Report of the

Expert Group Meeting on Public Sector Accounts

Washington, January 25-29, 1988

Bureau of Statistics

International Monetary Fund

Expert Group Meeting on Public Sector Accounts,
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Introduction

The meeting was opened by Mr. Dannemann, Director of the IMF Bureau of Statistics, who encouraged efforts to harmonize the Government Finance Statistics (GFS) and System of National Accounts (SNA) data systems to the extent possible to facilitate the work of policy¯makers and other users of statistics. Mr. Lutzel, of Germany, was nominated and appointed Chairman of the meeting. Participants were informed that, as part of the program to revise the SNA, the meeting was organized in an effort to find clarifications on many outstanding issues affecting public sector accounts. An important issue would be the harmonization of other statistical systems with the SNA as far as possible.

I. Conceptual and Data Links Between SNA and GFS

A. Structural relationships

1. Objectives 1/ 2/

The first questions posed concerned the types of data on government needed by GFS to guide IMF and member countries in their fiscal and financial policies and the types of data needed by SNA for the construction of national accounts, and the extent to which concepts serving the different objectives inherent in both systems could be harmonized and reconciled.

GFS data were developed to meet the need for measuring government in a format which could be useful for analyzing the financial and macroeconomic implications of government operations. A useful point of view taken in this regard was to measure government differently from the market sector of the economy because the motivations for government behavior, largely nonmarket and political in nature, were different from those governing the market oriented sectors of the economy. To do so, a functional classification of government and other sectors of the economy was adopted. In general, this functional definition or classification is an important aspect of Fund statistics. Another is that the statistics have

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1/ Discussion Paper (pp. 4, 5), Conclusions and Recommendations (p. 1).

2/ References made in this report to page numbers in the Discussion Paper correspond to pages in an expanded version of that paper which includes relevant materials distributed as addenda during the meeting.

to be verifiable. There cannot be imputations, which are not verifiable, and the numbers have to come out of the accounting system, generally on a payment basis. Reflecting the different motivation of government, Fund statistics on government embrace analytical concepts which depart from those in analysis applicable to other sectors. The most outstanding of these is the counting of lending with spending rather than with borrowing, because governments, to a varying degree, lend to promote public policy purposes. Therefore the key variable, the overall deficit/surplus, is calculated after including with spending the lending undertaken by government for public policy purposes. There are many concepts of government which are not of primary concern to this type of analysis. Fund missions do not try to make an estimate of the government's physical output; there is no special interest in government consumption as opposed to government transfer payments as an operating concept, and no attempt to calculate the net worth of government.

In contrast, in the SNA, the concepts of government product, value added and government consumption are very important. Accruals data are necessary to measure production and the distribution of income and estimates are necessary in order to arrive at several meaningful concepts. Furthermore, as a system that looks at all sectors of the economy, there is the necessity of maintaining symmetrical treatment of the activity being measured so that the statistical data for government can be aggregated with those for the rest of the economy.

These differences in objectives, however, allow certain opportunities for harmonization and reconciliation. Concepts of no importance in one system need not be reconciled when they are not a part of the other system. On the other hand, concepts that are very close, like the distinction between the concepts of current and capital in GFS, which parallel those in the SNA, may be discussed for possible reconciliation. Furthermore, where asymmetrical views of the same transactions arise, some systematic approach may be sought to the question of how to reconcile the two views in a system which looks at one sector and a system that looks at all sectors.

As part of the efforts to harmonize GFS and SNA, the United Nations Statistical Office (UNSO) and IMF undertook joint case studies of ten countries to examine what was being done in practice in measuring GFS and SNA. In a number of cases, neither system followed the rules that were being set down; in others, certain shortcuts and departures were made in practice for both systems.

In the ensuing discussion, participants expressed different views regarding the extent and nature of the differences between the GFS system and the SNA. One view was that there could have been far fewer differences if the starting point for the development of GFS had been the SNA, since many GFS aggregates were derivable as alternative concepts within the SNA. It was stated that the European Community (EC) had undertaken an exercise to create what was called the "budgetary presentation" from national accounts data on government with relatively few reclassifications, imputations and reroutings of data.

A different view was that the procedure for compilation could not obviate the conceptual differences deriving from the different objectives of both systems. While in some EC countries the national accounts were so well developed that government finance statistics could come out of the same compilation process, this was not the case elsewhere. In most other countries of the world, GFS correspondents had to draw data together from various national sources and make the necessary adjustments so that data in the standardized, internationally comparable format of the Government Finance Statistics Yearbook could be obtained. As a result of these efforts, the data published in the GFS Yearbook for 134 countries had been used by the UNSO for the development of national accounts in developing countries and for comparison with national accounts in both industrial and developing countries.

Differing views were expressed regarding the relative importance of each system for the economic analysis of government operations. One participant thought that the GFS system was focused primarily on the short-term analysis of government operations while the SNA provided a more general and complete framework allowing both short- and long-term economic analysis. While useful as a short-term framework, the GFS system, in this view, left out important issues of longer term structural analysis of government, such as analysis of government output, wealth, accumulation of assets and allocation of resources. Other participants argued that the reverse was true, particularly if one studied public finance literature, where GFS concepts were selected for use, for example, in economic analyses of tax reform and the effects of taxation on the labor supply. In the OECD Committee on Fiscal Affairs project on tax classification, problems were encountered with SNA figures because of their accrual basis and insufficient clarity on the distinctions between tax and nontax categories and between direct and indirect taxes. Moreover, since OECD revenue statistics went back to 1955 and GFS data had been published back to 1970, it was not accurate to argue that the GFS system was useful only for short-term analysis. Analysis of these data revealed important trends, movements and variations.

It was further pointed out that the difference in the analytical focus of GFS and SNA was not one of short- or long-term analysis but of statistics for one sector in contrast to statistics for all sectors. GFS are the sectoral statistics of government and constitute the language of government and of public debate about government in the economy. Discussion of government and fiscal policy is generally in terms of revenue and expenditure, the deficit and government borrowing. These concepts are not **explicity included** in the *SNA*, which measures **government product**, **government** value added, government consumption, government capital formation and government net lending or the change in government net worth. This provides an analysis of the government sector in terms comparable to the analysis of other sectors of the economy as a whole but not in terms of the specific analytical needs of the government sector in itself. Because of the different nature of the government sector, there is no concern in GFS for the government's asset position as a reflection of the government's wealth. GFS focuses on the breakdown between current and capital expenditures, the mix of total expenditures between transfers, wages and salaries, interest payments, and purchases, and the extent and nature of tax collection, in order to promote optimum development of the national economy.

There was general support among participants to harmonize concepts in **both** systems to the extent possible to bring the two systems closer together. However, the issue of harmonization generated discussions regarding the proper approach. Questions were raised regarding the status of one system **vis-A-vis** the other. One view expressed was that harmonization should proceed to establish the GFS system as a complementary system to the more general framework of the SNA.

An alternative view towards harmonization posed a number of questions on the appropriate relations between the two systems existing separately. Should GFS try to include in its framework all measurements for government currently undertaken in the SNA, including certain imputations, depreciation estimates, measurements of consumption and capital formation beyond what normally were available in government accounts? Should the SNA try to include all of the cash concepts of GFS though they do not correspond to the accrual basis of the *SNA?* Or, should the two different systems be delineated, underlining their relationships without attempting to have in each system concepts foreign to its basic principles?- A proper delineation of similarities and differences could establish harmonization procedures that could encourage cooperative sequential divisions of labor between GFS and SNA compilers whenever warranted. GFS compilers could compile government finance statistics from government accounts, which would then, with further imputations and adjustments, be converted into *SNA* statistics.

The group concluded that for the analysis of the government sector, both the System of National Accounts and the Government Finance Statistics System are useful and mutually supportive. Though it is not proposed that the two systems be altered in such a way that one provides all the information that is needed in the other, a major concern of the group is to find out whether it is possible to have additional information in the SNA or in GFS in order to harmonize the two systems to the extent possible.

2. Changes to facilitate reconciliation 1/

Following a brief description of the GFS analytical framework, illustrated graphically in Charts 1, 2 and 3 of Background Document No. 2 1/, some of the basic concepts in the GFS system were also mentioned: (i) Gross measurement of government payments and receipts. (ii) Distinction between current and capital transactions (as in SNA). **(iii)** Classification of transactions by the nature of what flows in the opposite direction. (iv) Division of flows in exchange for others' liabilities to government between those undertaken for public policy purposes and those for the management of government liquidity. (v) Balancing of the analytical framework by the change in cash balances.

Charts 4 and 5 of this background paper, which show a number of SNA components superimposed upon the GFS analytical framework, were used to illustrate some of the differences between the GFS system and the SNA, as follows:

(a) GFS are organized into a single balanced account, in contrast to the several accounts utilized in SNA. (b) The classification of taxes differs, for example, the classification of estate and gift taxes as capital transfers in SNA but as taxes and current revenue in GFS. (c) **Balancing concepts differ** in GFS **and SNA.** (d) There is a **need** to **impute** transactions in **SNA,** while GFS in general **avoids** the **imputation** of transactions. (e) There are differences in perception of some transactions, for example, those involving rerouting in SNA. (f) SNA adopts the accrual basis, while GFS are compiled primarily on a cash basis. (g) There are different consolidation rules.

It was agreed that there is a need to reconcile differences between both systems. A number of topics to be discussed during the meeting related to the harmonization of both systems: (1) Tax classification, (2) Social security funds sectorization, (3) Supranational authorities, (4) Debt cancellation as transfers, and (5) Monetary authorities sectorization.

Some of the other questions that were to be discussed during the week were mentioned briefly, such as the depreciation of government fixed assets, imputations and reroutings, etc., but these are SNA problems not directly related to the GFS system.

1/ Discussion Paper (p. 6), Background Document No. 2, "Overall relationship between Government Finance Statistics and the System of National Accounts," Conclusions and Recommendations (p. 1).

3. Small conceptual differences 1/

A number of questions were raised about the use of bridge tables to link the GFS and SNA systems:

(i) Is it fruitful or detrimental to have a detailed bridge table to delineate interrelationships between both systems?

(ii) In the past, these bridge tables have been used in a few countries to obtain SNA government accounts from GFS data; should this continue to be done in countries where SNA are not available even if it is not complete?

(iii) What should be done about small conceptual differences between both systems which remain after conceptual reconciliation efforts?

The use of detailed bridge tables for describing the link between SNA and GFS was favored by several participants and was considered especially useful in a number of countries that have GFS data but not SNA.

At the UNSO, officials have been working with bridge tables in an effort to link both systems. This has been very complex work because of many small differences between both systems. They have established operational bridge tables, i.e., bridge tables with figures, in some countries to convert from GFS to SNA; these bridge tables vary somewhat from country to country.

Background Document No. 3 1/ describes, as an example, the sequential procedure used for the Netherlands; it involves the following steps:

(1) Use of GFS data (on a cash basis) and for subsequent conversion to an accrual basis. (2) Conversion through operational bridge tables. (3) Adjustments for transactions in kind, etc. (different from country to country).

There are two uses for applying this technique:

(a) If a country has GFS and SNA data available, then the sequential procedure can be used to compare them and improve them. (b) If GFS data are available, but not SNA data, then SNA government accounts could be derived from GFS.

1/ Discussion Paper (p. 7), Background Document No. 3 "Derivation of SNA Value from GFS Data," Conclusions and Recommendations (p. 1).

In the UNSO, this exercise has been carried out also for Venezuela and efforts are currently being made for Mexico.

The meeting was concluded that it is difficult to give general recommendations on how to handle apparently minor conceptual differences between the GFS and the SNA, since differences may be large in one country and small in another. Conceptual bridge tables should show such differences.

B. Data links 1/

It was explained that originally the idea of using GFS-SNA bridge tables was with the purpose of **identifying conceptual differences between** GFS and SNA in order to explain them to users. However, the emphasis has shifted to establishing data links not only to identify conceptual differences but to obtain an approximation of SNA data. Bridge tables are now being used at the UNSO for that purpose.

Participants from other institutions and from different countries agreed that the sequential compilation procedure leading from government accounts, to GFS, to SNA, is **very** useful and should be applied. It was also agreed that bridge tables are very useful even if they cannot be completely filled out with numbers. However, the work of preparing a bridge table should be done by GFS and SNA people jointly in each country.

A question was raised as to how to go from a cash to an accrual basis. This is one of the difficult steps in the sequential procedure. It was also mentioned that for countries with high inflation, the use of accrual or cash basis can make a big difference. It cannot be said that cash basis or accrual basis is better than the other, but rather that they are complementary.

Some of the participants at the meeting work in offices which are responsible for preparing both GFS **and SNA. They found** the recommendation for using bridge tables to be very reasonable and acceptable and they believe these tables will help improve the information for both systems.

A distinction was also made between countries, particularly OECD countries, that may have facilities and resources to develop both GFS and SNA systems and establish a bridge between them, and other countries, where resources and information are scarce; in these countries, if GFS data are available, the SNA people can use them to obtain approximate SNA accounts for governments.

1/ Discussion Paper (p. 8), Background Document No. 3 "Derivation of SNA Value from GFS Data," Conclusions and Recommendations (p. 1).

It was concluded that bridge tables are very useful both for the users and producers of data. They could be used to identify conceptual differences between SNA and GFS in conceptual bridge tables, and can also show differences in figures and the reasons for these differences in operational bridge tables.

It is also very important that compilers of GFS and SNA talk to each other.

In those countries where no sector accounts for the general government are available within the national accounts, the GFS data and the operational bridge tables may serve as a first step in preparing estimates for the general government in the SNA.

II. Transactor Coverage

A. Borderline of general government

1. Nonfinancial enterprises/establishments

(a) Departmental enterprises/dual sectoring 1/

Departmental enterprises are government owned unincorporated units, (establishment type as defined in SNA), which are mainly engaged in selling goods and services at prices designed to cover the costs of production to the general public or in providing goods and services to other units of general government (as ancillary units). Some of the issues relating to departmental enterprises arise from the contrasting measurement of the output of the producers of government services and of industries. Both the SNA and GFS classify government owned industries in the nonfinancial public enterprise (NFPE) sector when their sales to the public are large and they are incorporated. There is no difference between both systems in this respect. Both systems classify unincorporated industries with only small sales to the public within the government sector and measure their activities using a different methodology from that applied to other government activities. The SNA production account for industries in government is based on the market value of sales, like the production account for enterprises outside government. In contrast, the SNA production account for producers of government services is based on inputs, because there are no market sales and there is not a precise way of measuring the value of output. Output is therefore assumed to be equal to input for the producers. of government services.

1/ Discussion Paper (pp. 9-11), Conclusions and Recommendations (pp. 1, 2).

Because the expenditures of departmental enterprises are used to produce goods that can then be sold, it is important not to classify their expenditures with the inputs for the production of government services. Similarly, on the receipt side, the sales proceeds of departmental enterprises, which must be used to meet production costs, should not be added to government revenues, which generally constitute disposable income for the government. What is done in GFS is to net the proceeds of departmental enterprises' sales to the public against their corresponding production costs and add only the net operating surplus or the net operating deficit to government receipts or expenditures, respectively, for classification by purpose or by other characteristics. Nonoperating receipts and expenditures of departmental enterprises are combined in their entirety with other government operations in GFS. Incidental sales of government are treated on a gross basis in GFS and SNA, since their costs cannot be identified.

Reservations were expressed with regard to the concept of small sales and large sales to the public as a criterion for classifying enterprises as inside or outside government, since a definition of small and large scale sales is not provided. There is a reluctance to apply this concept, which remains vague, and would differ in application to local or central governments.

While the principal question before the group was whether departmental enterprises should be kept within government or moved to the *NFPE* sector, it is regarded important for both *GFS* and SNA that, in either case, some mechanism remain for separating or netting the enterprise activities that are found in the government accounts from the activities of producers of government services.

It was the view of the group that a departmental enterprise is a goverment-owned enterprise which does not have a complete set of accounts and autonomy of decision-making but for which separate production account data are available. For the production account, therefore, a departmental enterprise should be treated as a market establishment with the operating surplus or deficit derived in that account being transferred to the income and outlay account of government. For the purposes of the income and outlay and capital finance accounts, the departmental enterprise should be treated as a part of a larger institutional unit of government and not as a nonfinancial public enterprise. The calculation in SNA provides a kind of netting parallel to that required by *GFS*. Incidental sales by government are to be treated without separation from the producer of government services. The group decided against the alternative of treating departmental enterprises as producers of government services.

One participant remarked that under the treatment adopted, operating deficits of departmental enterprises would imply the payment of a subsidy from the government to itself. It was explained that such a subsidy would be from the government to a market establishment of government. It was agreed that the distinction between market and nonmarket activities will be further discussed during the next Expert Group Meeting on Input-Output and Production Accounts. Also the treatment of operating deficits or surpluses of the departmental enterprises was to be further discussed later during this meeting (Agenda topic V.B.2).

The Expert Group agreed that departmental enterprises have accounting data for the production costs and sales income but do not have a full set of accounts; however, the scale of activities should no longer be a criterion for defining departmental enterprises in the next version of the SNA. It was therefore agreed that **departmental enterprises should** be **separated** from **producers** of nonmarket **government services** in the **analysis** of **production**, but not in the sector accounts.

(b) **Ancillary enterprises** 1/

The group discussed the valuation of the output and the coverage of ancillary enterprises which produce primarily for other units of government, and provide their output to other units of government at either nominal prices or no charge. There was concern on the one hand that such units' **output would be undervalued** if **measured** by sales price. This led to a proposal that such units be classified as producers of government services so that their output would be valued as the cost of inputs. There was concern, on the other hand, over classification of the same types of production, i.e., the government printer, as a market establishment in countries where the output is sold to other government units and as a producer of government services in countries where the output is provided to other government units at either a nominal charge or no charge. Two approaches were discussed to overcome these problems. One approach would establish a list of types of activities undertaken by ancillary enterprises which, for the sake of uniformity, should be classified as market establishments in all countries regardless of the level of charges to other units of government. There was a suggestion that such a list could be based on ISIC categories and discussion as to whether such a list of market establishments would be restricted to production of goods or could include services as well.

The other approach--referred to as the market-nonmarket solution--would classify as market establishments only those units which produce for other units of government at a level of charges designed to cover the major

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1/ Discussion Paper (pp. 12, 13), Conclusions and Recommendations (p. 2).

part of the costs of production. A vote taken indicated that the majority of the group preferred the market-nonmarket solution rather than the establishment of a list. Preference was also expressed for valuation at actual prices, of sale of market establishments and of inputs for nonmarket establishments, rather than at the price of parallel products in the market. A final determination of the basis for classifying units as ancillary enterprises, however, was referred to the subsequent Expert Group Meeting on Input-Output and Production Accounts. It was also recommended that in view of other uses of the term "ancillary," the appropriateness of the term "ancillary" to units providing goods and services to other parts of government be examined.

(c) Community production of services and capital goods 1/

The group was asked to consider whether the production of capital assets constructed on a communal basis for which the government has the **responsibility** for maintenance and repair should be attributed to government in the SNA. This question does not arise in GFS because in GFS the transactions are shown on a cash basis.

The group considered the following situations: 1) The community--through a nonprofit institution serving households--produces the capital assets and maintains them, and 2) The community produces the capital assets and, because of lack of resources, the government undertakes their maintenance. In the second case, should the SNA include an imputation to transfer the capital asset to the government? Two further questions remain: (i) a timing problem between the date of production of the capital assets and the date at which the government undertakes responsibility for their upkeep, and (ii) how the upkeep of the assets should be evaluated.

One participant indicated that unless the government is involved in upkeep, there would be no way to know about the production of the capital assets by the community. It was indicated that when the government maintains and repairs the capital assets, the government expenditures could be classified in SNA as current transfers to private nonprofit institutions.

The group agreed that structures produced on a communal basis should be treated as production and fixed capital formation of nonprofit institutions serving households. If the government will provide maintenance and repair of the structure, and if the ownership is not clearly retained by the nonprofit institutions serving households, then these assets should be transferred to the governnment balance sheet through the reconciliation account. The group did not discuss the treatment of services, as distinct from fixed capital assets, produced by the community.

1/ Discussion Paper (p. 14), Conclusions and Recommendations (p. 2).

2. Financial Institutions

(a) Monetary authorities functions and acceptance of deposit liabilities 1/

The group discussed possible means of reflecting in the SNA the treatment of monetary authorities functions in GFS and other Fund statistics undertaken to permit the basic distinction between monetary policy and fiscal policy. The IMF has over the last 40 years tried to make this distinction in the data being published and in the analysis of these data. It was explained that there are institutions in government which perform monetary functions; i.e., parts of the monetary policy are undertaken by government institutions. Such functions are treated in the Fund's GFS and financial statistics as carried out not by the government but by the monetary authorities subsector which includes also the operations of the central bank.

The question was raised whether the flows to or from government resulting from the performance of monetary authorities functions should be rerouted in the SNA and shown as government inflows from or outflows to the financial institutions sector.

An analogy was made with other parts of the SNA system, where a number of reroutings of transaction flows are carried out for analytical purposes; for example, employer contributions to social security or pension schemes which are rerouted through households. It was further explained that the GFS system tries to identify transactions in government that deal with monetary policy (and not fiscal policy) and in order to be consistent with this distinction, these transactions are treated separately, i.e., they are rerouted and shown in the monetary sector. This does not violate the integrity of the institutions. A recommendation was made that the SNA system should consider this treatment, to avoid the need to redesign money and banking statistics to cover the banking activities of government.

It was also explained that there are many countries in the world where the Treasury Department carries out monetary functions.

It was noted that the November 1987 Meeting of the European Communities Working Group on National Accounts recommended that where monetary authorities functions were carried by parts of government which are not separate institutional units, they should remain in the general government sector in national accounts. It was pointed out that the proposed rerouting would not separate such operations from the general government sector but simply reroute the transactions through the monetary authorities subsector.

1/ Discussion Paper (p. 15), Conclusions and Recommendations (p. 3).

A reference was made to Table 25 in the SNA (p. 201), "Financial Transactions in the Monetary System," which includes transactions of the Central Bank, other monetary authorities and the monetary functions of the Treasury, with the suggestion that this table might meet the data and analytical requirements. It was stated, however, that this table had been in place for 20 years **and** had not been found by the IMF to provide a satisfactory solution.

It was agreed that what is needed is to identify separately the transactions of the government sector in the SNA, and that this does not imply a split of the institutions. Where government agencies carrying out monetary authorities functions are not separate institutional units, they must remain part of the government sector. The group concluded that to meet the needs of both fiscal and monetary policy and to provide links to **GFS and money and banking** statistics, it will **be necessary** to **introduce appropriate sub-divisions** of the SNA transactions classification and a complementary presentation. The outlines of the subdivisions and complementary presentation should be taken up by the Expert Group on Financial Accounts and Balance Sheets.

(b) Government employee pension schemes 1/

The question was raised as to whether government employee pension funds invested with the employer government should form part of the government or of the financial institutions sector.

It was explained that the SNA separates out from the pension fund subsector all the pension funds invested exclusively with the employers. This classification is also followed in GFS.

However, because prudence or legal requirements lead many private pension funds to invest in government securities, the rationale for classifying such government employee pension funds within the employer government does not apply. Consequently, in the case of government employee pension funds, it was proposed that these should be classified in the pension fund subsector of the financial institutions sector. This would permit the analysis of government employee pension funds which can best be provided in the context of pension funds and insurance companies. The analysis would be independent of whether reserves are invested entirely with the securities of the employer government. The group agreed to this proposal and concluded that the fact that a government employee pension fund is invested in government securities is not a sufficient justification for including it in the government sector rather than in the financial institutions sector.

1/ Discussion Paper (p. 16), Conclusions and Recommendations (p. 3).

(c) Government employee welfare funds and unfunded welfare and pension schemes 1/

It was explained that there are three types of schemes: unfunded government employee pension schemes, unfunded government employee welfare schemes, and funded government employee welfare funds. The question was raised as to whether these three categories of schemes should be considered as social security schemes, with their contributions and benefits classified as social security contributions and benefits.

The SNA for the government sector calls for separate treatment of these schemes from the social security schemes. However, in practice it has been found that the SNA distinction was not being followed in many . countries, as national accountants found it difficult to make the distinction. Because the government's role as employer and as provider of social security overlaps in many cases, many such schemes are considered a part of social security or indistinguishable from it. This proposal for simplification was justified, therefore, from both a theoretical and practical point of view. It would bring no change in the total of employee and employer contributions and of benefits registered in the SNA for the government sector. An additional benefit is that there would not be any need for imputations of service charges for these three schemes. The proposal does not affect the institutional classification but rather the transaction classification.

The group agreed that the three schemes mentioned above should continue to be classified in the employer (government) sector. However, contributions and benefits should be classified as social security contributions and benefits.

3. Nonprofit institutions 2/

The group was asked to discuss an aspect of an issue covered by the Household Sector Meeting, which determined that the criteria to determine where to include private nonprofit institutions should be which sector the nonprofit institutions (NPI) serve.

For this meeting, the question raised was whether the government sector should include nonprofit institutions serving either households or enterprises with majority financing and control by.government. The discussion centered on the two criteria of financing and control.

1/ Discussion Paper (pp. 17, 18), Conclusions and Recommendations (p. 3).

2/ Discussion Paper (pp. 19, 20), Conclusions and Recommendations (p. 3).

It was stated that in both the GFS system and the present SNA, NPI are included in government only if they are both majority-financed and controlled by government, that is, if both criteria are met.

It was mentioned that in Finland there is a nonprofit institutions (NPI) sector separate from government and that the national accountants would like to keep that separation. The NPI sector in Finland includes churches, some of which are funded by government but have independent activities. It was mentioned that in Norway, where priests are paid by government, the churches are included in the government sector; however, it was recognized that it is a problem to determine, in the case of churches, if they are part of government and are in fact financed and controlled by government. Circumstances in the **individual** countries would determine whether churches met the criteria and should or should not be included in government.

The question was raised on how to classify NPI that are only financed or controlled by government. It was stated that if only one of the criteria is met, then the NPI should be considered private and classified according to the sector they serve.

It was stated that there appeared to be inconsistencies between countries in their definitions of finance and control. The criterion for finance **probably** differs in developing and developed countries. A suggestion was made that the SNA should provide some guidance in order to interpret these terms. At present, the countries have to make the interpretation themselves.

A question was also raised about the treatment of political parties. In Congo, the party, which receives about 95 percent of financing from government, is considered as part of government.

The group therefore agreed that the criteria for including NPI in government are that they are both majority financed and controlled by government. Private institutions (outside government) are allocated according to the sector they serve. NPI serving enterprises should be shown in the corporate enterprise sector even if they serve unincorporated enterprises. It was recommended that the revised SNA provide a further explanation of control.

4. International organizations

(a) Supranational authorities 1/

The SNA differs from the GFS in that the GFS defines supranational authorities as international organizations which are empowered to levy taxes within countries. The only supranational authorities which exist at the moment is the European Community. To give a complete measurement of overall government activities as regards taxes and expenditures, GFS includes governmental functions assigned to supranational authorities within statistics for government, by showing explicitly, unconsolidated data for the non-headquarters operations of supranational authorities within a country, and also data consolidated with the rest of national government of that country. GFS presents the consolidated data as data for general government, which therefore is defined to encompass both the national government and a non-resident sub-sector, the supranational authorities.

The SNA does not discuss supranational authorities but stipulates that: "International bodies, such as political, administrative, economic, social or financial institutions, in which members are governments, are not considered residents of the country in which they are located or operate." General government in the SNA does not include non-resident units.

The group discussed whether general government in the SNA should include, as a non-resident subsector, the non-headquarters operations within the country of supranational authorities.

It was agreed that supranational authorities should be discussed in general terms because of the possibility that other supranational authorities, i.e., other than the European Communities, might be created in the future. Several participants expressed reservations about the extension of the term general government to include a non-resident subsector. Several clarifications were offered on the GFS treatment. It was pointed out that the overall deficit/surplus of supranational authorities is always defined to be zero by having a balancing item which consists of net flows to or from headquarters. The GFS treatment implies no conflict with balance of payments statistics since data for supranational authorities are identified as those of a non-resident subsector and are shown separately under GFS. The advantage of the GFS treatment was seen to be the inclusion of all governmental activities, such as taxes and expenditures, within one overall total for government.

1/ Discussion Paper (pp. 21-23), Conclusions and Recommendations (p. 3).

The group decided that in the SNA, the term general government should be restricted to resident units and that supranational authorities should be separately identified as a subsector of the rest of the world. It was agreed that the combination of general government plus the transactions of supranational authorities in the country would be useful and it was suggested that a separate term for this combination be found.

(b) Other international organizations 1/

Participants in the Expert Group Meeting on External Sector Transactions concluded that, for completeness and symmetry of national accounts, an additional unit embracing international organizations classified as non-resident everywhere they operate should be defined and measured through the compilation and consolidation of data on their activities. Such international organizations were defined to include organizations that meet three criteria:

(a) Authority derived directly from the authority of the organization's members, which may be independent states or international organizations;

(b) sovereign status, i.e., the laws and regulations of the country or countries in which it is located do not apply to the international organization;

(c) production of services which are primarily nonmarket services.

The proposal was that data on operations of all international organizations excluded as nonresident from all countries' national accounts be aggregated as an additional unit to complete the universe of national accounts.

It was pointed out that the proposal for international organizations was different from that for supranational authorities in that data need to be prepared for supranational authorities' operations in each country, whereas the accounts to be prepared for international organizations would cover their operations throughout the world. It was also noted that while the proposal would not change the present SNA treatment of international organizations, in that transfers to and from international organizations already appear in the rest of the world accounts, data would also become available for international organizations' production.

The group agreed that it would be desirable to compile full economic accounts for international organizations in total.

1/ Discussion Paper (p. 24), Conclusions and Recommendations (p. 3).

B. Borderlines within general government

1. Central, state, local and other government levels 1/

The topic discussed was whether it would be useful to present data in **SNA** for the state, provincial or regional level of government, for countries where they operate as a level of government, separate from central and from local governments.

Data for state, **provincial**, or regional governments are published in the *GFS* Yearbook for about 22 countries. This level of government is defined in the *GFS* Manual Section I.D., as comprising "governmental units exercising a competence **independently** of central government in a part of a country's territory encompassing a number of smaller localities, that is, occupying an intermediate position between the central government and **independent** local **governments** that **may** exist."

The **1968 SNA** distinguishes only between central **government and** local **governments; however**, the **revised** UN—SNA questionnaire distinguishes a separate intermediate level of government, where it exists, between central and local governments.

The main benefit of separating state from local government data, where state governments exist, is that it allows a better understanding of the relations between the different levels of general government and of the financial flows between them. The role of a separate level of regional government in such flows may be particularly significant, justifying separate measurement. The separation of an intermediate level of government raises no difficulties in consolidating the different components of general government.

It was generally agreed that this was a useful proposal and discussion centered on issues arising in its implementation.

Different criteria are presently being used to decide whether such a level of government exists. The criteria cited by the discussion paper, drawing on the *GFS* Manual, is that "a government may be considered to have substantial autonomy when it has the power to raise a substantial portion of its revenue from sources it controls and its officers are independent of external administrative control in the actual operation of the unit's activities," (see p. 14 of the *GFS* Manual). While the OECD follows the same criteria as the IMF, in fact it reports intermediate level revenues only for the **six** OECD countries with a federal structure. It was suggested that both control of revenue and a federal structure may be too

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1/ Discussion Paper (pp. 25, 26), Conclusions and Recommendations (p. 4).

restrictive. The November 1987 meeting of the EC Working Group on National Accounts discussing this point examined an alternative criteria of the existence of a state parliament and state ministries, but reached no conclusion. It was suggested that this would restrict the intermediate level to federal countries, which would be too limited. A number of countries, among them Spain and Italy, are assigning greater importance to regional governments without calling it a federal structure. It was also stated that control of revenue need not be limited to tax revenue, since nontax revenue and block grants might also be significant. Besides control of revenue, moreover, attention should also be paid to control of expenditures.

It was pointed out that the criteria cited in the discussion paper did not fully represent the list of criteria set out in the GFS Manual (on page 14). It was agreed, therefore, that a full list of criteria like that in the GFS Manual would be useful to countries in deciding whether to report a separate, regional level of government. It was felt that the question of the existence of an autonomous regional government level was not only an economic question but also a political question, and that the decision as to whether to report data for such a level separately should be left up to the individual countries with the guidance of a list of criteria the SNA considered significant.

There was also a suggestion that perhaps it would be useful to have in the SNA a more refined classification of government units by regional groupings and the functions they exert. However, it was decided that this point should be discussed under the heading of statistical units.

The group agreed that it would be useful to introduce intermediate levels of government between central and local governments as an additional level of government for countries where this extra breakdown would be meaningful. The group noted that the GFS Manual contained helpful guidelines for identifying this additional level.

2. Social security funds 1/

Under the present SNA all social security funds are combined into a single subsector of government separate from the central government and local government subsectors. Under the GFS, however, social security funds do not form a separate subsector and are consolidated within the level of government at which they operate, though separate data on their operations are presented. It was demonstrated in the discussion paper and background

1/ Discussion Paper (pp. 27, 28), Background Document No. 4, "Sectorization of Social Security Funds," Conclusions and Recommendations (p. 4).

paper, and agreed upon during the meeting, that social security funds have lost a great deal of their financial independence and have been integrated more closely with government over the past two decades. It was felt, however, that to help maintain the integrity of social security funds and reassure contributors, it was important to continue to maintain separate statistics on operations of social security funds. It was stated, on the other hand, that presentation of data for central government excluding social security funds operating at the national level--amounting to only 56 percent of the combined total in France and 45 percent in Germany--would fail to meet the needs of users like the IMF requiring a measure of central fiscal policy. For some SNA users central government including social security funds would be of lesser interest, as intercountry comparisons were usually made at the general government level and production and consumption analysis might proceed by separating social security funds. Country practice differed markedly, with political discussion focussing on budgetary and social security fund operations separately in France and Germany, for instance, but together in the United States.

Against this background, there was complete agreement in the group that full information should be provided permitting cross-classification of social security funds by level of government so that they could be consolidated with either the level of government at which they operate or with social security funds at other levels. There was disagreement, however, as to which configuration of the data should come first in the hierarchy of presentation, as it was stated that some national publications were likely to present only the aggregates at the first level below general government. Most of the discussion centered on the hierarchy of presentation, therefore, some participants favoring consolidation of all social security funds first, others favoring consolidation of social security funds within each level of government first. There were objections to a compromise presentation including both central government, consolidated social security funds, and a combination of the two, on grounds that where social security funds existed also at other levels of government the combination would misrepresent decisions taken at the central government level. Another suggestion called for separate presentation of the social security fund and non-social security fund components of each level of government. It was stated that with sectorization, as with other aspects of SNA, a hierarchical arrangement should permit compilers to present more aggregate concepts in the event of the lack or insignificance of detail. There was also a suggestion that different configurations of the components might be preferred by different users and different countries.

The group concluded that harmonization of the GFS and SNA on sectorization of social security funds was desirable, that cross-classification of social security funds and levels of government to permit meeting both needs was essential, and that further consultation with users was necessary before determining which hierarchy of presentation should be preferred.

C. Public sector

1. Ownership, control

(a) Ownership and/or control 1/

Because of their special relationship with government, public **enterprises may be subject** to **different** influences **and motivations** than private enterprises, so that their analysis in a separate public enterprise grouping may serve to delineate separate patterns of behavior. The present SNA proposes that the criterion for **distinguishing between** public **and private** enterprises **should be** ownership **and/or** control but this criterion has been criticized for lack of clarity: does "and/or" mean "and" and "or," and how is control to be defined?

In 1984, the OECD Secretariat proposed that the next SNA should give four necessary conditions for classifying an enterprise as public:

(i) it is owned by government
(ii) it is controlled by government
(iii) it is large
(iv) it is intended that the enterprise will be retained in public ownership on a more or less permanent basis.

The question posed was whether the revised SNA should retain the present ownership and/or control criteria or adopt some new formulation.

In the ensuing discussion, participants agreed that the size criteria and intended permanent public ownership should not be taken into account. It was stated that the purpose of the criteria was to group enterprises which exhibit a pattern of economic behavior reflecting the influence of their special relationship to government and that this should be explained in the SNA. Others felt that the setting out of the criteria in the SNA **would avoid possible confusion.** It was stressed that clarity of interpretation of the criteria should be important and that the term and/or should be avoided.

The group agreed to treat as public corporate enterprises those in which the government owns the majority of the equity and those in which it exercises control over the enterprises' economic behavior even if it holds 50 percent or less of the equity.

1/ Discussion Paper (pp. 29-31), Conclusions and Recommendations (p. 4).

(b) Majority ownership 1/

The question posed here was whether government majority ownership should be defined to include units in which majority ownership is held not directly by the government but by a unit in which the government holds **majority** ownership.

The group decided that enterprises in which the majority of the equity is held either by the government or by other enterprises in which the government holds more than 50 percent of the equity should be treated as public enterprises.

2. Accounts and tables for nonfinancial public enterprises and public financial institutions 2/

The present **SNA** does not provide for a public/private split in the main accounts of the system although it does recommend a **public/private breakdown** in two supporting tables: Domestic Factor Incomes According to Kind of Activity and Institutional Sector of Origin (Table 17) and Capital Transactions of the Private and Public Institutions (Table 19). The question posed was whether the next **SNA should** provide for a **public/private** breakdown in the accounts or supporting tables. It was stated that such information was in widespread **public demand** and **would** be useful for **analysis carried** out, for example, **by** the World Bank.

The group agreed that a full set of accounts should be prepared for public enterprises (including both financial and nonfinancial enterprises). Because in some countries the compilation of detail might not be carried to the third or fourth levels, to have a public sector concept it would be necessary to make the public/private breakdown at the second level, immediately after making the subdivision between nonfinancial enterprises and financial institutions.

3. Nonfinancial public sector, **nonmonetary public** sector 3/

The **present SNA recommends** that in countries where the **public authorities play a particularly important role in the economy, it may be** useful to prepare accounts for the "Public Sector" consisting of general government plus nonfinancial public enterprises and public financial institutions. In order to ensure that certain important transactions such as central bank financing of general government and nonfinancial public enterprises are not eliminated in consolidation, the GFS Manual recommends consolidation of only the general government and the nonfinancial public

1/ Discussion Paper (p. 32), Conclusions and Recommendations (p. 4).
2/ Discussion Paper (p. 33), Conclusions and Recommendations (p. 4).
3/ Discussion Paper (p. 34), Conclusions and Recommendations (p. 4).

enterprises, referred to as the nonfinancial public sector. Similarly, for cases where government policy is carried out extensively through borrowing from not only the central bank but also from other government owned or controlled monetary institutions, it may be useful to focus on the nonmonetary public sector so as not to eliminate in consolidation the borrowing from the central bank and other public monetary institutions.

The group felt that it would be useful for the revised SNA to recognize and explain alternative formulations of the public sector such as the nonfinancial public sector, and the nonmonetary public sector. It was pointed out that the information for such a presentation is available and that guidelines for such a consolidation are discussed in the GFS Manual.

The group recommended that a consolidated presentation of the nonfinancial public sector (i.e., general government plus nonfinancial public enterprises) and the nonmonetary public sector (i.e., the nonfinancial public sector plus nonmonetary public financial institutions) should be included in the SNA as a complementary table providing information on the capital finance account.

II.' Statistical Units in the Government Sector

A. Classification of the Functions of Government (COFOG) 1/

Two main questions were raised; the first concerning appropriate statistical units in the Classification of the Functions of Government expenditures (COFOG) and the second, concerning the definition of an institutional unit in the government sector.

With regard to COFOG, the following questions were raised:

(i) Should the unit for classification of COFOG be in principle a transactor unit rather than a transaction?

(ii) If so, should the transactor unit be applicable not only to the production cost of government and output of government, but also to other expenses in the Income and Outlay and in the Capital Finance account?

(iii) Should the transactor unit be the same as the establishment-type unit recommended in SNA for classifying production accounts and capital formation by economic activity?

Both SNA and COFOG state, in principle, that with regard to the functional classification of government expenses, the unit of classification should be the transaction. However, for practical reasons,

1/ Discussion Paper (pp. 35-37), Conclusions and Recommendations (p. 9).

both recommend the use of establishment¯type units for the classification of production and capital formation expenses, and the use of the transaction as the unit for the classification of other expenses. It was suggested that, as the main aim of COFOG is to analyze government policies carried out through government programs in terms of the purposes they serve, programs integrating groups of expenditure that serve the same purpose might be used as the statistical unit.

It was mentioned in the discussion that statistical units can be classified according to three different criteria:

1) Activity, 2) Institution, and 3) Purpose or function. It was stated that for the activity classification, the establishment—type unit is clearly the statistical unit, and that the institutional classification is used in the sector accounts. It was therefore only for the COFOG presentation that statistical units needed to be discussed at the meeting.

Several members of the group called for a clear, explicit definition of units in the general government. It needed to be clarified whether, for example, a Ministry or a Department in a Ministry should be considered as a statistical unit. It was also argued that it would be very difficult to identify in the budget of many countries the programs referred to in the discussion paper.

The implications of using a transactor unit rather than a transaction unit as the unit of classification in COFOG were analyzed by looking at several examples. For instance, if the Ministry of Defense had a school for the children of military personnel, and the discussion paper's suggestion of using the transactor unit as the unit of classification were followed, the corresponding expenditures would be classified as Defense. However, most of the members of the group disagreed with this classification and stated that one should look at the purpose of these expenditures and therefore classify them in Education.

The group agreed consequently that the statistical unit for applying a functional classification of government outlays should be the transaction, or group of transactions which serve the same function, rather than the transactor.

However, as the grouping of transactions would usually depend upon the budget and accounting structure, it would have to be decided in each case how to group transactions for functional analysis.

B. Statistical Units for Sector Accounts 1/

The later part of the discussion dealt with the SNA definition of institutional units in the government sector. At present, an institutional

1/ Discussion Paper (pp. 35—37), Conclusions and Recommendations (p. 10).

unit is defined loosely in the SNA as a unit of decision, control and management. The central government is taken as one unit and various state, provincial, local governments and individual social security schemes are each considered as separate institutional units. It was stated that this might not be the most appropriate way to define a unit in the government sector and that for the analysis of government operations (by government subsectors, regional analysis, etc.), a more refined definition may be needed.

The discussion paper suggests possible additional criteria for defining an institutional unit, such as: (i) availability of separate accounting records on income and outlay and capital transactions; (ii) a separate accounting or budget office, or (iii) funding for the majority of its expenses by its own revenues (taxes).

It was stated that the definition of institutional units given in SNA cannot be different for the government sector. However, it was suggested that for analytical purposes it might be useful to define an intermediate unit between the institutional-type units used in the sector accounts and the establishment-type units used for the activity classification, one possible application being the World Bank studies of the impact of government policies on social structure, which would be difficult to carry out if establishment-type units were used. There were questions raised as to the existence of such intermediate units in many circumstances and what a clear definition would be.

In response to a question as to the kind of data one could refer to for an intermediate unit, it was suggested that an intermediate unit should have a full set of income and outlay accounts.

It was concluded that further clarification is needed on the definition of statistical units in the sector accounts for government and that for some analytical purposes, definition of an intermediate unit between the establishment-type unit used for the activity classification and the institutional-type unit used in the sector accounts would be necessary.

III. Registration of Transactions

A. Accrual and cash basis 1/

The group discussed two.basic questions: (i) how to define accruals for various government payments and receipts, and (ii) how to relate accrual and cash basis statistics. Whereas the SNA recommends that transactions should be recorded on an accrual basis, GFS adheres to cash basis reporting. The resulting differences are reflected in different types of transactions:

1/ Discussion Paper (pp. 38, 39), Conclusions and Recommendations (p. 5).

(a) Actual transactions in goods and services where the receipts and payments may be registered at different times in GFS and in SNA. (b) Transactions which are imputed in SNA, for example, wages and salaries in kind; these transactions are not recorded in GFS, except in some instances as memorandum items. (c) Transactions registered in both systems but treated differently, for example contributions which are paid by the employers directly to government, but which in SNA are channeled through the household sector.

It was pointed out that while the accrual basis in SNA is applicable to all sectors, the cash basis in GFS is dictated in part by the nature of government transactions, most of which are not for the delivery of goods and services, with most government receipts corresponding to taxes and most of government expenditure to transfers. The government cannot register its liabilities from others or to others completely on an accrual basis, since at the moment when many of the liabilities are generated the government is not a direct participant in the transaction. Because the nature of government **operations** is different from those of the other sectors of the economy, it is not entirely possible for the government to have complete registration of accruals of government liabilities to others or of others' liabilities to government.

It was generally agreed in the discussion that both the accrual and the cash basis are important for analysis of government operations and formulation of policy. It is therefore useful to show a link between the two basis. It was then suggested that it is important that the UNSO and the Fund's Bureau of Statistics continue the work already undertaken on the conceptual and operational bridge tables by spelling out for each type of transaction what specific adjustments would be necessary to go from one basis to another. This should distinguish between revenue and expenditure data for government. While an ideal solution would be to have both accrual and cash data showing the receipts and outlays of governments, permiting analysis from both perspectives, this is not possible in practice.

In the case of revenue, especially for tax revenue, cash basis data were most useful for measuring tax performance or tax effort. On the expenditure side, it was suggested that both sets of data would be useful, since they would show what accruing liabilities the government has incurred and what the actual disbursements were. For GFS, data on a cash basis can be derived in many countries from the government accounts after making some adjustments; these are shown in the derivation tables in the <u>GFS Yearbook.</u>

Differences between accrual and cash revenue data vary not only from country to country, but also according to the type of tax. For example, for external trade taxes, accrual and cash based data are very close; however, for income taxes they might be very different due to tax arrears, tax defaults, etc. The problem of arrears, which the group agreed is a very important one, will be further discussed in the meeting on Financial Flows and Balances.

It was felt that although in principle the SNA should be on an accrual basis and the GFS system on a cash basis, in practice this is not always the case, and in many countries there is actually not much difference between the basis of registration in GFS and in SNA.

In Brazil, for example, the records for revenue were reported to be **approximately** on a cash basis and those for expenditure approximately on an accrual basis. However, expenditures were registered not when the obligations are incurred but rather when the government recognizes these obligations. Because grace periods vary greatly from one tax to another, it has not proved practical to adjust the yearly tax statements of tax collections to an accrual basis for SNA. Nor has it been possible to adjust the approximately accrual basis expenditure data in detail for GFS purposes, so that adjustments have been made only for the totals rather than for the detailed data. This situation appeared to be typical of many other countries, with detailed data between a cash and an accruals basis.

It was pointed out that the Manual on Government Finance Statistics, in addition to calling for use of the best available data and adjusting it to cash basis total, recommends, in Section II.B, Supplementary noncash data (p. 40), that, for the proper analysis of government operations, one should use not only cash data but also available accrual data.

It was noted also that Eurostat has tried to reconcile its tax figures with those published by the OECD and has found that about 90 percent of the tax figures in Eurostat are on a cash basis.

Another factor raised in the. discussion was the compilation in the SNA not only of annual accounts but also of quarterly accounts, for which questions of timing are more acute and require additional adjustments for timing differences.

It was emphasized that a clearer statement is needed in SNA of what the accrual concept actually represents. One suggestion was that for the revision of the SNA, it might be helpful to consult the work done in the European System of Accounts (ESA) several years ago which includes specific recommendations on how to define the moment of recording.

In conclusion, the group confirmed that the accrual basis is the correct one for recording transactions in SNA, and the cash basis is the correct one for GFS. It was recognized, however, that for analysis of government operations supplementary presentations on the other bases are useful for both systems.

Currently, recording for both SNA and GFS was found to be a pragmatic mix of cash and accruals reflecting the state of the source data. It was recommended that the government authorities should be urged to maintain clear and consistent accounting practices.

It was concluded, finally, that further clarification of the accruals concepts is necessary in the revised SNA, and that prior to this, the IMF and **UNSO** should examine the relationship between the cash and accrual basis for different classes of transactions.

B. Consolidation 1/

It was noted that while in the GFS all transactions within the government being measured are eliminated in consolidation, in the *SNA* transactions within the government are eliminated only if they appear in the same account (i.e., production, income and outlay, or capital finance account) for both transactors. This limit on SNA consolidation is necessary so as not to alter input costs, value added, government output, and hence, GDP. The ESA follows the same basic **consolidation** rules as SNA but the ESA supplementary accounting system for government accounts follows the GFS consolidation rules. In the GFS and ESA supplementary accounts the **objective** is not to measure **government production, value added,** or consumption, but the flow of revenues, expenditures, lending and financing between the government sector and the rest of the economy.

To accommodate other purposes, such as analyzing the relationship between government and the rest of the economy, it was proposed that the SNA recognize other principles of consolidation, as was done in the SNA Draft Handbook on Public Sector Accounts, which, however, does not provide any details for such consolidation. It was felt that there would be advantages in providing for such further consolidation, facilitating the harmonization between GFS and SNA and making it possible to use *SNA* data for other purposes than the measurement of gross output.

It was also stated that very little explanation is given in the present SNA on the consolidation rules and that these rules would need to be made more explicit in the revised Blue Book.

Some members of the group expressed the opinion that they find satisfactory the extent of consolidation in the present SNA. It was mentioned that in previous meetings of the expert groups it was agreed that figures should be shown as unconsolidated as possible. However, it was also argued that the usefulness of the SNA would be increased if supplementary tables were introduced with consolidated accounts and also with a presentation closer to the one in the GFS Yearbook. The degree of consolidation would obviously depend on the statistics needed.

With regard to consolidation of different subsectors of government, it was noted that the principles of consolidation with regard to general

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1/ Discussion Paper (pp. 40, 41), Conclusions and Recommendations (p. 5).

government are the same in GFS and in SNA. In the GFS Yearbook, data for each of the levels (subsectors) of the government (Central, State, and Local) are shown separately and an additional table is presented for General Government, in which all the intergovernmental transactions have been eliminated. However, the tables for central government in the GFS Yearbook include the operations of national social security funds **separately** identified, whereas in the SNA social security funds data are shown separately from the central government.

The derivation table for central government in the GFS Yearbook shows data for some of the intragovernmental transactions that are eliminated in the consolidation of central government. There are also some memorandum items showing data that have been eliminated in consolidation such as taxes paid by government. There was discussion as to whether it would be useful to introduce other GFS memorandum items presenting more information on transactions which were eliminated in the consolidation.

It was agreed that although both GFS and SNA have different objectives, it is important that data from one system meet some of the needs of the other system, including those arising from different consolidation **principles**.

The group concluded that in the SNA government sector accounts, the extent of consolidation should be retained, but that it would also be useful to show certain flows in the government accounts on a more consolidated basis in supplementary tables.

C. Gross and net treatment 1/

Discussion centered on whether flows which have been previously shown net in SNA should be shown gross in order to increase the information on actual flows.

The principle in GFS is to show the most information possible. Therefore, all nonfinancing flows in GFS are shown gross with the exception of corrective transactions, such as refunds, and sales to the public by departmental enterprises, which are offset against corresponding operating costs.

In SNA, several entries are shown net, without a separate listing of their gross components. This includes, for example, gross fixed capital formation, which consists of acquisitions less dispositions of fixed capital assets. (This netting is distinct from the netting for depreciation.) While such netting may be useful in the household sector,

1/ Discussion Paper (pp. 42, 43), Conclusions and Recommendations (p. 5).

where fixed assets are mainly sold to other households, it obscures the different nature of acquisitions and sales when applied to the government sector, for which separate gross information on both the acquisition and **disposition** of fixed capital assets could be significant.

It was suggested that if gross fixed capital formation is presented for the government sector without offsetting dispositions against acquisitions, this should also be done for the other sectors, such as the corporate sector, though it might not be practical for the household sector.

It was also suggested that introduction of separate gross figures in SNA would be simpler if both gross flows (one of them necessarily negative) and the resulting net flow were restricted to one side of the account. It was mentioned that it would probably be more difficult for items in the production account to be shown on a gross basis as sales of second-hand goods, for example, are subtracted from consumption.

It was explained that when SNA was drafted it was believed that it **would** be more **difficult** to show the gross **amount** in some sectors, and it was therefore decided to show them as net in those sectors. This was only a matter of statistical presentation and not a matter of principle, however; in recent years entries for a number of categories, such as transfers, have been presented on a gross basis in SNA questionnaires.

The group agreed that in both the GFS and SNA transactions should, in principle, be shown on a gross basis, with netting an exception resorted to only when justified by statistical or presentational requirements.

At the end of the discussion, it was emphasized that the word "net" should only be used when similar items are deducted from each other. It was suggested that the term "net lending," which is presently defined in SNA as lending minus borrowing should be used only to designate lending minus the repayment of past lending, since, as the GFS Manual points out, for government, lending and borrowing are two totally different types of economic activity or behavior.

D. Imputations and reroutings

1. Separate identification 1/

It was the conclusion of previous expert group meetings that the present imputations and reroutings should *stay* in the SNA but that, to avoid overburdening data publications, only the most important should be identified. During the discussion, reference was made to the main

1/ Discussion Paper (pp. 44, 45), Conclusions and Recommendations (p. 5).

imputations and reroutings which give rise to differences between the SNA and GFS, as listed in the discussion paper, and in more detail in Bridge Table II of the GFS Manual (pp. 263-273). It was suggested that while compilers and users of data were both interested in bridge tables identifying the imputations and reroutings which constituted differences between the GFS and SNA, their interests were somewhat different. Conceptual bridge tables told compilers where they should be making adjustments. Users sought to know where the adjustments had been carried out, that is, where the differences had numerical values attached to them. It was suggested also that more importance be attached to the larger differences and that numbers might not have to be provided in all cases for some of the smaller items.

To meet the needs of compilers and users, the group strongly supported the use of both conceptual GFS-SNA bridge tables and operational bridge tables containing actual numbers to show the imputations and reroutings used in the derivation of SNA government data. A handbook on the government sector, rather than the Blue Book, should explain how the necessary estimates are to be made.

2. Consumption of government fixed assets 1/

The present SNA, while calling for calculation of the consumption of fixed capital for all assets which have finite lives, such as buildings, plants, machinery, and vehicles, excludes roads, dams, and bridges, which it assumes can last forever with normal maintenance. Experience now suggests, however, that roads, dams and bridges also have finite useful lives. The group was asked to consider, therefore, whether depreciation should be calculated for an expanded list of government fixed assets including such structures, as recommended by the Economic and Social Commission for Asia and the Pacific (ESCAP) Seminar on the Review and Development of National Accounts in 1986. It was pointed out that not all capital assets would be depreciable, as improvements in land, while forming a part of capital formation, would add to the permanent value of the land not subject to depreciation.

The group accepted the proposal to extend estimates of consumption of fixed capital to cover roads, bridges, dams and similar structures. It was agreed that even with regular repair and maintenance, structures of this kind will, in general, have finite lives.

2/ Discussion Paper (p. 46), Conclusions and Recommendations (p. 5).

3. Rent on government-owned buildings 1/

The present SNA does not include imputations for rent on government owned buildings nor on buildings owned by non-profit organizations. Government output is based on costs but the value of services produced by government capital assets such as government-owned buildings is not necessarily reflected in those costs. The proposal therefore was to impute a rent to government-owned buildings to reflect more accurately all services produced by government.

It was argued that in the private sector the value of rent on owner-occupied **buildings above depreciation** and operating costs would be included in the operating surplus. Because government output is calculated at cost, however, there is no operating surplus and the value of the rent and of overall production is **correspondingly** underestimated. It was also stated that in detailed analyses the asymmetry between government rental of buildings owned by others and government use of its own buildings gives rise to difficulties and anomalies. One example cited was the difference in income attributed to local areas where military families lived in housing on base, for which no rent was imputed, and where military families were given a housing allowance and rented private buildings off the base. It was to equalize such comparisons that previous reasoning had led to the imputation of households' rent on owner-occupied dwellings.

Opposing arguments focused on the undesirability of adding imputations to the SNA when they are not absolutely necessary. It was stated that for producers of nonmarket services this would require imputation of a separate producer of rent, with output, input, fixed capital formation, consumption of fixed assets, value added, labor costs paid, an operating surplus, etc.

It was noted that the 1986 ESCAP Seminar on *Review* and Development of National Accounts had cited the omission of imputed rents on government-owned buildings as a serious omission resulting in the underestimation of the contribution of the government sector to GDP. The November 1987 meeting of the EC Working Group on National Accounts, on the other hand, had opposed the proposal to impute rents on government owned buildings. In the discussion on the practicality of such imputation, it was suggested that rents of comparable buildings in the private sector could be used, as well as rents paid by government in privately owned buildings.

It was noted that GDP would normally be changed by the amount of the operating surplus that results from imputation of the rent on government owned buildings.

1/ Discussion Faper (p. 47), Conclusions and Recommendations (p. 6).

A majority of the group agreed that a rent should be imputed in respect of buildings used and owned by government. In principle, the imputation should be based on market rents for similar buildings. This imputation will normally result in a non-zero net operating surplus for government. Other participants disagreed with the proposal because of the practical problems connected with valuation of the rent services on the one hand and the proper identification of cost items associated with the imputed production of rent services on the other. Both elements would affect the resulting operating surplus.

4. Debt cancellations as transfers 1/

GFS does not include debt cancellation since it **involves a non-cash** transaction. SNA, however, treats debt cancellation in the flow accounts i.e., as a reduction in the value of an asset or liability with a counterpart flow of transfers. The issue posed was whether such changes in assets in the SNA should be recorded in the reconciliation account without being recorded through the flow accounts.

In the ensuing discussion, it was stated that the issue was already dealt with in the Expert Group Meeting on External Transactions (Paragraph V.9 of the Meetings' Report) and that the proposal decided there should be adopted. Following that proposal, the group recommended that in the SNA cancellations of debt by the creditor should be treated as capital transfers, but that unilateral defaults by the debtor should be recorded in the reconciliation account.

E. Valuation in current and constant prices

1. Transactions in kind 2/

The question presented to the group was whether government transactions in kind, such as the provision of wages in kind or of free education or health services, should be valued at cost or at prices for comparable marketed goods and services.

The SNA presently recommends valuation of these payments in kind at input costs, i.e., the sum of compensation of employees, consumption of fixed capital, and intermediate costs. The proposal to value government provision of goods or services in kind at market price would seek to correct an undervaluation of such transactions resulting from the omission of an operating surplus, or profit margin, for the government sector. One participant pointed out that in some cases the cost to the government of inputs could exceed the market price, so that valuing these goods or

1/ Discussion Paper (p. 48), Conclusions and Recommendations (p. 6).
2/ Discussion Paper (p. 49), Conclusions and Recommendations (p. 6).

services provided in kind at market prices could lead to computing an operating deficit for the government sector, which could then lead to a host of problems. It was also noted that use of market prices assumed that government goods and services were of the same quality as those sold in the market. It was agreed, therefore, that no change be made in the SNA valuation at cost of payments made in kind. It was recognized, however, in view of the difficulty of valuing the input costs of providing dwellings, that where the government provides employees free or subsidized accommodation in government-owned buildings, the imputed rent, which is to be included in compensation of employees as income in kind, should be estimated at the market rents of comparable dwellings.

2. Measurement of government output in real terms 1/

The group was asked to examine whether to maintain previous recommendations for the valuation in real terms of goverment value added and final consumption on the basis of output measures, if the government services are supplied to individuals, and on the basis of labor inputs in the case of "pure public services," despite the practice in most countries of basing calculations in real terms on inputs alone. It was recognized that at present most countries utilize some kind of input method which involves revaluing cost components--mainly compensation of employees and intermediate consumption--at base year prices, either by deflating current price values by wage and price indices or by using volume measures. The main objection to these methods is that by measuring only inputs they do not reflect changes in productivity.

It was the view of the group that the theory behind the output-based recommendations in the UN Manual on National Accounts at Constant Prices is correct and that, in spite of common practices, countries are making progress towards the compilation of output volume statistics which could be used in the future to apply the Manual recommendations.

The group recognized the difficulty of applying output measures. It recommended that, in line with the April 1975 Eurostat report on the Expert Group on Price and Volume Measures for nonmarket services (paragraphs 24—30), output measures should be used for services that can be statistically individualized but for more general services only input measures should be used, as output measures may be difficult to find.

1/ Discussion Paper (p. 50), Conclusions and Recommendations (p. 6).

IV. Analytical Framework

A. Current-capital distinction 1/

The group discussed whether military expenditures classified as capital formation should be restricted to dependents' housing, as in the present SNA and GFS Manual, or extended to include also military hospitals, structures, durable equipment used or usable for civilian purposes or for mixed civilian and military purposes, or other military durables.

It was noted that, in contrast to the SNA, the UN Handbook of National Accounting: Accounting for Production Sources and Methods recommends including certain items of a clear nonmilitary nature in government fixed capital formation, even if they are financed out of military budgets. These are family—type housing, schools, hospitals caring for civilians as well as military personnel, highways, port facilities and airports, if they are not limited to military use. It was therefore suggested at the meeting that some guidance is needed.

Two questions were raised: 1. Whether there should be a list of assets used by military and civilians, such as schools, hospitals, roads, etc., which would always be considered as capital formation.

2. Whether, when an asset is transferred from military to civilian use, requiring in SNA a reduction in consumption and a rise in capital formation, this transfer should be handled in the reconciliation account or in the flow accounts. (This second question was raised at an earlier meeting in Santiago.)

With regard to the first question, several participants suggested that in order to decide whether or not to change the present treatment, which excludes military durables from capital formation, it would be necessary to know the rationale for the present treatment. It was mentioned that one possible explanation is the uncertain lifetime of military assets, which could be expended in the course of hostilities.

It was suggested that the revised SNA should present a clear definition of what is meant by military purposes and explain whether internal order should also be considered as military. A distinction also needs to be made between expenditure by the military and expenditure for military purposes.

With regard to current practice, it was mentioned that in Brazil military equipment or weapons are not included in capital formation but

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1/ Discussion Paper (pp. 51, 52), Conclusions and Recommendations (p. 7).

military buildings are, and that this treatment is **also followed** in **Finland.**

It was reported that when these questions were discussed at the November 1987 meeting of the EC Working Group on National Accounts, opinions were divided. Those who opposed changing the present treatment argued that it would be very difficult to make the change operational; those who favored a change differed on whether only schools and hospitals used by the military and civilians should be included in capital formation or whether all military assets with possible civilian use should be included.

It was **stated** that the IMF's **position favored** retaining the present treatment, and also that any change in treatment would cause large changes in a number of measures of government and **economy-wide** performance, with an extensive effect on saving. The IMF position, as stated in the GFS Manual, recommends that any expenditure by the military for civilian use should not be considered a military expenditure. It was thought, however, that the concepts of "shared use by military and civilians" or "potential use by civilians" was very difficult to identify.

It was **argued** that **although** this **principle** of "civilian use" is a good one, it is sometimes difficult to apply in practice, and that perhaps one should therefore analyze the principal use or purpose.

It was stated that the World **Bank's position is** also that the treatment should remain the same. A change in the present treatment would have a major impact on the way the Bank operates with its capital-output ratios and with the required saving definition.

In the ensuing discussion, the group was **divided** as to whether military schools and hospitals should be included in government gross fixed capital formation. It was also stated that the lifetime of military assets should not be the only consideration in deciding how to classify them, since during wartime any civilian asset, such as a building, can have as short a lifetime as many military assets have. It was felt that whatever treatment is recommended should be the same in time of war or peace.

Following a broad exchange of views, it was agreed that many unanswered questions will need to be discussed again at the meeting of the Expert Group on Input Output and Production Accounts. However, in order to formulate a provisional. recommendation for that meeting, the members of the group voted on the following set of possibilities, going from the widest to the narrowest solution:

(1) Include all expenditure on durables (including weapons) within fixed capital formation; (2) Include all construction in fixed capital formation; (3) Include all military durables that can potentially be used for civilian purposes in fixed capital formation; (4) Include all durables that are used also for civilian purposes in fixed capital formation; (5)

Include all expenditure on durables which are primarily used for civilian purposes, (more than 50 percent), as well as expenditure on hospitals, in fixed capital formation; (6) Include all those fixed assets that are primarily used for civilian purposes in fixed capital formation, even if such assets are produced or acquired by military establishments (i.e., no change in the present treatment).

The majority of the group voted for the last proposal, with the understanding that it is only preliminary, i.e., that there should be no change in the present treatment but that this issue should be considered again by the Expert Group on Input-Output and Production Accounts. The provisional proposal approved by the majority includes as capital formation the construction of fixed assets by military personnel, if these assets are primarily used for civilian purposes.

It was agreed that further research will be carried out on the rationale for the present treatment and on the implications of any change in the system, with the resulting study to be presented to the Input-Output and Production Accounts meeting. In addition, users will also be consulted for their views on this question.

In the discussion of the second question on capital formation taken up by the group, involving how to treat a transfer of existing assets from military to civilian use, two situations were considered: (1) When the asset is sold, that is, the change is connected with a payment of money, and (2) When there is no payment of money involved. In the first situation, it was recommended that the transaction be treated as negative intermediate consumption of government. If the purchaser of the existing military durables is a household, the purchase should be classified as part of the final consumption of households; if the purchaser is a producer, then the purchase should be shown as fixed capital formation of the producers.

In the case where there is no payment of money involved, it was recommended that the shift of existing military durables to civilian use should be recorded in the reconciliation account.

Both recommendations were approved without further discussion.

An additional point discussed in connection with government capital formation was what should be included in the "change in stocks" of the government sector in the SNA. The present provision is to include in changes in government stocks only strategic stocks and stocks of departmental enterprises and ancillary enterprises. The question raised was whether this concept should be widened in SNA to include also other goods which are acquired but not consumed in the period of recording. It was pointed out that information on government stocks not yet utilized is generally not available. However, in theory, such unused materials could be considered to constitute capital assets rather than consumption, parallel to unused materials in the enterprise sector.

It was agreed, therefore, that in **principle it would be advisable to widen the present provision and to include all goods in the change in government stocks, though in practice it would generally be difficult to obtain the additional information.**

B. Own-saving and overall deficit/surplus

The group discussed whether the two concepts own saving and overall deficit/surplus should also be **provided** in **SNA**. It was noted that these two concepts are restricted in their application to the government sector and are included in GFS.

The reason given for including them in **SNA** is that they are very useful for the analysis of the government sector. Reasons for not including them are because: (1) they are not **applicable** to the other sectors of the economy, and (2) the numbers **prepared** for these concepts in SNA might differ from the GFS figures because of the different data bases used, etc., and consequently might confuse some of the users.

The two concepts were discussed separately.

1. Own-saving 1/

The concept of government own-saving corresponds to the portion of current income, other than grants from governments and international organizations, remaining after current outlays. It is used to reflect the special position in government operations of grants, i.e., official transfers, which are in some cases provided to help the recipient government undertake particular expenditures and in other cases provided as a form of budgetary support to meet a deficit that would otherwise ensue. Because of their special position, official grants received by government are identified in a separate category in GFS to permit users to include grants above or below the line, according to their needs. It was suggested that recognition of the concept of government own-saving in the SNA would facilitate this type of analysis of government operations in the SNA.

It was mentioned during discussion of the concept of own-saving, that in some cases countries incur some current expenditures only because of grants they have received, and that the expenditure would be counted in calculation of own-saving while receipt of the grant would not.

1/ Discussion Paper (pp. 53, 54), Conclusions and Recommendations (p. 7).

While the group generally agreed that the concept of own-saving is a very useful one for analyzing the performance of each level of government and also of general government if there are grants from abroad, it recommended that it should not be included in the SNA. The reasons given were that: 1) There is no need to overload SNA accounts by including every measure used in GFS, and 2) it only applies to the government sector.

However, it was stated that it is necessary to make it possible in SNA to derive this GFS item by identifying in the transaction classification these types of flows.

Because of the usefulness of this concept, it was proposed that it should be explained in the Handbook of Public Sector Accounts with the data shown in supplementary tables. The Handbook should explain the relationship between GFS and SNA with regard to this concept, and clarify any differences that may be found between the figures in the supplementary tables for SNA and the GFS figures.

2. Overall deficit/surplus 1/

The overall deficit/surplus concept, which has application only in the government sector, represents the single, most used measure of government performance. It is defined in the GFS Manual as revenue plus grants less expenditure less lending minus repayments. It is by definition equal, with an opposite sign, to the sum of net borrowing by the government, plus the net decrease in government cash, deposits and securities acquired for liquidity purposes. The GFS Manual distinguishes between government acquisition of financial assets for public policy purposes, which is treated like expenditure above the overall deficit/surplus line, and government acquisition of financial assets for the purpose of managing the government's **liquidity**, which is treated below the line as part of financing.

At present the overall deficit/surplus is not explicitly defined in the SNA and it is not generally derived from SNA data on government. The concepts used in the SNA. are the saving concept, which measures the government's current account deficit/surplus, and the SNA net lending concept, which represents the net result of government lending and repayment of previous lending, and of government borrowing and amortization of previous government borrowing.

The two related questions discussed by the group were: 1) Should the concept of overall deficit/surplus for the government sector be included in

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1/ Discussion Paper (pp. 55-57), Conclusions and Recommendations (p. 7).

the SNA? and 2) Can the SNA, in its revised version, make a better distinction between government lending and government borrowing?

In response to the first question, it was generally agreed that the concept of overall deficit/surplus is very useful and should therefore be included in the SNA; if it is not possible to include it within the central **framework**, then it **should** be included in **supplementary** tables, as is done in Eurostat **publications**. It was also agreed that it is very important to clarify the overall deficit/surplus concept in the SNA in order to eliminate any confusion resulting from differences in its presentation in the SNA supplementary tables and in the GFS publication.

With regard to the second **question**, it was agreed that it is necessary to replace the term "net lending" in the revised SNA.

C. Government operating surplus 1/

The group was asked to consider whether the value of government output should include some or all government interest payments in addition to other cost items, since the measurement of government output by the cost of inputs rather than by the market price of output omits the element of operating surplus from which interest payments are made in the enterprise sector. It was suggested that such government payments could be viewed as either the cost of borrowing by government or as the imputed interest on the government owned fixed capital assets used in the course of production of government services.

There was also the view that if interest payments were included in the cost of production, then interest received by government would also have to be included in the production account. The question was raised also as to whether the calculation should be limited to the interest paid for those loans invested for a productive purpose.

It was concluded, however, that the appropriate view of the problem was whether the cost of capital was being omitted and not whether interest payments should be counted. The discussion centered, therefore, on treatment of imputed interest on the fixed capital assets of the government. It was stated that the 1953 SNA recommended the imputation of interest on fixed capital assets of government used in the course of production, and that the major question faced under that provision was what rate of interest should be used for the calculations. This provision was deleted in the 1968 SNA, however, and the group's discussion was on the question of whether it should be restored. Some experts indicated that this imputation of interest in the production cost may represent a sharp increase in the resulting GDP. Others felt that such an increase in the

1/ Discussion Paper (p. 58), Conclusions and Recommendations (p. 6).

GDP would be justified if the GDP is otherwise considered to be undervalued by failing to take into account the full cost of government capital assets utilized in government production. There was no clear majority for either solution to this issue. It was recommended that the question be further studied in conjunction with the recommendation on imputed rent for government-owned buildings and that two experts--one expert in national accounts and another in economics--prepare a technical paper on the subject.

V. Classification

A. Taxes

1. Indirect taxes 1/

It was noted that in the present SNA indirect taxes consist of commodity taxes, which are taxes on goods and services that are proportional to the value of goods and services produced or sold by industry, and non-commodity taxes, which include taxes on payroll, payments by business of motor vehicle taxes, which are classified as direct taxes when paid by households, and payments by business of regulatory and administrative fees such as court fees, passport fees, etc., which are classified as current transfers when paid by households. GFS, however, does not identify indirect taxes separately and does not distinguish between payments by households and by business. Payments by households or business of motor vehicle "taxes" are classified in GFS as taxes and payments of regulatory and administrative fees as nontax revenue.

It was further noted that countries do not usually make the distinction between tax payments by business or non-business units when responding to the SNA and usually allocate the total receipts from one heading to the predominant element. In addition, analysis of national accounts data shows that the difference between total indirect taxes and commodity taxes is very small.

For practical purposes and to facilitate the link with GFS data in the construction of national accounts, the group was asked to consider two proposals:

(i) That indirect taxes be restricted to commodity taxes and the coverage of commodity taxes be expanded to include a major non-commodity tax such as taxes on payroll, which reportedly account for the major portion of non-commodity taxes;

1/ Discussion Paper (p. 59), Conclusions and Recommendations (p. 8).

(ii) That the distinction between payments by business and households be eliminated as regards motor vehicle taxes, **administrative** and regulatory fees by classifying these payments outside the purview of indirect taxes.

It was stated by several participants that the present SNA distinction between indirect taxes and direct taxes was not sufficiently clear and that the terminology should be replaced. It was felt, however, that the distinction between commodity taxes and non-commodity taxes should be maintained because the identification of commodity taxes was necessary for input-output analysis. In this connection, it was thought to be undesirable to reclassify taxes on payroll as commodity taxes since it would be difficult to allocate payroll taxes to the various commodities produced by a single enterprise.

With respect to the second proposal, it was argued that within the system of the national accounts a distinction had to be maintained between payments by producers and by households. The distinction could not be avoided in the context of the national accounts even if in practice there were some countries which did not have the statistical resources to separate certain payments by business from payments by households.

It was suggested, however, that the primary distinction should be between taxes and nontaxes, and not between payments by business or households. Then numbers could be taken from the government accounts, classified as taxes or nontaxes under GFS, with a breakdown subsequently made by national accountants to distinguish payments by business or households. In that way, consistent sets of statistics could be produced for GFS and the SNA and movement from one system to the other could be facilitated. The proper distinction between taxes and nontaxes, however, was referred to the group's subsequent discussion of fees.

The group recommended that the present SNA terminology of indirect and direct taxes be replaced. In addition, the group agreed not to change the distinction between commodity taxes and other indirect taxes and the distinction in the SNA between taxes paid by producers treated as indirect taxes, and by households treated as direct taxes.

2. <u>Estate and gift taxes</u> 1/

It was noted that the present SNA classifies estate and gift taxes and nonrecurrent taxes on property not as taxes but as capital transfers to government, whereas GFS. and the OECD's Revenue Statistics include these taxes in tax revenue and GFS classifies all tax revenue as current revenue of government. It was pointed out that the GFS and OECD treatment

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<u>1/</u> Discussion Paper (pp. 60, 61), Conclusions and Recommendations (p. 8).

represented the views of public finance theories, and that governments receive a continued flow of estate and gift taxes and regard them as recurrent in nature, like other taxes, in no cases earmarking their receipts for capital purposes. It was argued that from the point of view of households and governments, these payments are taxes and are current in nature and that the defining characteristic as to the current or capital nature of transfer payments should be the purpose of the payment. While **individual** households may sometimes pay these taxes through a reduction in their own assets, there is no perception that the payments are going to be used for capital expenditures by the government.

The group discussed a proposal to classify estate and gift taxes and nonrecurrent taxes on property in the SNA as taxes and as current receipts.

In discussion, it was indicated that during the Expert Group Meeting on the Household Sector, it was decided that the current and capital distinction should be discussed again at a future expert group meeting on the basis of a study to be prepared by the OECD. A proposal was therefore made to classify estate and gift taxes and nonrecurrent taxes on property as taxes in the **SNA** but to postpone discussion of their current or capital aspect to another expert group meeting when the OECD study would be available. However, the payments would be called taxes regardless of the decision made on their current and capital nature.

The group agreed that the borderline between current and capital taxes should be reviewed in the wider context of the distinction between current and capital transactions in another Expert Group meeting on the basis of the OECD study. The group also agreed to use the term tax with respect to those taxes included in the SNA capital account.

3. Social security contributions 1/

Discussing the difference in treatment of social security contributions between the SNA and the GFS and OECD Revenue Statistics, the group noted that social security contributions are not classified as taxes in the SNA, but referred to only as social security contributions. In the SNA, employer social security contributions are deemed to be routed through households as compensation of employees and simultaneously paid to government by households, while employee contributions are collected from households. The OECD Committee on Fiscal Affairs and GFS, on the other hand, classify compulsory social security contributions as taxes, since they are compulsory, unrequited, nonrepayable payments to government. Voluntary social security contributions are classified as nontax revenue. However, reflecting the distinctiveness of social security contributions,

1/ Discussion Paper (pp. 62, 63), Conclusions and Recommendations (p. 8).

which allow contributors to be admitted to a benefits system, social security contributions are separately identified from other payroll taxes, and in the OECD Revenue Statistics publication total taxes are presented both with and without the inclusion of compulsory social security contributions. The proposal before the group was not to change the SNA treatment of social security contributions, channeled through households, but to identify them as part of the overall category of taxes so as to correspond to OECD Revenue Statistics and GFS definitions and facilitate international comparisons of data.

It was explained that as sectoral systems of statistics focusing on government, GFS and OECD Revenue Statistics could not very well exclude social security contributions from overall taxes, since the contributions were widely regarded within public finance literature as taxes. It was felt on the other hand, however, that social security contributions were not regarded as taxes in a number of countries and that it would be difficult to include them in the context of the SNA as part of taxes. It was determined that a single figure combining taxes and social security contributions was not a necessity in the SNA context, so that by omitting such a number from SNA confusion with the GFS and OECD Revenue Statistics concept of total taxes could be avoided.

The group agreed, therefore, not to apply the term tax to social security contributions in the SNA, but to avoid using the term total taxes in the SNA. In addition, to facilitate the link to the tax concept of GFS and OECD Revenue Statistics, the group recommended showing a supplementary presentation in the SNA in which all taxes and compulsory social security contributions would be totalled to reach the GFS and OECD concept of total taxes.

4. Fees 1/

The group examined the differing treatment of fees in the SNA and in the GFS and OECD Revenue Statistics with a view to clarification and the possible elimination of differences between them. It was noted that in the SNA fees are classified as indirect taxes if paid by businesses and as a part of fees, fines and penalties if paid by households other than for non-regulatory services. In the GFS and OECD Revenue Statistics, on the other hand, the classification of fees is not determined by whether they are paid by businesses or households. The principle followed by the GFS and OECD Revenue Statistics classifies fees as nontax revenues, in a GFS category for administrative fees and charges, if they are paid in return for a service--whether compulsory fees for provision of a regulatory service or voluntary charges for provision of a non-regulatory service--unless the

1/ Discussion Paper (pp. 64, 65), Conclusions and Recommendations (p. 8).

payment is out of all proportion to the cost or distribution of the government service provided to the payer. It was pointed out that practioners had found themselves unable to agree on identification of regulatory and non-regulatory services. In addition, as there were differences in interpretation of this definition among OECD countries, the decision taken, after years of discussion, in the OECD Fiscal Affairs Committee, and adhered to by the GFS, was to follow the predominant practice of tax administration authorities and provide a specification of which fees are classified as taxes and which are classified as administrative fees and charges.

It was proposed that harmonization could be advanced if the primary decision in the SNA could be taken on the basis of the nature of the fee as tax or nontax, with determination of its classification resulting from payment by businesses or households made subsequently. It was felt that **compulsory** fees could be treated as taxes in the SNA, with the proviso that those paid by businesses be classified as indirect taxes and those paid by households as direct taxes.

With regard to fees paid for a service, there was discussion of whether fees considered to represent payment for a service could be accommodated in the SNA production account for enterprises. Agreement was reached that such fees could be classified as part of enterprises' intermediate consumption, the provider of the service being the government. It was noted, however, that fees out of all proportion to the cost to government of **providing** the service would be classified as taxes rather than as payments for a service, in line with the provisions followed by OECD Revenue Statistics and GFS.

It was stated that in principle SNA already permitted classification of some fees as payment for a service provided by government. It was agreed that the group ask for clarification in the SNA of the borderline between fees that are transfers and fees that are payments for a service and recommend that the borderline be the same as it is in the GFS and OECD Revenue Statistics. This would permit establishment of a similar borderline between taxes andnontaxes in the SNA and the GFS-OECD Revenue Statistics, though the subdivision of individual tax categories in the SNA between payments by business and by households would lead to necessary differences in some further classifications of taxes. It was agreed that such subsequent classification by who pays fees and taxes and whether they are to be included in the production account or income and outlay account is essential to the SNA. The group concluded that attempts should be made to harmonize, to the extent possible, the SNA and OECD/GFS borderline between taxes, fees, and service charges, in respect of both classification and terminology.

B. Property income

1. Withdrawals of entrepreneurial income 1/

The question put to the group was whether the category of dividends received by government should be combined with the category of withdrawals of entrepreneurial income from quasi-corporations, to eliminate a distinction which many governments do not make and which is not made in GFS.

It was pointed out that in practice it is very difficult to identify what corresponds to dividends from corporations or income from quasi-corporations, because the distinction between corporations and quasi-corporations is not clear in many countries. The group felt, however, that it would be useful to keep the greatest degree of information for those countries where it is available. It was pointed out that the breakdown applies also to other sectors and not to government alone. The group concluded, therefore, that the distinction between withdrawals from entrepreneurial income of quasi-corporations and dividends is a useful one and recommended that it should be retained.

To accommodate the reporting of data combining both categories when information permitting this separation is not available, it was proposed that an entry combining both categories be provided at a higher level in the reporting hierarchy. It was not felt to be appropriate for the group to resolve reporting hierarchy questions. No concrete recommendation was advanced, therefore, as to the level of the transaction classification hierarchy at which this distinction should be made.

2. Operating deficits of departmental enterprises 2/

The group was asked to decide whether the operating deficits of departmental enterprises should be treated as government subsidies or as negative entrepreneurial income. It was pointed out that in the absence of adequate information it would be difficult to determine whether a departmental enterprise's loss on sales to the public was the result of a deliberate government policy to keep prices below costs or of an inability by the enterprise to contain costs below sales price. As the government's role vis-a-vis departmental enterprises was as both an owner and a possible provider of public policy subsidies, both alternatives were possible. It was noted that in GFS the basic public policy orientation of government in its operation of departmental enterprises was taken as overriding, and therefore operating losses were classified as subsidies. There was no

1/ Discussion Paper (p. 66), Conclusions and Recommendations (p. 8).
2/ Discussion Paper (pp. 67, 68), Conclusions and Recommendations (p. 9).

provision in the GFS for a category of government current transfer payments to enterprises other than subsidies.

It was pointed out that in the SNA the two alternative treatments represented negative entrepreneurial treatment in one case, and the imputation of a subsidy payment to the departmental enterprise in the other, resulting in no negative operating surplus (operating deficit).

Several participants felt that a distinction was necessary between those cases in which operating deficits of departmental enterprises were deliberate, representing a government policy of subsidizing prices, and those cases in which they were not. It was agreed that flexibility of treatment was necessary so that both possibilities could be reflected in the classification of government payments to meet departmental enterprises' operating deficits. It was pointed out that an operating surplus is treated in the SNA as either entrepreneurial income or indirect taxes, depending on whether or not it arises as a result of deliberate policy, as in the case of a fiscal **monopoly**. It was argued that symmetry should be maintained in the case of an operating deficit, which should be treated as either a subsidy or as negative entrepreneurial income, depending on whether or not it arises as a result of deliberate policy.

The group decided, therefore, that both possibilities should be provided for in the next version of the SNA—that is, as a negative operating surplus and as a **subsidy--and** that the subsidy solution should be used in cases where it is clear that the operating losses of a departmental enterprise's sales to the public arise from a deliberate government policy of providing particular goods and services at below cost.

3. Indexation payments 1/

The group discussed the question of whether indexation payments on debt, used in some countries with high inflation to increase the attractiveness of government securities, should be classified as interest paid for use of capital or as amortization paid for repayment of capital in real terms. At present, both SNA and GFS generally classify indexation payments as interest payments, so that they appear in the SNA income and outlay account rather than in the capital finance account and above the line, increasing the deficit, in GFS. It was suggested that appropriate treatment should reflect the behavior of the recipients of indexation payments: if lenders in an inflationary environment view their indexation payment receipts as a return of capital to be reinvested for maintenance of their capital's value, classification of such payments as interest in the income and outlay account would tend to overstate income and saving.

Participants stated that the topic had been discussed many times before this meeting and that the recommended treatment of indexation payments as interest had remained unchanged. It was felt that the

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1/ Discussion Paper (pp. 69, 70), Conclusions and Recommendations (p. 9).

experience of countries using indexation could contribute to the analysis. There was discussion of the Chilean case, in which there was a high nominal rate of interest, but the payments were not divided between interest and amortization. It was reported that in Brazil indexation payments were treated as interest in the public sector statistics but not in all other statistics, since analyses of changes in the public debt found that most of the variation is explained by the nominal change in the value of the liabilities involved, which was equivalent to the indexation of the liabilities. Practices in different countries were found to vary significantly and the group did not feel there was enough information for it to make a recommendation. It was concluded that the subject should be referred to the Expert Group on Financial Flows and Balance Sheets.

C. Social assistance to households

1. Individual consumption concept 1/

2. Subsidies and social assistance 1/

The objective of this discussion was to examine the consequences for the government sector of proposals made in the Expert Group Meeting on the Household Sector for the treatment in the revised SNA of consumption expenditures and of total and individual consumption and their financing.

In a summary of discussions held at the Household Sector Meeting it was noted that that the meeting had rejected a proposal by some of its members that certain items of government expenditure which are now treated as subsidies (such as subsidies designed to lower prices, or to diminish the financial burden on households of certain goods and services), should instead be treated as final consumption expenditure of government, i.e., showing the government as bearing part of the cost. Noted also was another proposal, rejected at the Household Sector Meeting, that some of the subsidies mentioned above be treated as social benefits, with the households sector expenditure recorded as if they had paid full price.

It was reported that the Household Sector Meeting had agreed that the concept of total consumption should be introduced in the central part of the SNA and that five components of final consumption should be shown: (i) individual consumption expenditure by general government, (ii) collective consumption expenditure by general government, (iii) individual consumption expenditure by private non-profit institutions serving households, (iv) collective consumption expenditure by private non-profit institutions serving households, and (v) (individual) consumption expenditure of households.

1/ Discussion Paper (p. 71), Background Document No. 7, "Total Consumption of the Population," Conclusions and Recommendations (p. 9).

The Expert Group of the Household Sector had suggested that the main criteria for the allocation of final consumption expenditure to the sector accounts should be the "ultimate bearer of the expense." It was stated, however, that the implications for the government sector of the conclusions reached at the Household Sector Meeting had not been carefully analyzed.

At the present meeting it was suggested that it was very important to first spell out clearly how to integrate income and consumption in a total presentation; only then could the implications for the government sector be **analyzed.**

It was also stated that for GFS purposes, it would be very important to maintain the distinction between transfers and purchases of goods and services, and that the breakdown between individual consumption and collective consumption should be at a secondary level. In this way one could still see what the government purchases are and what the government **provides** as transfers to others.

It was suggested that there should be two concepts of presentation: the expenditure concept and the consumption concept. For GFS purposes, the expenditure, concept would be more important; for SNA purposes, the consumption concept would also be important.

The group concluded that it could not discuss the repercussions of introducing the concepts of individual consumption, consumption subsidies, and social assistance because the ramifications of introducing these concepts for the government sector had not been completely worked out, and that a more detailed study would need to be prepared for this purpose.

3. Food coupons 1/

The group discussed whether the issuance of coupons to households for use in purchases of food or other commodities, with subsequent redemption by government, should be classified as government purchases of goods and services, as subsidies, or as social assistance grants to households.

It was noted that government payments for goods and services provided to households is classified as government intermediate consumption in the SNA only when the households have no choice as to the goods or services provided. When the households have some choice as to the products for which the coupons are to be employed, it was felt that the overall operation should be regarded not as a government purchase of goods and services but as an unrequited transfer. It was necessary to determine, however, whether it should be regarded as a subsidy to enterprises or as a social assistance grant to households.

1/ Discussion Paper (p. 72), Conclusions and Recommendations (p. 9).

Another question to be decided was the timing of the registration. In **SNA**, which is an accrual-based system, these operations could be registered when the coupons are issued to households, when the households use the coupons to make purchases and receive delivery, when enterprises present their claims for payment from the government, when such payment is due at some interval after presentation for payment, or when payment is actually made. In the GFS system, issuance of such coupons is registered at the time the payment is made to enterprises redeeming the coupons.

It was recommended that the issuance of coupons should be treated as social assistance grants to households rather than as subsidies to enterprises, since such **coupons** do not change the market price in any respect and payment to enterprises for **redemption** of the coupons is not unrequited. It was also recommended that the coupons should be recorded in SNA in the period in which they are issued.

4. Welfare work assignments 1/

The group discussed whether payments to welfare recipients requiring performance of work assignments should be classified as social assistance grants or as payments for factor services. It was noted that this classification is becoming very important because of the growing number of welfare systems which include such work assignments.

One suggestion was that if the work contributes to improve the character of the person doing the work, it should be considered a social assistance grant, but that if the work adds to the product, it should be considered a payment for factor services.

It was suggested, however, that for the sake of international consistency this question should be discussed with the International Labor Organization (ILO), since it is related to employment and unemployment statistics. It was stated that if the person involved is considered to be employed, then the payments should be considered to be wages and salaries; if the person is considered to be unemployed, then the payments should be treated as social assistance grants. The determination of whether the person is considered to be employed or unemployed should be made after consultation with the ILO. This consultation should take place before the Expert Group Meeting on Input-Output and Production Accounts.

It was noted that the European Communities had also been looking into this matter and had found it to be a very complicated question because of the wide range of existing welfare work schemes. The questions emerging were not only whether to classify the persons involved as employed or unemployed but also how to determine the amount to be recorded.

1/ Discussion Paper (p. 73), Conclusions and Recommendations (p. 9).

D. Functions

1. Revision of COFOG

(a) Treatment of administrative, regulation and research expenditures 1/

It was explained that COFOG differs from the former SNA Table 5.3 in that COFOG distributes all expenditure on general administration, regulation and research among the heads of classification down to the most detailed three digit level. This aspect of COFOG classification raises two problems. On a practical level, it was reported during the discussions that many EC countries had found the procedure too detailed for systematic data compilation and as a result did not intend to follow this COFOG recommendation. On a general level, it was suggested that this COFOG recommendation hinders attempts to isolate the **individualizable** consumption expenditure of government. This is so because it does not distinguish between two types of government administration expenditure:

(i) local administration expenditure within units producing services (for example, hospitals and schools) which could be provided by comparable private sector units, and which should be included as individual consumption;

(ii) general administration, regulation and research expenditure which cannot be found in private sector institutions providing individual services, and which should therefore be considered as collective consumption.

The group voted to recommend that expenditure for general administration, regulation and research be identified as a separate group within each major COFOG group, that is the fourteen first level groups.

(b) Functional allocation of subsidies 2/

The group was asked to consider whether the functional classification of subsidies in COFOG should depend on: (1) the ministry which pays it, (2) the industry which receives it, or (3) some perhaps more subjective assessment of its purpose (e.g., welfare). It was noted that COFOG does not appear to provide clear direction as to which criteria to follow,

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1/ Discussion Paper (pp. 74, 75), Conclusions and Recommendations (p. 10)-

2/ Discussion Paper (pp. 75, 76), Conclusions and Recommendations (p. 10).

although it does single out certain subsidies such as certain food and housing subsidies for classification under welfare (criteria 3) instead of under the industry which receives the subsidies (criteria 2).

Interest in this question had arisen from proposals to include the value of certain subsidies in the total consumption of the population. To calculate total consumption of the population, some exercises have added the **value** of certain social or consumption subsidies to the values of household consumption and the "individual" consumption expenditure of general government and private nonprofit institutions, in the belief that such "social" subsidies have an effect similar to the direct provision of the goods or services by government. In this connection, the Expert Group meeting of the Household Sector in September 1987 had decided against the idea of introducing consumer subsidies as a form of final expenditure but had recommended a detailed classification of subsidies by type and purpose.

The group **voted** to recommend that in **COFOG subsidies** should be allocated to the purpose served. However, in cases where the purpose is not sufficiently clear, the subsidy should be allocated to the function corresponding to the activity classification of the producer who receives it.

(c) Relationship with ISIC 1/

In a discussion on the relationship between COFOG and the International Standard Industrial Classification (ISIC) it was noted that COFOG stipulates that the transaction is in principle the unit of classification but that for many types of outlays related to production activities COFOG' codes will have to be assigned to units of the establishment types. In addition, SNA paragraph 5.31 recommends that these establishment type units should be the same as for the activity (ISIC) breakdown of producers of government services so as to allow "transferring data classified according to kind of economic activity of the producers into data classified according to the purpose they serve."

It was reported, however, that a study by Eurostat into the structure of COFOG and the structure of ISIC indicated that even if the establishment types were the same, the two classification systems were so different that it would in practice be very difficult to transfer data from one classification to the other. The group considered, therefore, whether COFOG should be revised so that, at a moderately aggregated level, it would be possible to achieve a simple correspondence between COFOG categories and ISIC categories.

1/ Discussion Paper (p. 77), Conclusions and Recommendations (p. 10).

The group recommended that a study should be carried out into the **possibility** of reconciling COFOG and ISIC but not so far as to jeopardize the concepts and analytic requirements of the two classifications which were designed with different aims in mind--one, a classification by purpose (COFOG) and the other, a classification by activity (ISIC).