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**STRATEGIC ISSUES LINKED TO THE MEASUREMENT OF INTERNATIONAL  
TRANSACTIONS**

**SESSION IIA: SELECTED MEASUREMENT ISSUES: SOME CURRENT ACCOUNT  
ISSUES**

**ABOUT A VALUATION PROBLEM OF TRANSACTIONS WITH THE REST OF THE  
WORLD**

Note by the Hungarian Central Statistical Office

**I. THE PROBLEM AND A SUMMARY**

1. The balance of external merchandise trade of Hungary has improved since Hungary's accession to the European Union; the former negative balance significantly decreased by 2007. A key role is played in the improvement of the balance by a group of special distributors and – as revealed by our analysis – the related valuation problem.
2. To analyse the role of the special distributors' group, cash data of the line "goods" in the balance of international payments for the period 2003–2006 were used in addition to statistics on external merchandise trade. The analysis of comparable data covered detailed enterprise-level data as well.

## II. DISCUSSION

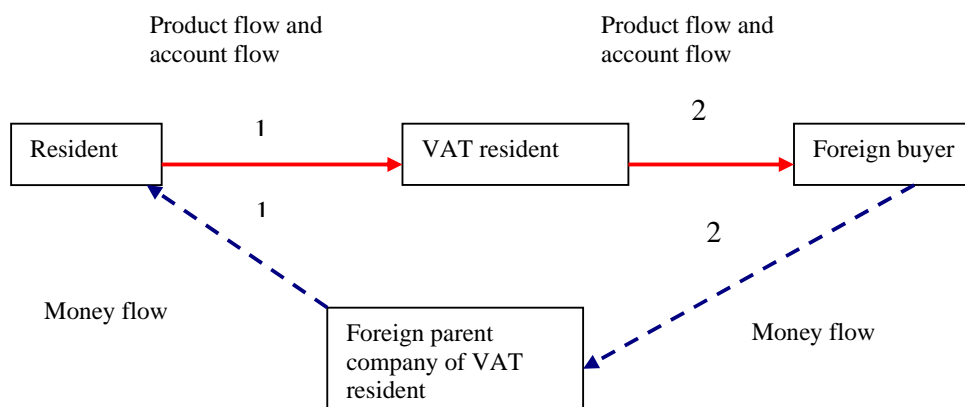
3. The valuation problem refers to a group of special distributors, the **VAT residents** of foreign enterprises in Hungary. In accordance with the legal rules in effect, a foreign firm in Hungary – as is the case in other countries, for the purpose of performing commercial activity –, is allowed to claim to being within the provisions of the Act on value added tax, and to apply for a tax number without being required to set up a business, local unit or employ a person. The distributor is obliged to submit a value added tax return but is not obliged to make a corporate tax return.

4. To compile external merchandise trade statistics, export and import data are collected directly from the distributor group or are obtained from customs records. Although export share of the distributor group was insignificant at the time of accession to the European Union, it is more than 10% today, and the distributor group have an even more important role in influencing the balance of external trade.

5. Based on the analysis, the different valuations and differing measurements applied by external merchandise trade statistics and settlement statistics can be illustrated by the following basic transactions.

### A. Exports

(a) Transactions: a Hungarian resident sells products to a VAT resident in Hungary, and then the VAT resident sells the products abroad. The transaction can be illustrated in the following manner:



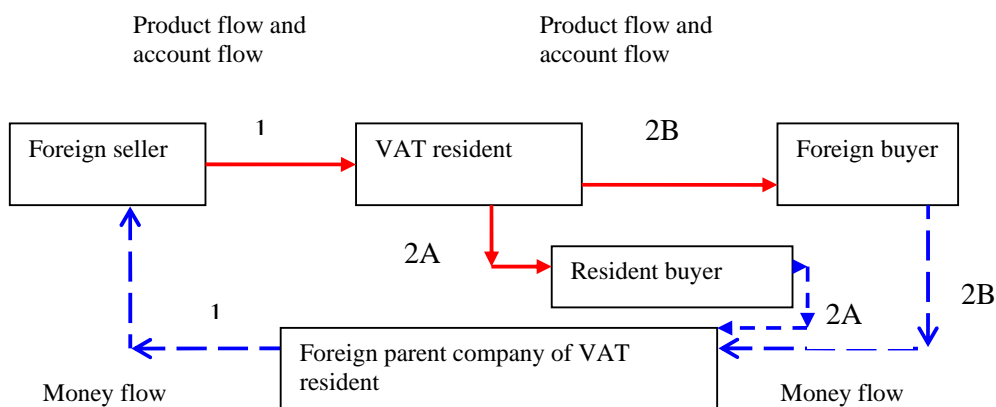
(b) Product flow and account flow: between the resident and the VAT resident in Hungary (1), and from Hungary abroad (2).

(c) Money flow: transfer from the account of the parent company of the VAT resident to the resident company (1), and from the foreign company buying the product to the account of the parent company (2). By involving the VAT resident, the transaction (and thus the value) measured in external merchandise trade statistics and balance of payments statistics is different.

6. Comments: the transaction between the resident and the VAT resident is a domestic transaction from the point of view of the VAT system. The resident makes out the invoice in the name of the VAT resident, and it is included in the value added tax return of both of them, but the product becomes the property of and is recorded in the books of the parent company of the VAT resident. From the angle of settlement statistics, the export transaction takes place already between the resident and the VAT resident. In external merchandise trade statistics, the value of the transaction between the VAT resident (essentially its parent company) and the foreign buyer is measured.

## B. Imports

(a) Transactions: the VAT resident imports the product, after which **in case A** sells it to the resident, or **in case B** sells it abroad.



### Case A:

(b) Product flow and account flow in case A: in stage one from abroad to Hungary (1), i.e. between the foreign company selling the product and the VAT resident, while in stage two in Hungary, between the VAT resident and the resident company (2A).

(c) Money flow: from the Hungarian resident to the foreign parent company of the VAT resident (2A), and between the parent company and the foreign seller (1).

7. Comments: from the point of view of external trade statistics imports take place in stage one, whereas in settlement statistics the second transaction is measured, the value of which is different from that of the first transaction.

### Case B:

(d) Product flow and account flow in case B: compared to case A in stage two, the product is exported (2B) after import (re-export transaction).

(e) Money flow: between foreign companies (2B), residents are not involved.

8. Comments: Both transactions are measured in external trade statistics, but neither in balance of payments statistics.
9. In the first case, the value of exports measured by external trade statistics is higher than exports measured in settlement statistics, while in part A of the second example, the value of imports is lower than imports registered in settlement statistics. Purchasers' price and sales price measured in external merchandise trade statistics may be different in case 2B as well, while the total turnover and the possible balance are excluded from settlement statistics. The difference between the two types of statistics is realized in both cases in the books of non-resident enterprises.
10. In practice, in addition to the above basic cases, several variations of external trade transactions may take place with the help of VAT residents, if, for example, the transaction is realized with the involvement of a VAT warehouse, or combined with re-export following processing under contract.
11. In macro statistics (national accounts and balance of payments statistics) the above-mentioned distributors can be regarded as "notional units", or – as in the Hungarian case – non-residents. External merchandise trade data are used in the two statistics in their own data systems, therefore to ensure consistency it is necessary to value transactions identically at national level, and make estimations of the trade margin realized by foreigners.
12. Three methods were analysed to estimate the differing measurements of external merchandise trade statistics and settlement statistics, i.e. revenues realized abroad:
  - (a) **Balance difference method.** HCSO managed to delimit a group of resident enterprises to which VAT residents with significant turnover can be assigned as transactors. Turnovers, i.e. invoice value, "corresponding" to balance of payments transactions, were estimated for residents and VAT residents thus defined. The export and import balance of residents is overestimated in external trade statistics by the difference between the estimated merchandise trade balance and the cash balance;
  - (b) **Estimation using VAT data of VAT residents.** VAT residents distribute products - their value added tax returns contain relatively simple transactions. Using VAT data, a simplified balance of revenues (the sum of export and domestic sales) and expenditure (the sum of import and domestic purchases) and, based on this, the sales surplus and its proportion to total sales can be compiled. This is assuming that prices are identical in each export direction, and multiplying exports of the above-mentioned distributor group by the proportion of the sales surplus equals the sales surplus realized by foreign enterprises.
  - (c) **Imputed trade margin method.** The surplus realized on imports and exports is calculated by imputing the percentage trade margin specific for international business practice, assuming that total imports are sold in Hungary and total exports derive from the Hungarian market.

13. In the first two cases, the difference can be divided between exports and imports according to their proportion to each other, while in the case of the third method, the division is given. The order of magnitude of the results received by the three methods was identical.

### **III. SUMMARY**

14. The balance of goods measured in external merchandise trade statistics contains a component that is related to foreign enterprises, is recorded in their books and cannot be deduced from residents' transactions. Accounting for the correction concerning foreign enterprises may be the following in macro statistics:

(a) Adjusting external trade prices to domestic prices, i.e. valuating imports at domestic sales prices and exports at domestic purchasers' prices. Price adjustment requires the division of the difference between exports and imports;

(b) Accounting for the revenue surplus of foreign enterprises as services imports or income.

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