Distr.
GENERAL

CES/AC.68/2004/16
29 April 2004

ENGLISH ONLY

STATISTICAL COMMISSION and ECONOMIC COMMISSION FOR EUROPE

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT (OECD)

CONFERENCE OF EUROPEAN STATISTICIANS

COMMISSION OF THE EUROPEAN COMMUNITIES (EUROSTAT)

Joint UNECE/Eurostat/OECD Meeting on National Accounts
(Geneva, 28-30 April 2004)

UPDATING THE 1993 SNA: SETTING THE SCOPE AND RECENT METHODOLOGICAL DEVELOPMENTS

With reference to the February 2004 Meeting of the Advisory Expert Group (AEG) on National Accounts

Paper submitted by United Nations Statistics Division[1]

INTRODUCTION

1. With the February 2004 Meeting of the Advisory Expert Group on National Accounts (AEG) at the International Monetary Fund (IMF) from 16 to 20 February in Washington DC, the international statistical community has embarked on a comprehensive review of the 1993 System of National Accounts (1993 SNA), to be completed by 2008. The mandate for this review by the AEG was delegated at the thirty fourth session of the Statistical Commission (E/CN.3/2003/34) with certain limitations, most noticeably that the review should not lead to fundamental changes and in that light should be considered an update rather than a full scale revision.

2. The need for a comprehensive review as compared to an incremental updating process had been recognised by the Statistical Commission based on the large number of identified issues that had arisen from new economic developments and conceptual consistency perspectives. Meanwhile the Commission is cognisant of the fact that it had to set limitations on the review in order to prevent a widening statistical divide between countries at different levels of implementation of the 1993 SNA, and subsequently compromising the international statistical comparability. Moreover,

---

[1] Paper prepared by Ivo C. Havinga.

the Commission spelt out that the consistency between the SNA and other macroeconomic (financial) statistical standards like the Balance of Payment Manual and Government Finance Statistics Manual should be maintained and where possible improved. Where possible and feasible, also the latest developments in the international business accounting standards should be taken into account. Finally, the Commission instructed that any amendments proposed should not only adhere to conceptual integrity but also take the implementation aspects in countries into account. Evidently, it entrusted this review to the AEG under the overall coordination of the Intersecretariat Working Group on National Accounts (ISWGNA) with the understanding that issues are brought to conclusion in a spirit of consensus.

3. One of the main objective of the first meeting of the AEG was to set the scope of the updating process through the review of the issues identified by the ISWGNA, the IMF Balance of Payments Committee in its revision of the BPM5 and the Taskforce on Harmonisation of Public Sector Accounting (TFHPSA) in their process of harmonisation between the international accounting and statistical standards in the area of public sector accounts. It is noted that the candidate issues identified by the ISWGNA are part of the deliberations of various existing expert groups like the Canberra II Group on the Measurement of Non-Financial Assets, electronic discussion groups and taskforces.

4. In addition, the first AEG meeting addressed the recommendations on methodological development put forward in issue papers concerning treatment on taxes on holding gains, military weapon systems as fixed assets, treatment of employer retirement pension funds, employee stock options, cost of ownership transfers on non-financial assets, measurement of production on non-life insurance, measurement of production of (non-insurance) financial services, and measurement of output of central banks.

5. The recommendations made by the AEG on the accepted list of issues and accepted recommendations on methodological development are at this stage **provisional** and will be circulated to the national statistical offices of the UN Member States for information and comments. These comments will be consolidated by the ISWGNA and submitted to the AEG for further deliberations. It has been considered of paramount importance to ensure widespread discussion including regional debates with national accountants and other users. In this process the engagement of all UN Regional Commissions is envisaged.

6. In the remainder of this paper, the agreed scope of the updating of the 1993 SNA and the accepted recommendations regarding methodological developments will be presented in turn.

7. For further detail on the proceedings of the first AEG meeting and other aspects of the updating process, the reader is referred to the United Nations Department of Economic and Social Affairs/ Statistics Division website
http://unstat.un.org/unsd/nationalaccount/snarw1.htm

SCOPE OF UPDATE OF THE 1993 SNA WITH NO FUNDAMENTAL CHANGES

8. With the working title of the updated version of *1993 SNA* deliberately worded as *1993 SNA* Rev. 1, the working title is meant to send a signal that a fundamental change is not envisaged.

9. In annex 1, the single and integrated list of issues accepted by the AEG for review has been presented in a table followed by the summary descriptions of the issues. In total 44 issues have been recognized along with the responsible agency or expert group, and the expected date of completion. In addition, several cross-cutting issues have been merged which had been identified separately by different expert groups, e.g. units which combines the treatment of ancillary units and ancillary corporations.

10. The reasons for the acceptance of the issues are diverse (the number in brackets refer to the identification number of issues in annex 1). In some instance, *changing economic circumstances* require a certain conceptual treatment to be addressed like employee stock options (3), residence (39) and definition of units (25) in the new global environment with multi-territorial presence, and their establishment under specific legal structures and for specific purposes. Other issues are proposed to follow *symmetric treatments* like the case of unfunded employer retirement pension schemes (2), government transactions with public corporations (34) and retaining earnings of mutual funds, insurance companies and pension funds (42). Some issues pertain to the rewording and adjustments to the *classifications* such as classification and terminology of assets (28) and financial assets classification (44). Again others are accepted to ensure *consistency with other macroeconomic standards* like the case of BPM for goods sent abroad for processing (40) and merchanting (41) and like the case of GFSM for private, public and government sector delineation (36). Finally, some issues have been accepted to follow-up to developments in the *international business accounting standards* as the cases of non-life insurance services (5) and financial services (6).

11. In the deliberations on the proposed issues, some issues were rejected like on consumer durables and consumer subsidies. In the first case, the recognition of consumer durables would entail a fundamental change in the production boundary and the asset boundary. In the latter case, the issue of consumer subsidies had been considered extensively and rejected in the preparation of the 1993 SNA and no new convincing arguments have been put forward to change to present treatment.

12. Some proposed issues required no further explicit discussions such as the recognition of the importance of some macroeconomic aggregates like net domestic product and the rewording for cultivated assets in line with the System of Economic and Environmental Accounting (SEEA). These issues require simple rewordings in the SNA and can be dealt during the editing.

13. In addition to the above-mentioned accepted list of issues, some members of the AEG proposed some supplementary issues pertaining to: Wages and salaries in cash and in kind – some clarification is needed, review the purposes and uses of SNA, multi-country accounts—monitoring economic and monetary unions, financial accounts—a special chapter on FA to be developed, financial innovation—better clarification of financial derivatives, improve the SNA as a basis for comprehensive productivity analyses, integrate policy oriented variables, review SNA terminology for user-friendliness, special issues of quarterly national accounts, treatment of transport costs in basic prices and regional accounts.

14. It was decided that those additional issues including justification would be submitted to the ISWGNA for review. The consolidated recommendations of the ISWGNA on the issues would be submitted to the AEG members for their consideration.

RECOMMENDED METHODOLOGICAL DEVELOPMENTS

Treatment on taxes on holding gains

15. The AEG agreed not to change the SNA regarding the classification of taxes on holding gains; they will continue to be classified as current taxes on income and wealth (D51). However, taxes on holding gains should be shown as a special sub-category within D51.

16. The AEG considered the possibility of discussing in some paragraphs of the SNA alternative concepts of household income. However, the AEG considered that this is not a priority for the present SNA review.

Military weapon systems as fixed assets

17. Following an intensive discussion, the group voted to include expenditure on military weapon systems as gross fixed capital formation. In order to distinguish between military equipment and other equipment, there was general agreement that defense GFCF for defense equipment should be presented separately from other types of GFCF.

Employee stock options (ESO)

18. The AEG approved the four main recommendations presented in the issue paper: treatment of ESOs as compensation of employees; spreading the value of ESOs between the grant and vesting dates if possible; valuation at market price, or by using a suitable option pricing model; the recording of the ESOs in the financial accounts not as an financial derivatives but as an instrument category entitled “financial derivatives and employee stock options,” with the subcategories of (a) financial derivatives and (b) employee stock options.

Cost of ownership transfers on non-financial assets

19. It was recommended to preserve the link in the 1993 SNA between the value of an asset to an enterprise and the value of the services to be rendered by the asset over the length of time it is held. This implies maintaining COT to be treated as capital formation. However, the AEG considered that rather than depreciate the COT over the lifetime of the underlying asset as proposed by the current SNA, the cost of ownership transfer should be written off over the period during which the acquirer expects to hold the asset. If expectation is met, this means that the COT will be entirely depreciated when the asset is resold, thus resolving the issue raised of overestimating operating surplus.

Measurement of production on non-life insurance

20. The first recommendation sets as a general principle that the production of insurance services does not occur when the risk occurs. The concept of insurance service is the service of covering for the risk. As such, its measurement should not be affected by the volatility of the

occurrence of the risk. Neither the volume nor the price of insurance services is directly affected by the volatility of claims. The AEG accepted the recommendation to continue to use a formula based on the difference between premium (plus premium supplements) and claims, but to use *adjusted* claims and, optionally, *adjusted* premium supplements in this formula in order to correct for the volatility of observed flows.

21. The recommended formula for the measurement of output of non life insurance in the SNA 1993 rev 1 will therefore be: [Actual premiums earned [i.e. premiums receivable less changes in the reserves due to pre-payment of premiums] + Adjusted premiums supplements - Adjusted claims incurred. The recommendation regarding the adjustment of premium supplements remains optional.

22. There are three practical solutions to implement this general recommendation. The expectation approach (which uses statistical smoothing of past data), the accounting approach, and the sum of costs plus “normal” profit approach.

23. The *expectation approach* consists in replicating the *ex-ante* model used by insurers to price their premiums, on the basis of their expectations.

24. The *accounting approach* would be required an extension of technical provisions to include equalization provisions and the other special provision when expected risk occur.

25. The *sum of cost plus “normal profit”approach* may be a solution for countries that do not have full information on insurance services.

<u>Measurement of production of (non-insurance) financial services</u>

26. The AEG reviewed the provisional recommendations of the OECD Task Force. It was noted that the recommendations should be regarded as work-in-progress.

27. Three recommendations were submitted: a new definition of financial corporations; the principle of non-exclusion of own funds in the measurement of output; a reference rate approach for the measurement of FISIM.

28. The following comments were made: the new definition is broader than the present 1993 SNA treatment, which is a good development; and the term “financial intermediation” should not disappear from the definition.

29. The AEG invited the OECD Task Force to produce a comprehensive presentation of all the inter-related issues of sector and industry definition, valuation of output, allocation of output to users, role of own funds, treatment of unincorporated money lenders, and ancillary units such as companies’ treasury departments, etc.
30. A small group of AEG members will submit a specific proposal to the AEG members on (informal) money lenders in developing countries. The treatment of Islamic banks should be clarified. The IMF agreed to propose the text.

<u>Measurement of output of central banks</u>

31. The AEG reviewed the recommendation made by the ISWGNA in 1995 on the measurement of the output of central banks.

32. The AEG agreed that, because of the unique functions that may be performed by central banks, the value of their output obtained by the method recommended by the *1993 SNA* (the difference between property income receivable less interest payable) may sometimes be exceptionally large or small or even negative. In such cases the output of central banks or at least part of it could be measured at cost. Further work is needed to clarify these cases. This does not imply reclassifying the central bank to the government sector. Clarification is needed of which sectors consume the output of the central bank.

Annex 1

1993 System of National Accounts (SNA) updating
List of issues accepted for review by the Advisory Expert Group (AEG)

by the first meeting of the AEG

	Issue	Responsible	Expected date of completion
1.	Repurchase agreement	IMF	November 2004
2.	Employer retirement pension schemes	IMF	November 2004
3.	Employee stock options	Eurostat	**Completed February 2004**
4. 4a. 4b.	Valuation of non-performing loans, loans and deposits Non-performing loans Valuation of loans and deposits; Write-off and interest accrual on impaired loans	 IMF-EDG BOP Committee	 November 2004 November 2004
5.	Non-life insurance services	OECD Taskforce	November 2005
6.	Financial services; Allocation of the output of central banks	Canberra II IMF	November 2004 November 2004/5
7.	Taxes on holding gains	Canberra II	**Completed February 2004**
8.	Interest under high inflation	UNSD	November 2004
9.	Research and development	Canberra II	November 2005
10.	Patented entities	Canberra II	November 2005
11.	Originals and copies	Canberra II	November 2004
12.	Databases	Canberra II	November 2004
13.	Other intangible fixed assets	Canberra II	November 2005
14.	Cost of ownership transfer	Canberra II	November 2004
15.	Cost of capital services: production account	Canberra II	November 2004
16.	Government owned assets	Canberra II	November 2004
17.	Mineral exploration	Canberra II	November 2004
18.	Right to use/exploit non-produced resources between residents and non-residents	Canberra II and BOP Committee	November 2005
19.	Military weapons	Canberra II	**Completed February 2004**
20.	Land	Canberra II	November 2004
21.	Contracts and leases of assets	Canberra II	November 2005

1993 System of National Accounts (SNA) updating
List of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

22.	Goodwill and other non-produced assets	Canberra II	November 2005
23.	Obsolescence and depreciation	Canberra II	November 2005
24.	Build-own-operate-transfer (BOOT) schemes	Canberra II	November 2005
25.	Units		
25a.	Ancillary units	UNSD to set up EDG	November 2005
25b.	Institutional units a. Holding companies, special purpose entities, trusts; b. Treatment of multi-territory enterprises; c. Recognition of unincorporated branches	BOP Committee	November 2005
25c.	Privatization, restructuring agencies, securitization and special purpose vehicles (SPVs)	TFHPSA	November 2004
26.	Cultivated assets	Canberra II	**Completed February 2004**; rewording accepted
27.	Classification and terminology on assets	Canberra II	November 2005
28.	Amortization of tangible and intangible non-produced assets	Canberra II	November 2005
29.	Assets boundary for non-produced intangible assets	Canberra II	November 2005
30.	Definition of economic assets	Canberra II	November 2004
31.	Valuation of water	Canberra II	November 2005
32.	Informal sector	UNSD/Delhi Group	Preliminary paper: Nov. 2004 Final: Nov. 2005
33.	Illegal and underground activities	UNSD	November 2005
34.	Super dividend, capital injections and reinvested earnings (government transactions with public corporations (earnings and funding))	TFHPSA	November 2004
35.	Tax revenues, uncollectible taxes, and credits (recording of taxes)	TFHPSA	Preliminary paper: Nov. 2004 Final: Nov. 2005

1993 System of National Accounts (SNA) updating
List of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

36.	Private/public/government sector delineation (sectorization boundaries)	TFHPSA	November 2005
37.	Activation of guarantees (contingent asset) and constructive obligation	TFHPSA BOP Committee	November 2005
38. 38a. 38b. 38c.	Transaction concept Change of economic ownership (as term) Assets, liabilities and personal effects of individuals changing residence ("migrant transfers") Application of accrual principles to debt in arrears	BOP Committee	November 2005
39.	Residence a. Meaning of national economy b. Predominant center of economic interest (as term); c. Clarification of non-permanent workers and entities with little or no physical presence	 BOP Committee BOP Committee UNSD	November 2005
40.	Goods sent abroad for processing	BOP Committee	November 2005
41.	Merchanting	BOP Committee	November 2005
42.	Retained earnings of mutual funds, insurance companies, and pension funds	BOP Committee	November 2005
43.	Interest and related issues a. Treatment of index linked debt instruments; b. Interest at concessional rates; c. Fees payable on securities lending and gold loans	BOP Committee	November 2005
44.	Financial assets classification	BOP Committee	November 2005

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG)

by the first meeting of the AEG

1. Repurchase agreement
A repurchase agreement (repo) involves the sale of securities or other assets with a commitment to repurchase equivalent assets at a specified price. The right to on-selling has become almost universal. The 1993 SNA and the BPM5 treat the repos similar to that of a collateralized loan or as other deposits if repos involve liabilities classified under national measures of broad money. Should the 1993 SNA treatment be revised?

2. Pension schemes in macroeconomic statistics
In the 1993 SNA, promises to pay future pension benefits are not recognized as liabilities of social security schemes and unfunded employer schemes. The review will investigate the analytical relevance of recording these liabilities in the national accounts and, if appropriate, formulate recommendations regarding their valuation and measurement. The review will also formulate proposals to reconcile the recommendations of the 1993 SNA and the IMF Government Finance Manual regarding the treatment of unfunded employer pension schemes.

3. Employee stock options
Employee stock options are a common tool used by companies to motivate their employees. Given that the 1993 SNA does not provide guideline to this issue, the question raised is whether stock options should be considered as compensation of employees and therefore as a cost to employers. Experts at the OECD meeting on national accounts in October 2002 arrived at the consensus to include employee stock options in compensation of employees. Further harmonization with international business accounting standards is required.

4. Valuation principles
4a. Non-performing loans
The treatment of non-performing loans is a topic on which the Thai authorities had asked the ISWGNA for clarification as to what extent unpaid interest should be accrued (considering that the financial intermediation services indirectly measured on such interest may affect the GDP). The purpose of the review is to determine what criteria should be applied to the writing-off of non-performing loans and to make sure that they are consistent with the other major macroeconomic statistical systems (balance of payments, government finance, and money and banking statistics).
4b. Valuation of loans and deposits
The valuation of loans positions and deposits are subject to alternative perspectives. Nominal or face value valuation might be misleading because of the risk of default and/or changes in interest rates. This difference becomes apparent when the loans are traded. However, these valuation issues are equally applicable to non-trade loans. The business accounting standards are considering using the concept of “fair value” for the valuation of loans as if they were traded.

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

5. Non-life insurance services
This issue is devoted to the measurement of non-life insurance services, with a special focus on the treatment of catastrophic losses. The output of insurance services as calculated using the 1993 SNA algorithm depends on the balance of premiums to claims (on an accrual basis) and can therefore be extremely volatile (even negative) following major catastrophes. The massive claims generated by the 11 September terrorist attack, is a recent example. It had impacts on GDP and balance of payments (reinsurance). The objective of the review is to propose measures that would be more consistent with the perception of production in this activity. In particular, medium to long-term aspects of non-life insurance are to be taken into consideration.

6. Financial services
This issue is devoted to the measurement of the output of financial intermediation services and portfolio management in the national accounts. The business of financial corporations has undergone a structural transformation towards a rising importance of the portfolio management of financial assets. This generates holding gains and losses, that, typically, national accounts exclude from the production boundary and therefore income. The review will consider whether and how the production boundary can be adapted to this rising activity, and how this could influence income.

7. Taxes on holding gains
Taxes on capital gains are treated as taxes on income and deducted from income while the tax base (the realized holding gains) is not included in the SNA definition of income. Is this a contradiction that should suggest alternative treatments or should the SNA treatment remain the same?

8. Treatment of nominal holding gains and interest on financial assets under high inflation.
Peter Hill and Andre Vanoli have written to the ISWGNA, with regard to the treatment of nominal holding gains and interest on financial assets under conditions of high inflation, as described in the 1993 SNA Chapter XIX, Annex B and subsequently in the OECD publication "A Manual on Inflation Accounting" written by Peter Hill along a position different from that taken in Annex B in the 1993 SNA. Andre Vanoli has written a paper for discussion at the 1998 IARIW conference which raised issues regarding the inflation accounting treatment. Peter Hill has responded with a paper also submitted to the 1998 IARIW conference, essentially giving counter-arguments and in turn raising issues regarding Annex B. The EDG on this issue did not arrive at a distinct conclusion. This issue will be put forward to the Advisory Expert Group on National Accounts.

9. Research and development (R&D)
The 1993 SNA treats research and development (R&D) expenditures of market producers as

**1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued**

by the first meeting of the AEG

production of a notional establishment and intermediate consumption of other establishments of the same enterprise while R&D expenditures by non-market producers are recorded directly into intermediate consumption. Questions have been raised whether R&D costs should be capitalized. If that solution is chosen, should expenditure on basic research be treated similarly as expenditures for applied research and experimental development? Should the R&D activities of non-market producers be treated as for market producers?

10. Patented entities – Research and development expenditure
In the system patented entities are treated as non-produced intangible assets. However, payments received from patent users are by convention recorded as output of services similar to rentals from lease of fixed assets. This is contrary to other non-produced assets such as land. Should R&D costs and the original derived from it be linked or capitalized separately? Furthermore, how should originals be valued and what types of price indexes should be used to deflate the output of services from patented entities?

11. Originals and copies
How should expenditures on originals and copies be recorded, should both be recorded as expenditure (on new goods) on the basis that originals are distinct from copies, or should originals be considered as being analogous to a ‘stock’ of copies, and so expenditure on a copy partly (or mostly) reflects a sale of an existing good? How should the transactions in copies be recorded?

12. Databases
The 1993 SNA recommends that large databases should be capitalized. Should SNA provide a clear definition of databases to be capitalized covering characteristics such as size and marketability of the data as well as the database itself.

13. Other intangible fixed assets – new information and specialized knowledge
The 1993 SNA mentions these not-elsewhere classified items in the Annex of Chapter XIII, which are restricted to the units that have established ownership rights over them or to other units licensed by the latter. What is intended to be included in other intangible fixed assets?

14. Cost of ownership transfers
The review was initiated by a request from the Singapore Statistical Office and its principal focus has been whether the COT of fixed assets should be expensed or capitalized. The review has since broadened to include issues such as, if COT is to be capitalized what should be the service life, how should we treat COT when the underlying asset is sold by the original owner, and, by extension, how should we treat the termination costs of the underlying asset.

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

15. Capital services

Capital services provided by fixed assets to the production process are not explicitly defined by the 1993 SNA. The OECD's Measuring Capital defines capital inputs as the actual or estimated pure economic rent payable; that is, by the sum of depreciation and the capital, or interest, costs. There is a need for a definition of capital services in the SNA. Should it be rental or pure economic rent? Given the latter definition, the capital services of rented produced fixed assets are only part of the rental paid by the user to the owner (the remainder being the costs incurred by the renter in providing the service), and which appear in the SNA as intermediate input; and likewise, the capital services of rented non-produced assets are only a part of the rent paid, and appear in the SNA as part of gross operating surplus. For own-use fixed assets, capital services appear as part of the gross operating surplus. How should capital services be shown in the accounts for productivity analysis purposes? Should the treatment of capital services be introduced into the core of the SNA or be treated in a satellite account?

16. Government-owned assets

Services from government-owned assets, which are used in the production of government services are reflected in the output of the government services only as consumption of fixed capital. This means that neither return on capital to these assets nor opportunity cost is recognized. Should the SNA treatment of imputed output to the general government activity remain the same or should capital services be included?

17. Mineral exploration

Expenditures on mineral exploration are classified as gross fixed capital formation. The rationale is that mineral exploration creates a stock of knowledge about the reserves that is used as input in future production activities. The question has been raised as to whether this knowledge should be seen as independent of the stock of economically exploitable reserves or whether this leads to double accounting when both discovered stocks of resources and stock of exploration are capitalized.

18. Transactions of the right to use/exploit non-produced resources between residents and non-residents and between residents

Except for land, transactions of the right to use or exploit non-produced resources between residents and non-residents have not been fully elaborated by the 1993 SNA. For land a notional resident unit is created which is deemed to purchase the land while the non-resident is deemed to purchase a financial asset (equity) of the notional unit. Should the treatment of land be extended to other non-produced resources such as water, fish, etc. or should there be alternative treatments?

19. Military weapons

The 1993 SNA divides military assets into those that can be used for civilian purposes and those

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

that can only be used for military purposes. The former are treated as gross capital formation, the latter as intermediate consumption. This treatment does not provide an appropriate accounting system for existing weapons as weapons that have already been expensed can actually be taken out of stock for use or for exports and would have to be balanced by a negative component in government final consumption. Should the line between gross capital formation and intermediate consumption be drawn differently?

20. Land
The SNA currently records improvements to land as gross fixed capital formation, but in the balance sheet such improvements are included with land itself – a non-produced asset. Should land be split into two, with one part recorded as a fixed asset and the other part recorded as a non-produced asset? If so, how should the separation be made? One option is to distinguish between land that is in, or nearly in, its natural state as a non-produced asset and the remainder as a fixed asset. Another option is to separate land from the improvements made to it, and record the former as a non-produced asset and the latter as a fixed asset.

21. Contracts and leases of assets
Contracts and leases of tangible assets are defined by the SNA. However, the treatment of intangible non-produced assets is not clarified. These assets comprise governmental tradable leases/licences such as casino, taxi permit, foreign trade licenses and emission permits, non-governmental tradable contracts (option to buy not yet produced assets, contracts on authors, football players and other performers, etc.), subcontracting to third party of tradable leases/contracts/licenses, franchises and goodwill. Should and under what conditions should a lease/license/contract on non-produced assets be treated as a sale or rent of the asset? Should the criteria provided by the ISWGNA on mobile phones be applied or should they be further elaborated? Should a legal construct be recognized as a non-produced asset when it is signed? How should one treat a change in the market prices of a lease or contract when its value is different from the discounted sum payable? If it is recognized, should it be treated as a financial derivative or a non-produced asset? Should the concept of financial leases be broadened to include assets that are not leased for their entire service life?

22. Goodwill and other non-produced assets
The 1993 SNA only records purchased goodwill and it treats purchased goodwill for corporations and unincorporated enterprises differently. Should goodwill continue to be recognized only when purchased or should internally generated goodwill be recognized? Should purchased goodwill be treated the same way for corporate and unincorporated enterprises? Should the balance sheet recognize assets such as brand names, trademarks, franchises, etc.?

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

23. Obsolescence and depreciation

Consumption of fixed capital (i.e. depreciation) is defined in the 1993 SNA in general terms as the decline, during the course of the accounting period, in the current value of the stock of fixed assets owned and used by a producer as a result of physical deterioration, normal obsolescence or normal accidental damage. It is referred to as time series depreciation because it is defined in terms of the change in value of an asset over time. An alternative definition, called cross section depreciation, is defined to be the difference in value of two assets that are identical, except one is older than the other by the same length of time as the accounting period. Cross section depreciation is used in the derivation of estimates of multifactor productivity, and it seems that in practice, most, if not all, countries estimating depreciation are in fact applying this definition. Should time series depreciation continue to be the one defined in the SNA and, if so, how should it be applied?

24. Build-Own-Operate-Transfer (BOOT) schemes

BOOT is a scheme in which a private enterprise builds or purchases a facility that provides services for the general public (such as toll booth, highway, prisons or electric generating facility) at its own expenses in return for the right to operate it and to charge a regulated fee that allows it to earn a net profit for an agreed length of time. At the end of the period, the ownership of the facility is transferred to the government without compensation. Should SNA provide guidance to the treatment of the various BOOT schemes?

25. Units

25a. Ancillary units

The concept of ancillary units pertains to non-productive unis and the cost of the ancillary activities carried out centrally should be distributed over the establishments it serves. Following this approach, head offices and other ancillary units would disappear from the regions they are located and understate the regions' GDP. The 1995 ESA deals with the above situation by stating that "ancillary activities may be carried out in separate location, located in another region than the local KAU's they serve. The strict application of the rule (ancillary activities should be integrated with local KAUs they serve) for geographical allocation of the ancillary activities would result in underestimation of the aggregate in the region where ancillary activities are concentrated. Therefore according to the principle of residence, they have to be allocated where the ancillary activities are situated". However, 1995 ESA does not present a mechanism for achieving this regionalization scheme and further discussions are needed to work toward a clearly spelled-out convention.

25b. Institutional units

A related issue is the present treatment of ancillary corporations as an integral part of the parent corporation and not as a separate institutional unit. However, in financial markets and asset management, separate entities have come into existence that only hold assets or liabilities but do

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

not enter into production. Such entities use legal structures or/and are set-up for specific purposes such as ad-hoc structures specialized in managing portfolios of assets and debts, restructuring agencies, special purpose entities, shell companies, limited liability partnerships or trusts. For these entities, principles have to be formulated whether to treat them as separate institutional units.

Similarly, with the appearance of multi-territory enterprises that operate as a single legal entity in more than one territory, principles have to be adopted whether to allocate the unit to the predominant territory or to use pro rata splitting.

Principles of recognizing these ancillary units as separate institutional units should take into account different residency and the institutional sector of the (ultimate beneficiary) owner, sources of information, etc. Moreover, the sectorization of those units has to be determined.

26. Cultivated assets - rewording
During the System of Economic and Environmental Accounts discussions, it was agreed that the present definition of cultivated assets in the SNA is ambiguous. Should the SNA's definition be tightened as follows: "cultivated assets cover livestock for breeding, dairy, draught, etc. and vineyards, orchards and other trees yielding repeat products ***whose natural growth and regeneration*** is under the direct control, responsibility and management of institutional units"? The words in bold italics replace the words "that are" in the SNA.

27. Classification and terminology on assets
Should the classification of assets be revised in line with the review of other issues such as leases and licenses? Should the tangible/intangible dichotomy be suppressed?

28. Amortization of tangible and intangible non-produced assets
The final report of the ISWGNA on mobile phone licenses includes a brief discussion of the issue of the amortization of intangible non-produced assets. Should this issue be further elaborated for various cases of non-produced assets such as contracts, leases, goodwill and others?

29. Assets boundary for non-produced intangible assets
Should instruments involving the securitisation of future receipts of government be regarded as intangible non-produced assets?

30. Definition of economic assets
Should we add a criterion of 'reliability of measurement'? The SNA currently gives two criteria for an asset - an entity functioning as a store of value over which ownership rights are enforced by institutional units, and from which economic benefits may be derived. Should there be a third criterion "reliability of measurement" to bring the definition more into line

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

with business accounting standards? With this third criterion, some 'assets', such as brand names, could be excluded because it is too hard to quantify them.

31. Valuation of water

When water is no longer a free resource, how should the charge for it be treated? Should it be treated in a similar way to land or mineral resources as giving rise to rent? It is complicated by the fact a large part of the charges is distribution costs.

32. Informal sector

An extract from the resolution of the Fifteenth International Conference of Labour Statisticians (Geneva, January 1993) concerning the distinction between the formal and informal sectors is reproduced as an annex to chapter IV in the 1993 SNA for the benefit of those countries that wish to introduce the distinction between formal and informal sectors into their sub-sectoring of the households sector as well identify the informal sector dimensions in the production structure.

As part of the review, it was considered advisable to review the annex to chapter IV in light of the work undertaken of the Delhi Group and related work on international standards by international organizations including ILO, UNECE, IMF and OECD on the measurement of the non-observed economy.

33. Illegal and underground activities

The 1993 SNA makes no distinction between legal and illegal transactions as long as the exchanges are occurring with mutual consent. While, it is noted that obtaining credible information on these illegal transactions will be very difficult, at the same time it is stated that their exclusion will introduce errors in the accounts including the balancing items. The 1993SNA draws a distinction between illegal activities and underground activities of which the latter activities are defined as those that are concealed from the public authorities for various reasons like evasion of taxes, health and safety regulations. Both the illegal and underground activities may in some countries be a significant part of the economy. It is therefore particularly important to estimate the production from underground and illegal activities even if they may not always be separately identified. A summary of best practices based country experiences should provide further guidelines on their treatment.

34. Government transactions with public corporations (earnings and funding) – super dividend, capital injections and reinvested earnings

While this issue is generally applicable to the treatment of the transaction of dividends (losses) between corporations (quasi-corporations) and their controlling shareholders, in particular the attention will be given to the treatment of transactions between public corporations and government. More systematically, the accrued profits and losses of all public corporations could

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

be treated on similar lines as the reinvested earnings of the resident foreign direct investment enterprises with non-resident share holders. Super dividend or other lump sum payments are made to the government treated as non-financial transactions would allow governments to manipulate the timing of recording; when treated as financial transactions this manipulation would not be possible. Otherwise, capital injections could be perceived as compensation for past and future losses of public corporations that failed to be (or will not be) accrued and therefore should be construed as expenses rather than treated as a financial transaction.

35. Tax revenues, uncollectible taxes and tax credits (recording of taxes)
Expensing tax credit separately for tax revenue is increasingly hampered by the fact that source data may not allow separate recording of expenses, reducing internal comparability. Moreover, uncollectible taxes should not be expected to accrue. An estimated uncollectible amount based on experience could be either deducted from the gross amount under the accrual principle ('net recording") or alternatively recorded as capital transfer ("gross recording"). Another alternative treatment would record unpaid taxes via the other change in volume accounts. Time of recording is an issue for income and wealth tax. For instance, for households it might be preferred to record the taxes at the time of assessment because it affects behavior at that time. This treatment would be a deviation from the accrual principle that calls for recording taxes when the obligation to pay arises.

36. Private, public sector, government sector delineation (sectorization boundaries)
In 1993 SNA, the *notion of control*, which defines the public sector boundary, is more elusively defined. Weak areas refer to special purpose vehicles (SPV), notably created in the context of public private partnerships (PPP) or securitization. Other areas relates to how control is determined, including the link with the "mainly financed" concept for non-profit institutions. Another issue relates the *market versus non-market* distinction. The distinction between government and public corporation might be based on a legal status or whether production takes place at economically significant price. The ESA 1995 has established a rigid rule of 50 percent of the costs to be covered by sales. Is the 50 percent high enough?

37. Activation of guarantees (contingent assets) and constructive obligations
This issue basically pertains to the formulation of the treatment of flows between the original debtor and creditor and between the original debtor and guarantor when the guarantee is activated or between debtor and creditor when collateral is called by the creditor. While the 1993 SNA does not treat these flows, GFSM 2001 describes the treatment of debt assumption involving general government: either acquisition of financial asset, acquisition of equity, capital transfer, or other volume changes. In addition, this issue addresses the recognition of constructive obligations which are not legally enforceable liabilities but are nevertheless expected to result in outflows. The recognition of the latter would result in the relaxation of the economic asset boundary.

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

38. Transaction concept

38a. Change of (economic) ownership (as term)

The principle of ownership is central to the determination of the timing of recording of transactions in financial and non-financial assets (including transaction in goods). However, the 1993 SNA does not explicitly define ownership. The term “economic ownership” better reflects the underlying economic reality of the transaction where risks and rewards of ownership lie.

38b. Assets, liabilities and personal effects of individuals changing residence (‘’migrant transfers’’)

The flows of goods and changes in financial account arising from a change in residence of individuals are treated as imputed transactions in the BPM5, which are offset in the capital account by capital transfers called migrants’ transfers. The 1993 SNA is not explicit on this account. Because no change in ownership occurs, it is proposed that changes in financial claims and liabilities due to change in residence of individuals be treated as reclassification in other changes in volume account

38c. Application of accrual principles to debt arrears

The time of recording principle for scheduled payment is different between on the one hand BPM5, External Debt Guide, and GFSM2001 and the 1993 SNA on the other hand. The first uses the due-for-payment date basis involving imputation of transactions that the liability has been repaid and replaced by a short term debt. The latter uses accrual basis involving no imputation of transactions but continuing to show arrears in the same instrument until the liability is extinguished. If the accrual basis is followed, sub-headings or memorandum items for all or selected arrears might be introduced.

39. Residence

39a. Meaning of national economy

The concept of national economy is closely related to the concept of residence. In the 1993 SNA, it is discussed in terms of ‘’economic territory of a country’’ for which two contradicting criteria are used: “administration by a government” and “free circulation of persons, goods and capital”. Clarification is also needed between domestic and national economy.

39b. Predominant center of economic interest (as term)

With globalization, there are an increasing number of institutional units with connections to two or more economies. The concept of “predominant” center of economic interest has been put forward to address this issue.

39c. Clarification of non-permanent workers and entities with little or no physical presence and/or production

For those enterprises and other entities, production and location might not be useful criteria. As a result, the jurisdiction that allows the creation of and regulates the entity will be considered as the entity’s predominant centre of interest. In case of non-permanent workers with connections to two or more territories, it would be useful to prepare supplementary presentation for countries where

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

the number of non-permanent resident persons is significant, bringing together relevant components of contract services, compensation of employees, workers' remittances and migrants' transfers with short-term non-resident workers. Also harmonization of the residence concept with demographic, tourism, and migration statistics should be sought and any remaining differences spelt out.

40. Goods sent abroad for processing
The BPM5 and the 1993 SNA treat the goods sent abroad for processing differently. The BPM5, as a practical matter, suggest a convention that all processing be assumed substantial and therefore gross flows are recorded. The 1993 SNA only records gross flows in case of substantial processing (reclassification of the good at three digit CPC). The issue is that no change in ownership and thus transaction takes place. Moreover, can a distinction be made between the different levels of processing? It is mentioned that the current treatment of goods for processing in the 1993 SNA was to facilitate input-output analysis. Therefore, any change should take into account this issue.

41. Merchanting
"Merchanting" is a term used in BPM5 for the activity of trading in goods that do not enter the territory of the trader. In such case, the treatment is to report only the margin earned in the territory of the trader. In case the trade is not concluded during the accounting period, changes in inventories are shown as imports (negative if inventories decrease). The issue is not covered in 1993 SNA.

42. Retained earnings of mutual funds, insurance companies, and pension funds
In the 1993 SNA retained earnings of an entity are generally treated as the income and saving of the entity, rather than the owner. However, exceptions are made for life insurance companies, pension funds and foreign direct investment companies, where there is an imputed flow to the policyholders, beneficiaries, and owners, with an equal financial account flow. The ESA 95 introduces an imputed transaction for the retained earnings of the mutual funds where income is attributed to the investors and then reinvested in the fund. That treatment brings about some consistency with the treatment of life insurance and pension funds which are other types of collective investment schemes. Other symmetries of the treatment of retained earning have been suggested, either expand or reduce the imputations. Moreover, the issue of negative earnings has to be addressed.

43. Interest and related issues
43a. Treatment of index-linked (foreign currency) debt instruments
For index-linked debt instruments, changes in principal arising from indexation are recorded as interest. However, should both creditor and debtor approaches for index-linked debt

1993 System of National Accounts (SNA) updating
Summary descriptions of issues accepted for review by the Advisory Expert Group (AEG) -continued

by the first meeting of the AEG

instruments be clarified? Moreover, the 1993 SNA, BPM5 and other manuals mention exchange rates as one of various indicators to which indexation can be linked. However, they are not explicit on whether debt instruments with both principal and interest indexed to a foreign currency should be treated similarly to index-linked instruments or to foreign currency debt instrument.

43b. Interest at concessional rates
Loans with concessional interest rates could be seen as providing current transfer equal to the difference between the concessional interest and the market equivalent. If such transfers are recognized, interest recorded would be adjusted for the same amount. Concessional rates in commercial and international assistance programs should be distinguished because in commercial situations these rates are used to encourage purchases.

43c. Fees payable on securities lending and gold loans
Neither the 1993 SNA and BPM5 discuss the issue of fees payable on securities lending and gold loans. The fee for securities lending is for putting a financial instrument at the disposal of another unit but it does not fit with the definition of interest when the legal ownership is transferred but the economic risks and rewards of the ownership remaining with the original owner. The fee payable on gold loans appears to be a payment for services as gold in this instance is non-monetary gold.

44. Financial assets classifications
With financial derivatives treated as a separate instrument in the 1993 SNA, it would be appropriate to introduce the term “debt securities” to replace “securities other then shares”. Moreover, all types of financial derivatives are currently treated as a single item but there is an interest in splitting derivatives in forwards and options, given their different behavior. Further considerations are to be given to the introduction of employee stock options. Again it is raised whether nonmonetary gold should be classified as a financial asset rather than under valuables in the asset classification. Non-monetary gold being a financial assets would allow for the gold transactions to be netted, in line with financial transactions. Moreover, as a consequence, fees payments to owners under gold loans would be classified as property income rather than a service.

* * *