

**BALANCE OF PAYMENTS TECHNICAL EXPERT GROUP (BOPTTEG)**

**OUTCOME PAPER (BOPTTEG) # 2**

**JUNE 2004**

(1) Topic: **Activation of Guarantees**

(2) Issues – see BOPTTEG Issues Paper #2

(3) Recommendations:

(i) The group agreed with the current treatment in international statistical guidelines. This is that a guarantee is a contingency until it is activated at which time the old liability is eliminated from the balance sheets of the original creditor and the original debtor, and a new liability is recorded in the balance sheets of the original creditor and the guarantor.

(ii) Concerning the treatment of flows arising from the activation of a guarantee, a strong majority of the group proposed that all changes in balance sheets of all involved parties (original creditor, original debtor, and guarantor) be shown through the Other Changes in Volume of Assets Account. However, some members suggested that the flows between the creditor and guarantor should be treated as transactions. The group recommended that for the reason of consistency and practical considerations, it would be appropriate to record all flows arising from the activation of guarantees in the Other Changes in Volume of Assets Account (also see section 4 for various reasons). One argument advanced was that the terms and conditions of the activation of the guarantee, and the flows that arise, are set at the time the guarantee is agreed and not on activation. It would also be useful to consider arrangements and implications of guarantees arising from direct investment relationships. It was clarified that the actual payments between the creditor and guarantor are financial transactions. One practical problem was noted that might appear in those cases where data on flows are derived from stocks. In the absence of additional information, the changes in positions would include, among other things, changes due to activation of guarantees.

(iii) The group noted some similarities between guarantees, insurances, and credit derivatives; but concluded that guarantees should be treated as distinct from insurances and credit derivatives.

(4) Rejected Alternatives:

A strong majority of the group did not support the treatment of flows arising from the activation of guarantees as transactions. Several arguments were raised, including that the activation of guarantees reallocates the sectoral distribution of existing claims/liabilities; guarantees cross the asset boundary from being a contingency to an actual claim/liability; treatment as transactions would involve imputations; treating one leg (say, between the creditor and the guarantor) as transactions and another (say, between the creditor and the

original debtor) as other volume changes would require imputations of contra entries; and activation may often be related to the liquidation of a debtor.

(5) Questions for the Committee:

- (i) *Does the Committee agree with the retention of the current treatment of guarantees (that a guarantee is a contingency until it is activated)? See 3(i) above.*
- (ii) *Does the Committee agree with the recommendation that all flows arising from the activation of guarantees be treated as other changes in volume of assets? See 3(ii) above.*