, the market/non market distinction is a question of degree: this is the meaning of § 22.32. Consequently, the test consists in a comparison between receipts from sale and production costs.

However, what is actually at stake in §§ 22.34-22.38 refers to the question whether there is, or not, a market situation.

There are indeed two different issues when public producers are involved:

1. The first one may be summarised by the question: is there a market situation ?

The extreme case is when there is only one public producer, or a set of public producers, that provide services that are paid for by government units which, in addition, may not necessarily be the ultimate consumers.

In this situation, it is irrelevant to refer to sales and to prices. Any producer, public or not, market or not, needs financing, at least to survive. The issue is thus: does this financing correspond to a market situation, does it take the form of a sale ?

This issue is, more or less, dealt with in §§ 22.34-22.38.

2. The second issue deals with a public producer that is facing a situation that is potentially market, that is where the producer has the possibility to adjust its supply in function of prices, and purchasers/consumers react in consideration to the prices that are proposed.

This situation may be encountered in the situation of the so-called natural monopolies, in which it is frequent to have public corporations.

In this case, it is the level of the price that is relevant.

The wording could therefore be amended along the following lines:

1. For public producers - which refers to units that are not covered by the term “government units, discussed in §§ 22.17-22.20 -, the classification depends on the market/non-market description of their output.

This relies on the definition of economically significant prices, in its simplest form (see below the criticism that is borne to the present wording).

§§ 22.29 and 22.30 could be deleted.

2. The need for a taxonomy

The interesting §§ 22.31-22.33 should result in a distinction between

- cases where there is no market situation
- cases where a test has to be carried out

it should be specified that the distinction may be made at the level of group of producers, when the nature of the relationship prevails over a decision based on a ratio.

3. The case where a test has to be carried out: this applies to the case where a public producer faces users/purchasers that have a market behaviour.

2. Detailed comments

§ 22.28 In general, it is not wise to try to specify what the definition of economically significant prices means. The definition according to which they have "*a significant effect on the amounts that producers are willing to supply and on the amounts that purchasers wish to buy*" is relevant by its generality. It simply means that a market situation is one where supply and demand are regulated by prices, by difference with other ways of regulation (quantities, for instance). It can be adapted to any kind of market configuration.

Any way of trying to be more specific may be criticised, or it should be necessary to be complete and precise, which is out of reach, especially in this chapter, where it is not a main topic. In particular, before any specification may be undertaken, it is necessary to examine the nature of the transactors.

Here, for instance, it may be criticized to specify that "*a producer has an incentive to adjust supply with the goal of making a profit in the long run*". In the theory of market competition, producers do not make profit in the long run. And, insofar as "*covering capital and other costs*" is concerned, this is not specific to market producers: non-market producers may be encouraged to do the same, however they will continue to be non-market if their resources do not consist in sales.

The following sentence: "*Consumers have the freedom to purchase or not purchase*" is no more relevant in all cases:

- purchasers are at stake, rather than only consumers (investment goods may be concerned, the expenditure may be borne by units that are not the actual consumers);
- in situations of market competition, purchasers decide the quantities they want to buy, they are not facing the only alternative "to buy or not to buy";
- particularly when government is in the position of the purchaser, there may be situations of monopsony, where purchasers are price-makers, and not price-takers.

§ 22.29 By difference with just above, in the very specific situation where there is a public producer and purchasers that have a market behaviour, it is legitimate to base the market/non market distinction on the ability of the producer to recover costs from receipts from sales.

However, some may find that the 50 % threshold is too prescriptive.

It is a mistake to mention subsidies on products here (see below).

About the 50 % threshold

The concern about the 50 % threshold is that, although attention is drawn on the fact that it is not prescriptive, this will actually be taken as a rule in practice and will become such.

Although this threshold is not so laxist, since in particular the cost side includes financial costs, it raises some basic concerns:

1. The origin of this threshold is uncertain: does it correspond to a balance between pure non-market output - for which sales should be deemed to be nil - and pure market output - for which net operating surplus would cover just the cost of financing in a long-run competitive context?
2. The consequences it implies for a producer operating just above the 50 % threshold should be examined. In the context of this chapter, such a producer would therefore be a corporation, that is a unit that is able to distribute profit to its owner.

3. The concern is that such a producer will necessarily need resources from government - its owner - under the form of a kind of subsidy or other transfer.
4. If the producer gets its financing from equity from government, its owner, it will be in a bad situation for distributing dividend as a counterpart. This enters in contradiction with the description of the producer as a corporation.
5. If the producer gets its financing from debt issuance, it is unlikely that it can borrow without the guarantee of its owner. Very often, the government/owner will borrow on behalf of the producer. This is in contradiction with its description as an institutional unit.

In other words, from a conceptual point of view, it would be better to avoid even the mention of a 50 % threshold. This does not preclude that some countries could implement such a threshold on the basis of practical considerations. In practice, cases are in limited numbers.⁵

§ 22.30 The last sentence of this paragraph is hard to understand. First, it is not very relevant to use the expressions “market (or non market) institutional units”. All institutional units cannot be reduced to their production function. Whatever inelegant it can be, it is pedagogically better to refer to “institutional units in their capacity of producers”.

Then, the actual meaning is not clear. Is it question to combine the accounts of two different institutional units ? Or does it mean simply that: “*The general government sector cannot include institutional units that are market producers*” ?

§ 22.31 As it is a general sentence, it is more relevant to refer to private producers, rather than only to private corporations. Heavily subsidised farmers are also market producers, when they produce in the context of households’ unincorporated enterprises.

However, there is a concern, because “private” covers also NPIs.

§§ 22.34-22.37 Although the general spirit of these statements is relevant, there is a risk being too specific. All these prescriptions could be summarised in a single sentence that ultimately would explain that public producers are likely to be non-market producers when they supply goods or provide services to government, in a context where they do not enter in an actual competition with other private producers.

§§ 22.39-22.40 Definition of sales and costs

As the aim is to decide if the output of a producer is market or not, it is necessary to be careful about the terminology. Therefore, as long as the decision is not taken, expressions such as “basic prices” or “subsidies on products” should be avoided, since they are relevant only for market output. More neutral expressions have to be used.

Tentative proposal:

In order to assess the market nature of the output of a public producer, it is necessary to carry out a comparison between, on one side, the receipts from the sale of the goods or services supplied, and, on the other side, the production costs of these products. Sales are measured before any taxes that are attached to the products. Sales exclude all payments received from government, except if they are granted to any type of producer in this kind of activity. Own-account production is not considered part of sales in this context.

Note: it is not necessary to mention transfers to cover an overall deficit. When the producer is market, these payments are subsidies on products. This wording comes from a misunderstanding in the wording of the ESA95 text.

Production costs: it is necessary to mention that production costs that are linked to the own-account production have to be eliminated, since the related output does not enter in the comparison.

Note that “subsidies on production” is ambiguous. On the side of production costs, only other subsidies on production are at stake.

5. The alternative would be that public corporations are considered to be different from other corporations, and are assumed to behave differently. There is no such a prescription in the SNA.

6. Detailed comments: Decision tree

It could be useful to specify that the decision-tree can be followed in an iterative way. In complex cases, it is only when analysing in depth the relations of a unit in order to decide about control that it appears that this unit is eventually not an institutional unit.

As it stands, the decision-tree suffers of a lack of logic, that stems from the fact that the government nature of a unit has been defined after its public nature has been assessed first (see remarks above about §§ 22.13-22.15).

Thus, for instance:

- in *b*, it is asked whether the institutional unit is a government unit: logically, if yes, the decision-tree is terminated; however, here, it is only concluded that the unit is public, and the decision is postponed in *c*;
- in *c*, the wording is very confused. The first question is : is it a market or a non-market producer ? If it is a non-market producer, it is part of government. If not, does it sell at economically significant prices ? which is exactly the same question. In other words, it is possible to have units that are not non-market producers in the first part, and that are finally non-market producers in the second part !

All that could be avoided by coming back to “*fundamentals*”. It should be made clear that the decision-tree does not apply to units/entities that completely fulfil the demanding definition of a government unit, that is provided in § 22.17. In other words, this consists in “extracting” this question from the leg *c* of the decision-tree.

It should be specified that the decision-tree is restricted to the case of units that come forward as being principally producers of goods and services.

7. Detailed comments: Sub-sectors of the general government sector

Social security funds may be either included in each level of government, or excluded and grouped in a separate sub-sector.

8. Detailed comments: Borderline cases

Quasi-corporations

All what is told here is excellent, and well worded. However, for the purpose of the chapter, it has been forgotten to specify that, by construction, quasi-corporations owned by government belong to the public sector.

In addition, all that should be expressed in the same way in chapter 4. Is it a purpose of chapter 22 to be, at most, self-sufficient ?

Restructuring agencies

All the recommendations made here are welcome. The only concern refers to the idea, that is mentioned in § 22.53 and in § 22.54-b, that the possible market or non-market character of these units could be relevant in the treatment.

Only the case of agencies set up on purpose is dealt with. As for units engaged in financial activities, the productive aspect of such an agency is secondary with regard to its other functions. Thus, decisions about its classification should certainly not be taken on the basis of the considerations such as a ratio between sales and costs.

As for its productive activity, such an agency provides services only, or mainly, to the government that has established it. Therefore, its case has to be dealt with in the context of ancillary activities or - which is equivalent - in the context of §§ 22.34-35, where a public unit provides services to government in absence of any competition.

Such an agency is likely to cover its costs by withdrawing money on the cash flows it manages. These payments are not to be considered as sales of services.

In other words, the market/non-market issue is not relevant for this case.

Special purpose entities

In order to be completely clear, it should be specified in § 22.58 that “*Non-resident SPEs are always classified⁶ as separate institutional units in the country/economy where they are established*”. Not to specify this point could lead the reader to understand that such a unit is, for instance, a kind of extra-territorial enclave.

In the same §, it would be better to say: “*All flows and stock positions between the general government and the non-resident SPE should be recorded in the general government and the rest of the world accounts when they occur*”. National accountants cannot indeed compile accounts for non-resident units.

The same changes may be borne in § 22.59.

Joint ventures

§ 22.64 It is not clear what the following sentence means: “*Public units can also enter into joint operating arrangements that do not involve separate institutional units.*”

Of course, such arrangements involve several units. So, the only meaning should be: “ ... *that do not involve the establishment of separate institutional units.*”

Supranational authorities

§ 22.66 the wording: “*it is possible to construct a set of accounts for the authority as if it were a resident unit of the member country*” is ambiguous. It should be specified that, nevertheless, the authority remains non-resident.

6. “treated” or “considered” would be better than “classified”. From a classification point of view, such units are classified in the RoW.

C. The Government finance presentation of statistics

Very few observations are made about this section. However, as a general remark, it may be useful to make reference to the IMF GFS, in order for a reader to have additional information on specific concepts, such as revenue, expense, etc.

§ 22.70 “Grants” has to be included in the list of the headings for revenue. “Grants” is an elementary category in IMF GFS, that is not included under Other revenue.

§ 22.75 “Subsidies” has to be included in the list of the headings for expense. “Subsidies” is an elementary category in IMF GFS, that is not included under Grants or Other expenses.

§ 22.84 The presentation of the changes that affect the level of liabilities is not very clear and it may be misleading, if not erroneous.

First, despite the English label of the balancing item of the capital account, it is not fully right that net borrowing increases the level of liabilities, while net lending reduces it. A deficit - net borrowing - may be financed by the disposal of existing financial assets, having thus no impact on the level of liabilities. Furthermore, it may happen that the level of liabilities is reduced with a nil balance.

From this observation, it comes that some statements of the paragraph are partially wrong. For instance:

- indent a: it is not right to state that, as such, the level of liabilities is reduced by an acquisition of financial assets; no acquisition of financial assets can reduce by itself the liabilities of anybody; symmetric remark for the disposal of financial assets.
- indent b: instead, it is tautological to state that the level of liabilities is increased by an incurrence of liabilities and reduced by repayments of liabilities.

In fact, it is the sum of net lending/borrowing and of the movements that affect financial assets that have a resulting impact on the level of liabilities, when it is the total of liabilities that is involved. Conversely, when attention is focused on the level of a sub-total of the liabilities in selected financial instruments - the financial debt, or the so-called public debt, e.g. - this level may be also impacted by the movements that may affect the other liabilities - i.e. the liabilities that are not included in this sub-total.

In absence of other flows, the right expression is as follows (care has to be taken of minus/plus):

$$\begin{aligned} \text{Changes in total liabilities} &= \textit{minus} \text{ Net lending/borrowing} \\ &\quad \textit{plus} \text{ Transactions in financial assets} \end{aligned}$$

For instance:

1. Suppose that the non-financial transactions of government - or any other unit - result in a surplus, i.e. a net lending of 100;
 - suppose also that this surplus materialises in an increase of the cash position, of 100;
 - to subtract the second amount - which sums up the total transactions in financial assets - from the first one leads to 0, which is the amount of the change in liabilities: the level of liabilities is indeed unchanged.
2. Suppose again that the non-financial transactions of government result in a net lending of 100;
 - suppose now that this surplus is completely used in order to repay some liabilities;
 - the total transactions in financial assets amount to 0; therefore the changes in liabilities is equal to *minus net lending*, showing a reduction in the level of liabilities.

3. Suppose now that the non-financial transactions of government result in a deficit, i.e. a net borrowing of 100 (it is also possible to say a net lending of *minus* 100);
- suppose now that this deficit has been financed by an incurrence of liabilities;
 - as the total transactions in financial assets amount to 0; therefore the changes in liabilities is equal to *minus net borrowing*, which is positive, showing an increase in the level of liabilities.

If it is a sub-total of specified liabilities that is aimed at, the expression is modified as follows (other liabilities refer to the liabilities that are not included in the sub-total):

$$\begin{aligned} \text{Changes in the total of specified liabilities} &= \textit{minus} \text{ Net lending/borrowing} \\ &\quad \textit{plus} \text{ Transactions in financial assets} \\ &\quad \textit{minus} \text{ Transactions in other liabilities} \end{aligned}$$

§ 22.84 Although the other changes have certainly to be mentioned, it is not completely relevant to state that, because deficits have accumulated over many years, the other changes may be significant on the level of government liabilities.

The level of liabilities is quite not impacted by other changes in volume. Uncompensated seizures by governments have seldom occurred since Russia in 1917. Instead, debt forgiveness by creditors is recorded in the capital account, and not in another changes of assets account.

Conversely, the changes that affect interest rates are reflected in the revaluation account. They may be significant in periods of high inflation. However, the impact does not depend on the fact that the debt has accumulated over many years, except if this means that the level of the debt is high.

§ 22.84 The first sentence deals with the *net level of government liabilities*, which, in absence of any consolidation, is meaningless. The "level" is enough.

§ 22.86 The reference to *credit* and *debit*, which are not commonly used terms in national accounting, and seem to become out of fashion in business accounting, brings no additional clarity. It is enough to have made acquaintance in this chapter with revenue and expense !

D. Accounting issues particular to the general government and public sectors

1. Detailed comments: Debt and related operations

§ 22.115 “*In addition to the financial transaction concerned, the forgiving unit records a capital transfer payable for the amount forgiven ...*”

This formulation is not very clear. It would be better to say that the recordings of capital transfers are made as counterparts of the transactions in liabilities.

§ 22.120 Debt defeasance: there are two concerns in this paragraph.

1. The relevance of the mention of this type of debt defeasance, as an operation typical of debt management for governments

In its most formal understanding, debt defeasance is one of the technical arrangements consisting in pairing assets and liabilities, most frequently inside a dedicated structure/vehicle. Other ones are referred to in this chapter:

- some cases of bailouts - specifically those mentioned in § 22.129-c and § 22.134;
- cases of securitisation.

The specificity of debt defeasance, as it is described in § 22.120, consists in the fact that liabilities are segregated in a dedicated vehicle, to be matched with assets, whereas for the two above-mentioned cases, assets are segregated this way.

As such, the arrangement that is described here, in § 22.115, relates to operations that are common for businesses, but that are not usual for governments. It is not common indeed for governments to remove liabilities from their own balance sheets, in order to pair them with high quality assets.

Instead, especially when interest rates change, it is a method for businesses to upfront, at one point in time, profits or losses, depending in the direction of the changes of interest rates, accruing from their liabilities. It is a less costly alternative to the repurchase of those liabilities.

In other words, this paragraph about debt defeasance should be better inserted in the chapter on the financial account - where it is probably -, rather than here, where it is in fact not relevant (or the reader will not see its relevance).

2. The case of SPEs

As a “by-product”, § 22.120 sets out an interesting mention about SPEs, stating that “*a special purpose entity is usually not recognized as a separate institutional unit*”. The end of the paragraph is even stronger, since it suggests that defeasance debt operations undertaken through a SPE should be treated as “*on balance sheet*” rather than “*off balance sheet*” of the originator.

This statement is interesting to the extent that such a position could have been a valuable option in the SNA update, under the condition of a complete reconsideration of the classification of some financial instruments. However, may be because of lack of boldness or an excess of caution, this has not been the choice. It is indeed stated in chapter 4 that, in some circumstances, resident SPEs are considered as full institutional units, to be classified into the “Captive” sub-sector.

In securitisation arrangements, it is necessary, from an accounting point of view, that SPEs used as securitisation entities been recognised as institutional units, in order for the securitisation be treated as a sale of assets, when this is actually the case.

It is therefore excessive to state here that the general rule consists in not recognising SPEs as institutional units. It would be more balanced to state that conditions for this recognition are demanding⁷. See also the wording that is used in § 22.57, that is more careful.

7. As a whole, the reader of the SNA08 will be puzzled about the treatment to apply to SPEs: are they institutional

§ 22.122 Since the choice is made here to mention alternative treatments that have finally not been retained in the SNA, it would be relevant to mention, in addition to the imputation of current transfers, the possibility to impute capital transfers.

§ 22.124 Without explaining in detail the treatment of guarantees as financial derivatives, it may be useful to simply mention that all transactions relating to these guarantees are financial transactions (they have thus no impact on net lending/borrowing of the general government).

§ 22.130 As a general statement, this assertion is too strong. For instance, in case of guarantees - that is referred to in § 22.129-a -, there is no capital transfer at the time the guarantee is granted. When loans are purchased or segregated, it is questionable whether a capital transfer is recorded.

§ 22.132 And so what ? What would be the consequences if loans were tradable ?

§ 22.133 Rather than be recorded as a revaluation, the change in value of the loan would be better recorded as an other change in volume in this case.

§ 22.134 As already mentioned, the feature consisting in placing itself at risk is no longer a criterion for treating a unit as a financial intermediary. A better rationale would consist in stating that the unit acts on behalf of government.

§ 22.135 and following Securitisation

A general concern with the paragraphs that deal with securitisation - §§ 22.135-22.137 - is that, although they are happily confined to general guidelines, they present a treatment that prevailed, in Europe, at the time the draft chapter on the government and public sectors was written, and that the recommended treatment has now changed slightly. That is a drawback when trying to be too prescriptive.

However, there are more general remarks on these paragraphs.

1. The definition that is provided in § 22.135 of securitisation is not relevant

Although it is not the purpose of chapter 22 to explain in depth what securitisation is, it is nevertheless useful that all the SNA text have a pedagogical purpose, thus avoiding to provide inadequate definitions.

In its most general understanding, securitisation consists in issuing securities on the basis of the financial flows that are expected to be generated by assets, or other rights liable to generate cash flows. In this regard, it is very different from the traditional credit relationship that prevails between a bank and a borrower, where it is the general creditworthiness of the borrower that is considered by the lender, i.e. by the bank. In a securitisation arrangement, instead, it is the ability of the only securitised assets/items to generate cash flows that is considered, and that can be largely spread and channelled to investors. This change in the credit conception is a fundamental feature of the financial innovation.

As a financial arrangement, securitisation may entail various advantages that may be considered by the various parties, originators and investors as well:

- for financial institutions, it is a way to improve their solvency ratios, which implies that the securitisation entity appears to have no legal link with them;
- for governments as originators, it is a way to improve their liquidity without increasing their liabilities, in matching assets they own with issued securities in a sale arrangement;
- for investors, it is also an opportunity, that is not discussed here.

2. The definition is furthermore illogical

The actual problem raised by securitisation in national accounting is precisely to decide if there is, or not, a change in the ownership of the securitised assets/rights, from the originator to the securitisation entity.

units or not ? This doubtful interrogation may be eventually better than certainty resulting from strong and unrestricted assertions about their actuality as institutional units.

It is therefore illogical to state that “*securitisation occurs when a unit ... conveys the ownership rights over ... assets ... to another unit*”, the change of ownership being precisely what is at stake in the SNA treatment. Therefore, the wording presents as a definition what has to be established.

3. Proposal for wording: something as:

Securitisation is a financial technique which consists in issuing securities - usually bonds - on the basis of the financial flows that are expected to be generated by assets, or other kinds of rights liable to generate cash flows, belonging to a unit, which usually - but not necessarily - happens to be the originator of the arrangement. Securities issued this way are referred to as “asset backed securities (ABS)”.

When a government unit is the originator of a securitisation arrangement that is carried out with the support of a securitisation unit, the main issue, for national accounts, consists in deciding if there is an actual change in ownership of assets in this arrangement. If there is such a change of ownership, the arrangement is treated as a disposal of, financial or non financial, assets, by the government unit. If there is no change in ownership, the arrangement leads to record a borrowing by the government unit.⁸

§ 22.136- indent a

The issue does not refer actually to the level of the purchase price, but to possible clauses implying that the government may be interested in the occurrence of additional payments if the securitised assets are eventually resold at a price that is higher than the purchase price. These clauses are usually referred to as “deferred purchase price” clauses. In other words, to be treated as a change in ownership, the sale should be unconditional. It may be that this situation is the actual topic of § 22.137.

§ 22.137 Neither the case under review, nor its treatment in national accounts are very clear.

Furthermore, there is a case of securitisation that does not seem to have been dealt with. It refers to the securitisation of future income flows - property income or rentals -, that is flows accruing from existing assets. There is an issue when such income flows are partially securitised, i.e. only some periods of income flows are securitised without the ownership of the underlying asset being disposed of. In this case, the securitisation is recorded as borrowing. This is another aspect of the full transfer of ownership.

Securitisation: some conclusion.

It is probably out of reach to have a complete view of securitisation, an arrangement that, in addition, is not so widespread for governments.

It is probably enough:

- to provide a good definition of securitisation, especially when it is undertaken by government;
- to explain under which conditions it may lead to record the disposal of an asset by the government unit that is the originator: the asset must pre-exist in the SNA balance sheet of the government unit, there should be a full transfer of ownership of the securitised assets as evidenced by the transfers of the risks and rewards linked to these assets, the transfer of ownership being for the full economic time life of the assets; if not, national accounts record borrowing by the government unit.

2. Detailed comments: Relations of general government with corporations

Privatisation

8. There are two issues that are neither mentioned, nor solved, in this wording, and that have an impact on the general government accounts :

- are the securitised items assets in a national accounts perspective ?
- what is the classification of the securitisation unit, that is deemed to take ownership of the securitised assets in the case there is a change in ownership ? if this unit is classified outside the general government sector, there may be an impact on the net lending/borrowing of the general government, and there is no change in the general government’s liabilities.

§ 22.144 Although, *stricto sensu*, privatisation should mean that the privatised corporation leaves the public sector, the accounting rules applying to the arrangement are the same even if the shares of the involved corporation are only partially sold or if they are sold to another public corporation. The impact on the general government account is identical.

Instead, in limiting privatisation to sales of shares to units being outside the public sector, the wording may be understood to mean that the treatment should be different if the sale was made inside the public sector. Which is wrong.

§ 22.145-146 It should be possible to merge the two paragraphs that deal with issues that are not basically different.

However, despite the fact that the case of non-financial assets is specifically interesting, because of the differentiating impact on B.9, it should be stated that the treatment applies also to the case of financial assets. If some financial assets owned by a public corporation are sold, and the proceeds paid back to government, the operation leads to the recording of a withdrawal of equity. This is important because some of the transferred funds may be “dressed” under dividends.

§ 22.147-b The restructuring unit referred to here seems to belong to the family of holding companies, i.e. units that, according to NACE rev.4, belong to class 6420, as units that own a group of subsidiaries⁹.

Transactions with the central bank

§ 22.155 It is not sure that it is interesting and worthwhile to underline the fact that the central bank is the single exception of a unit having non-market output not classified in the general government sector. This is a remark which, in addition to be anecdotal, is wrong: insofar as institutional units are concerned, all NPISHs have a non-market output while not being classified in the general government sector.

Furthermore, it is not clear what the “because” means: is it because, among other reasons, the output of central banks may be non-market that it is controlled by government ? this would be a strange rationale.

What is missing in this paragraph is two-fold:

- the central bank as a whole is controlled by government by virtue of a specific legislation, in that it carries out tasks having a general policy purpose;
- furthermore, it is relevant, in regard to § 22.156-b, to mention that the ownership of government refers specifically to the management of reserve assets: there is an equity relationship between the government and the central bank with respect to the stock of reserve assets held by the central bank.

§ 22.157 This paragraph is useless in this chapter.

Public-private partnerships

As a whole, the description of PPPs, of the accounting issues they raise and of the treatments to adopt is very clear and adequate. The text is not too much prescriptive, which is happy since things may change.

However, there are three remarks concerning this text:

- the choice, in §§ 22.158-22.159, for a presentation that is supposed to be general is unhappy, and should be changed in favour of a simpler exposition (see below on §§ 22.158-22.159);
- the alternative treatments could be more precisely specified;
- the text could be altered by consideration of the changes that occur in the accountancy profession.

As far as this last point is concerned, it may be recalled that, during the SNA updating process, it was

9. In addition, in chapter 4, there seems to be a misunderstanding about holding companies and head offices. According to explanatory notes of ISIC Rev.4, head offices - class 7010 - seem to be of an establishment-type of unit (the text refers to head offices of enterprises and companies), whereas holding companies - class 6420 - are of an enterprise-type of unit (reference is made to a group of enterprises).

more or less concluded that the position that is reproduced in the present chapter was provisional, but that national accounts would follow the position that could be taken by international organisations of accountants, namely IASB. It happens that the IFRIC has taken a position on similar topics, and that the IFRIC position is generally understood to emphasize the criterion of control. It is the criterion that is shown in § 22.164-b. To follow this interpretation would result, in most cases, to allocate the concerned assets to the balance sheet of the public partner.

Without modifying the general organisation of this topic, nor its conclusions, the chapter could simply indicate that the control criterion may be seen as decisive (by some, for instance).

§ 22.158-22.159 It is not wise, from a pedagogical point of view, to try to make a general and abstract presentation of the PPP arrangements, without specifying who the partners are. It is not easy for a reader to understand who, in § 22.158, is the first unit, who is the second unit, and who are the first and second party in § 22.159. In addition, this line of presentation is no longer followed in §§ 22.162 and following.

It is better to present the topic using the reference situation in which a government unit is the public leg, and a private corporation, or a private producer, is the other leg. In fact, the private side may be many-fold, consisting in a developer, a constructor, a financier, etc. Ultimately, there is a producer of services. With reference to this polar case, other situations may be mentioned, such as when a public corporation is the public leg.

It is not very useful to mention other denominations (BOOTs, PFIs, ...) since "PPP" is now a well-spread and universal terminology.

§ 22.159 It is not clear what the last sentence of § 22.159 means: "*In order to compensate ... for the loss of value of the assets, the first party is allowed to charge above market prices ...*". What is this supposed loss in value ?

- there is actually an issue in the case where:
 - the private partner delivers services the purchaser of which is the government unit itself - 1st case of § 22.162;
 - the private partner is committed to leave ownership on the assets at the end of the contract without compensation, or with a low compensation, although the assets have been maintained in full operational state;
- this means that the operator foregoes a stream of expected operating surplus, although it has undertaken the corresponding capital expenditure;
- in this case, the contractual remuneration may be analysed to be made of two components: a payment for the specific provision of the contractual services, and a payment by the government unit for the acquisition of the assets at the end of the contract;
- however, in this very case, it is not very relevant to mention "market prices", because there is no actual market for such services, even if it is right that the payment is higher than what would be necessary for the only provision of services;
- it is no more relevant to mention a loss of value of the assets, that do not actually suffer any loss.

The case where the private partner provides services that are purchased by the public in general - 2nd case of § 22.162 - is far more complex to analyse. The underlying economic model is not clear.

§ 22.167 Although the general wording of the paragraph is relevant, it may be mentioned that the recording of the way the respective claim and liability build up are sometimes complex.

Once again, it is necessary to differentiate the two cases:

- where it is the public partner that pays for the provision of the services;
- where payments are made by the public in general.

In the first case, it is not completely right to tell that the "*government obtains legal and economic ownership at the end of the contract without an explicit payment*", since it comes from above that the contractual periodic payments have included an element for the acquisition of the assets. However, in this case, if the records are properly made, there is no difficulty to record a claim being built up for the public partner, and to record the extinction of the claim/liability relationship by the transfer of the ownership on the assets.

In the second case, things are less simple, since there is no actual payment from the public partner to the private one. So the building up of the claim of the public partner should be recorded as the counterpart of an imputed kind of property income, relating to a financial instrument that would have a nil value at inception. Or it may be simply analysed as the accumulation of a fiscal claim.

§ 22.168 If the government unit is assessed to be the economic owner of the assets, it is also necessary to reflect the fact that the assets are put at the disposal of the private partner in order for the latter to operate the assets in the context of the provision of the services, since it is actually the private partner that provides the services.

This may be achieved by recording an operating lease, where government is the lessor. Which implies a complete reconstruction of the observed flows.