

B.12 Treatment of Equity in International Organizations That Is in the Form of Unlisted Shares or Nonnegotiable Equity

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A recent Clarification Note² provided guidance on the treatment of participations in the capital of international organizations (IOs)³ and of the respective income. It recommended that all the capital subscriptions in IOs that are not tradable, including those in the form of unlisted shares, be classified based on their economic nature under other investment irrespective of the legal form of the capital (i.e., unlisted shares or other equity). Consequently, the income on such subscriptions should be recorded under primary income – other investment. This treatment introduces a change with respect to current guidelines in the IMF’s Balance of Payments and International Investment Position Manual, sixth edition (BPM6). This Guidance Note describes the necessary changes to update the recommended treatment in both the balance of payments and the international investment position.

SECTION I: THE ISSUE

BACKGROUND

1. **It is a fact that international organizations (IOs) can issue (unlisted) shares and distribute the profits in the form of dividends,⁴ although in most cases the capital of IOs is not in the form of securities (shares).** In this context, should the participations in the capital of IOs and the respective income be reflected in different functional categories depending on the form of the capital? Is this meaningful from a conceptual point of view or should all these participations be included under the same functional category, as the purpose and characteristics of the investment are the same and are not linked to the legal form that capital may take?

2. **The BPM6 classifies capital subscriptions to IOs in portfolio or other investment depending on the legal form of the capital.** Paragraph 6.32, *BPM6* mentions that equity in IOs is excluded from direct investment, even in cases in which voting power is 10 percent or more, so equity contributions are included in portfolio investment (if in the form of securities) or other investment – equity (if not in the form of securities). Equity in IOs would not generally qualify as reserve assets, even if denominated in foreign currency because of the lack of liquidity (i.e., they are not readily available).

¹ Prepared by Carmen Picón Aguilar (ECB) and Kristy Howell (IMF).

² International Monetary Fund (2020), “Treatment of Participations in the Capital of International Organizations and the Respective Income”, available at <https://www.imf.org/external/pubs/ft/bop/2020/pdf/Clarification0324.pdf>. A previous version of the CN was prepared by the European Central Bank and presented at the thirty-second meeting of the IMF Committee on Balance of Payments Statistics in October 2019 (see BOPCOM 19/16b at <https://www.imf.org/external/pubs/ft/bop/2019/32.htm>).

³ International organizations are entities established by formal political agreements between their members that have the status of international treaties; their existence is recognized by law in their member countries; they are not treated as resident institutional units of the countries in which they are located (2008 SNA, paragraph 4.173).

⁴ The Bank for International Settlements (BIS) capital (€1bn) is in the form of unlisted shares. The European Stability Mechanism (ESM) capital (€80bn) is in the form of unlisted shares and its earnings will be distributed to the shareholders in the form of dividends.

Paragraphs 6.32 and 6.106, *BPM6* clearly state that capital subscriptions to IOs are included under portfolio investment if they are in the form of securities.

3. **The participation/subscription of a country in the capital of IOs follows geopolitical and institutional considerations (i.e., only selected countries can be members of a certain IO and the capital subscription is restricted to certain institutions, e.g., the central government or the central bank).**⁵ Due to the “political” nature of IOs, member’s capital subscriptions are determined based on economic and/or demographic indicators of the member countries, and hence they are usually not readily available to the holder. Transactions in the equity of IOs are mostly due to (i) a re-assessment of the share of each country member by the IOs when new countries join or leave; (ii) a re-assessment after certain number of years (e.g., five years in the case of the ECB) to adjust for the change in economic/demographic weights of the country members; and (iii) increases in the paid-up contributions to support the activities of the IOs. None of these transactions are triggered or decided by individual country members (investors). Most probably the only decision (if any) that an individual country member may take is to request joining and/or leaving the IOs, and therefore this decision will be linked to the acquisition/redemption of its participation. In any case, those transactions will be conditional to defined criteria and will in most cases depend on the consent of the issuer (IOs).

ISSUES FOR DISCUSSION

4. **Bearing in mind that the capital subscriptions are not legally and freely (unconditionally) tradable by member countries, it does not seem very appropriate to consider them under portfolio investment, even though they may take the form of (unlisted) securities.** Similarly, if these equities are not liquid and readily available, they should also not be included under reserve assets, even if they are held by the monetary authority and denominated in foreign currency. As recommended by the international statistical standards, it indeed seems appropriate not to record subscriptions to the capital of IOs under direct investment even though these contributions may exceed 10 percent of the voting power of these institutions. Therefore, all the capital subscriptions of IOs that are not tradable would conceptually be more appropriately reported under other investment without making any distinction based on the legal form of the IOs capital.

5. **The classifications of all capital subscriptions of IOs that are not tradable under other investment would better reflect the non-negotiable nature of the participations in IOs;** however, according to the *BPM6*, the classification of investments in “unlisted shares” is not foreseen in other investment. Consequently, taking into account the above-mentioned assessment, this guidance note presents three possible classifications options:

Option (I) – Amend the standard presentation of balance of payments by changing the components *other investment – other equity* (financial account/IIP) and *other investment income – withdrawals from income of quasi-corporations* (primary income) to, respectively, *other investment – equity in international organizations and other equity* and *other investment income – dividends and withdrawals from income of quasi-corporations*.

⁵ This note does not cover international institutions which have capital in the form of tradable equities nor other supranational institutions that are more profit oriented and whose capital is held by other sectors than the central government or the central bank. Such capital would be included under portfolio investment.

Option (II) – Amend the standard presentation of balance of payments by adding a new component under Other investment to cover “equity in international organizations” and introduce changes in the updated Manual to clarify that all capital subscriptions that are not tradable should be classified here. Consistently, a new component under other investment income should be added to cover “dividends and withdrawals from income of international organizations.”

Option (III) – Keep the current standard presentation and components and clarify in the Manual that all the capital subscriptions in IOs that are not tradable should be classified under *other investment: other equity* irrespective of the legal form of the capital. Consistent clarification should be included for the related income as well.

6. **Option I is the preferred one as it reflects the economic characteristics of the participations in the capital of IOs without introducing additional breakdowns in the balance of payments standard presentation.** Option II allows for a more transparent presentation but adds an additional breakdown that may not be necessary since other equity excluding capital subscriptions of international organizations may be a small component for some compiling economies. The third option is similar to Option I with the drawback that a regular user will not identify easily where the capital subscriptions in IOs are reported.

SECTION II: OUTCOMES

7. **The guidance note recommends that the discussion of capital in IOs in *BPM6* be modified to reflect Option I for the treatment of all capital subscriptions that are not tradable under other investment (see also suggested text in Annex I).**

8. The standard presentation for the balance of payments should be modified as follows:

- a. *Other investment – other equity* should be renamed as *Other investment – equity in international organizations and other equity*
- b. *Other investment income – withdrawals from income of quasi-corporations* should be renamed as *Other investment income – dividends and withdrawals from income of quasi corporations*

9. The standard presentation for the international investment position should be amended as follows:

- a. *Other investment – other equity* should be renamed *Other investment – equity in international organizations and other equity*

10. **The Balance of Payments Task Team (BPTT) consultation largely supported Option I, and associated changes to be reflected in the updated version of *BPM6*.** The members acknowledged that the classification of capital subscriptions in IOs under other investment instead of portfolio investment is meaningful due to the non-tradable and nonnegotiable character of these instruments.

Questions for Discussion:

1. *Do you agree with the proposed changes to the standard presentation for the balance of payments and international investment position (Option I)?*
2. *Do you agree with the suggested text changes in Annex I?*

Annex. List of Proposed Updates

Changes marked in red

BALANCE OF PAYMENTS AND INTERNATIONAL INVESTMENT POSITION MANUAL, SIXTH EDITION

5.26 *Other equity is equity that is not in the form of securities.* It can include equity in quasi-corporations, such as branches, trusts, limited liability and other partnerships, unincorporated funds, and notional units for ownership of real estate and other natural resources. The ownership of many international organizations is not in the form of tradable shares and so is classified as other equity. ~~(although equity in~~ **Although equity in some international organizations, such as the BIS is in the form of unlisted shares), this equity is not unconditionally tradable by member countries; therefore, it is not appropriate to classify this equity under portfolio investment. Instead it is classified with other equity under equity in international organizations and other equity.** Ownership of currency union central banks is also included in other equity (see paragraph A3.44).

6.32 Equity in international organizations is excluded from direct investment, even in cases in which voting power is 10 percent or more, ~~so equity contributions are included in portfolio investment (if in the form of securities) or;~~ **instead equity contributions are included in other investment – equity in international organizations and other equity (if not in the form of securities).** Equity in international organizations would not generally qualify as reserve assets because of the lack of ready availability (see paragraph 6.69).

6.62 Other equity is included in other investment, when it is not direct investment or reserve assets. ~~Other equity, as defined in paragraph 5.26, is not in the form of securities, so it is not included in portfolio investment.~~ Participation in some international organizations is not in the form of securities **(or is in the form of unlisted shares that are not unconditionally tradable)** and so it is classified as **equity in international organizations and other equity.** In most cases, equity in quasi-corporations for branches and notional units for ownership of land is included in direct investment; however, it is included in other investment if the share of voting power is less than 10 percent.

6.106 Capital subscriptions to international organizations that are not readily available to the monetary authorities do not meet the definition of reserve assets. ~~These Equity arising from these subscriptions are included in other investment – equity in international organizations and other equity, unless they are in the form of securities, in which case they are classified as portfolio investment.~~

11.107 Other investment income on equity excludes income on direct investment equity and portfolio investment in equity securities. Equity participation in some incorporated or unincorporated enterprises (such as partnership or joint ventures) does not qualify either as direct investment (because the equity participation is below the 10 percent threshold) or as portfolio investment (because they are not equity securities). Such equity participation is classified under other investment (see also paragraphs 5.26 and 6.62) and any income distributed to the owners should be classified in other investment income. Similarly, some investment funds may be organized by and limited to a small number of members but may not meet the definition of direct investment or portfolio investment. Both distributed and reinvested earnings on such investment fund shares are classified under other investment income. **Income on equity in international organizations that is not tradable is also classified under other investment income on equity.**