

**DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG)**

**OUTCOME PAPER #9 (2): SECTOR CLASSIFICATION OF HOLDING COMPANIES THAT ARE  
SPECIAL PURPOSE ENTITIES**

**FEBRUARY 9, 2005**

1. **Topic:** Sector classification of Holding companies that are Special Purpose Entities
2. **Issues:** See DITEG and BOPTEG issue paper #9 ‘The sector classification of special purpose entities’ by Stephan Klinkum and Frank Ouddeken (De Nederlandsche Bank)
3. **Recommendations:**
  - (i) DITEG discussed the sector classification of holding companies that are special purpose entities (SPEs) resident in another economy than the parent company and *not* owning enterprises in the same economy. BOPTEG had agreed in its June meeting that SPEs are separate institutional units and that SPEs in the form of holding companies should be classified on the basis of their own economic function in the host economy as a unit belonging to the financial sector. DITEG was of the opinion and recommends that holding companies that are SPEs should be classified as Other Financial Intermediaries (OFIs), provided that the definition of “intermediation” is modified to take account of the activities of these holding companies.
  - (ii) DITEG also discussed the sector classification of holding companies that are SPEs that are resident in an economy other than that of the parent company and owning companies that are resident in the same economy as the holding company that is an SPE. The following four cases were considered:
    1. *Holding companies that are established as SPEs in an economy for the purpose of owning all the local subsidiaries or production entities in the host economy:* Most members of DITEG felt that the sector of the resident holding company should be based on the predominant activity of the group the “local group”, i.e., those members of the group that are resident in the economy of the holding company that is an SPE, in line with 1993 SNA treatment.
    2. *A holding company that is an SPE that only owns holding companies in the host economy that, in turn, only own subsidiaries in a third economy:* Most members of DITEG felt that the sector of the resident holding company should be classified as an OFI because the predominant activities of that holding company or the entire “local group” are holding activities.
    3. *A holding company that is an SPE that owns subsidiaries in the host economy (both SPEs and nonSPEs) and in another economy:* Most members of DITEG felt that the classification of the holding company that is an SPE should be based on which activity dominates . That is, if the activities of the subsidiaries in the host economy are relatively small compared with the operations of the subsidiaries in another economy, it would be classified as a holding company and as an OFI. If the activities in the host economy are relatively large compared to the operations of the subsidiaries in the other economy, then the holding company that is an SPE should be classified based on the

local group's predominant activities. In effect, the treatment should be the same as in 3(ii)1, and is in line with the 1993 SNA.

4. *A holding company that is an SPE that owns subsidiaries in a third economy and having non-financial sister companies in the host economy:* DITEG agreed and recommends that the holding company that is an SPE should be treated as an OFI, in the same manner as 3(i). The other sister companies' activities would not have a bearing on the classification of the SPE/holding company.
- (iii) However, some members felt that the sector/industry classification of the SPE/holding company should be a holding company in all instances (in line with BOPTEG's recommendation, with the exception of (ii) 5. above). This view was considered to be very important in the case of a currency union as the classification might change between the local economy and the currency union. The reason for this is that the "local group's" predominant activity may not be the same as the group's predominant activity at the currency union level.

#### 4. **Rejected Alternatives:**

- (i) DITEG rejected the alternative to classify holding companies that are SPEs that are resident in another economy than the parent company and *not* owning enterprises in the same economy as financial auxiliaries because the function of these auxiliaries does not comply with the function of these types of holding companies.
- (ii) Although it may be difficult for the resident compiler to determine the sector of a SPE/holding company in a non-resident economy, DITEG rejected the alternative to classify all holding companies as OFIs. A classification of all holding companies as OFIs gives a wrong view of the sectoral breakdown of the economy involved.

#### 5. **Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop on International Investment Statistics (WIIS):**

- (i) *Do the Committee and the WIIS agree with DITEG's recommendation to classify as Other Financial Intermediaries holding companies that are SPEs and that are resident in an economy other than that of the parent company and that do not own enterprises in the same economy?*
- (ii) *Do the Committee and the WIIS agree with the recommendation to classify to the sector of the predominant activity of the "local" group holding companies that are SPEs, and that have been established in an economy to own all the local subsidiaries or production entities in the host economy?*
- (iii) *Do the Committee and the WIIS agree with DITEG's recommendation to classify holding companies that are SPEs and that own only other SPEs and/or other holding companies in the host economy, and which, in turn, own only subsidiaries in a third economy, as Other Financial Intermediaries?*
- (iv) *Do the Committee and the WIIS agree with DITEG's recommendation to determine the sector of a holding company that is an SPE and which owns both subsidiaries in the host economy (not exclusively SPEs) and in another economy on the basis of the predominant activity, which may either be the activity of the local group or as a holding company,*

*depending upon the size of the holding company activity relative to the size of the local group's activities?*

- (v) *Do the Committee and the WIIS agree that a holding company that is an SPE and that owns subsidiaries in a third economy and that has non-financial sister companies in the host economy should be classified as an autonomous entity based on its own economic function and should be classified as an OFI if it has no other function than holding shares of its subsidiaries abroad?*
- (vi) *If the Committee and the WIIS agree with the classification of (some) holding companies that SPEs as OFIs do they agree that the definition of "intermediation" may have to be modified to accommodate the somewhat different nature of holding companies' activities from the more standard intermediation functions?*