

**Eighteenth Meeting of the  
IMF Committee on Balance of Payments Statistics  
Washington, D.C., June 27–July 1, 2005**

**Report of Discussions of Second Meeting of the Advisory Expert Group on National  
Accounts on Issues Submitted by the IMF Committee on Balance of Payments  
Statistics: Report by United Nations**

**Extracted from Reports by  
United Nations, Statistics Office**

**REPORT  
OF  
Second Meeting of the Advisory Expert Group on National Accounts  
8 -16 December 2004  
at United Nations, New York**

*More detailed extract covering issues submitted by IMF Committee on  
Balance of Payments Statistics*

#### **14. Progress on the Work Programme of BPM update: Balance of Payments issues for the SNA review (information)<sup>1</sup>**

133. This session was chaired by Ivo Havinga, UNSD, and Manik Shrestha, IMF, presented the progress on the Work Programme of BPM update (document No. SNA/M2.04/17).

134. The mechanism adopted for seeking solutions to the issues identified to be included in the updated BOP manual provides ample opportunities to all stakeholders to participate. The draft Annotated Outline for the revised BOP manual has raised about 100 questions for which suggested solutions have been invited. The responses received from the interested parties are first considered by Technical Expert Groups (TEGs) specially constituted for the purpose. The recommendations of the TEGs are in turn considered by the IMF Committee on Balance of Payments Statistics (BOPCOM) and if the issues so considered are deemed to have linkages with the SNA, then these are brought up to the AEG. About seven of such issues have been resolved.

135. The progress on the issues since the last meeting of the AEG has been summarized in the document No. SNA/M2.04/17. The AEG expressed satisfaction about the progress of the work.

136. One of the members enquired about progress on the issue relating to the meaning of the “national economy” as the same was not indicated in the document. The aspects of this topic being dealt with by the BOP community are the inclusion of offshore centers and SPEs (discussed under units, below) and the meaning of an economy or economic territory in general and in the context of economic and monetary unions (to be discussed by the BOPCOM in June-July 2005). Several AEG members voiced their concern, as the issue is important for the SNA update and it would be better if the preliminary discussion was held early before the issue is brought up to the BOPCOM for deliberations.

#### **15. Change of economic ownership (decision)**

137. This session was chaired by Ivo Havinga, UNSD, and Manik Shrestha, IMF, presented the issue (document No. SNA/M2.04/18).

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<sup>1</sup> Paragraph numbering from original document has been maintained, in order to allow easier comparison with the longer document that summarizes the discussion on all topics. The full document may be found at <http://unstats.un.org/unsd/nationalaccount/AEG/Papers/m2report.pdf>

138. The reason for considering this issue is that currently the 1993 SNA does not explicitly define ownership, and ownership can be interpreted on either legal, physical or economic basis, which deserves further clarification in the 1993 SNA update. Financial leasing is a typical case in the 1993 SNA where economic ownership with well-defined risks, rights and benefits is recognized. Therefore, the purpose for adopting the term “economic ownership” is to eliminate the ambiguity in all manuals and macroeconomic statistics, which would set a clear timing for recording transactions that change economic ownership. In this regard, it was suggested that business accounting standards should be taken for reference.

139. It was noted that the term “*change of economic ownership*” received a broad consensus in the BOP Committee.

140. The following question was therefore put forth before the AEG: *Does the Committee agree with the proposal to adopt the term “change of economic ownership” instead of “change of ownership”?*

141. The AEG unanimously supported the recommendations of adopting the term “*change of economic ownership*”, though further clarification is warranted, especially about the real meaning of economic ownership.

142. Concerns were expressed about the difficulty in observing changes in economic ownership, e.g. internal transactions among multinational enterprises, re-export, and exclusive export zones. One member cited the example of public railway enterprise, with legal ownership that lies with the finance corporation, and economic ownership attributed to the railway corporation. Others referred to the implications for possible shared ownership of assets and the time at which change in ownership occurs (e.g. signing a contract), as well as issues that still need to be explored, e.g. military contracts.

143. The AEG requested the Canberra II Group for further clarification of the following issues:

- (i) provide better definitions of ownership, i.e. physical, legal and economic ownership, and clarify what constitutes the change of economic ownership;
- (ii) consider the issue of economic ownership as cross-cutting issue with respect to originals and copies, repo arrangements, financial leasing, delivery contracts of military equipments and the like.

## 16. Application of accrual principles to debt arrears (decision)

144. This session was chaired by Ivo Havinga, UNSD, and Manik Shrestha, IMF, presented the issue (document No. SNA/M2.04/19).

145. Debt arrears occur when scheduled payments (repayment of principal or coupons) are not made by their due-for-payment date. The current statistical manuals seem to follow two separate bases for time of recording of debt arrears, and the issue is whether the GFSM and BOPM should align with the SNA on the treatment of debt arrears.

146. The *External Debt Guide* defines arrears as amounts that are past due-for-payment and unpaid. The time of recording basis followed in the *BPM5*, *External Debt Guide*, and *GFSM 2001* is that when a debt liability goes into arrears, transactions are imputed as if the repayment of debt liability had been made and a new short-term liability created. This type of recording conforms to the due-for-payment basis as repayments are recorded at the time they are due.

147. The treatment followed, in principle, in the 1993 SNA and *MFSM 2000* is that repayments of debts are recorded when they are extinguished (such as when they are paid, or rescheduled, or forgiven by the creditor). This type of recording conforms to the accrual basis. Under this approach, arrears will continue to be shown in the same instrument until the liability is extinguished.

148. When a liability goes into arrears, the terms and characteristics of the entire liability or only the portion in arrears may change. If the terms and conditions change with respect to any part of the liability, that part is to be treated as a separate instrument. However, the 1993 SNA does not discuss this issue specifically (for example, whether to treat such events as transactions similar to debt reorganizations or as other changes due to reclassification of instruments).

149. The AEG was asked the following questions:

(i) Does the AEG agree that the time of recording and treatment of arrears be harmonized in various macroeconomic statistics?

(ii) Does the AEG agree with the recommendation that no transactions should be imputed when a liability goes into arrears?

(iii) Which of the two alternative treatments – transactions or reclassification/other changes – is appropriate if the terms and characteristics of financial instruments change when a liability goes into arrears?

150. The AEG members supported unanimously that the various statistics should be harmonized on the treatment of arrears, that no transactions should be imputed, and that arrears should be recorded as reclassification if the terms and characteristics of a liability changes when it goes into arrear.

151. On the question of the term structure of loans under arrear, one member said that a long-term loan remains long-term even if it goes into arrear since we classify loans according to original maturity.

152. The AEG concluded that:

(i) the time of recording and treatment of arrears should be harmonized in various macroeconomic statistics, (ii) no new transaction category will be created for recording of interest in arrears, and (iii) if terms and characteristics of the financial instrument change when it goes into arrear, it should be recorded as reclassification in the other changes in volume of assets account.

153. The AEG asked the IMF to include the clarification of the treatment of arrears in a paper that would also include the treatment of non-performing loans (as noted under non-performing loans, above).

## **17. Residence of households (decision)**

154. This session was chaired by Ivo Havinga, UNSD, and Robert Dippelsman, IMF, presented the issue (document No. SNA/M2.04/20).

155. The presentation was based on earlier discussions in the Balance of Payments Technical Expert Group (BOPTTEG) and the recommendations of the Balance of Payments Committee. The situation presented under this item is arising as a result of globalization and an increased international mobility of labour. Therefore compilers call for more guidance on determining residence of individuals. The importance of symmetry of reporting on both sides was also mentioned.

156. Four questions were presented to the AEG for decision. The experts' views and conclusions are summarized in the sequence of the questions.

157. *Question 1: Does the AEG agree with the approach of harmonization of residence concepts?* Members of the AEG unanimously supported seeking harmonization with the residence concepts of demographic, migration, tourism and education statistics, as long as the conceptual integrity of the SNA can be maintained.

158. *Question 2: Does the AEG agree that “predominant center of economic interest” be adopted?* It was explained that this criterion is needed to decide the residency of persons with multiple residences and migrant workers who work most of the year in a country but spend some time of the year in their home country. In conclusion, the majority of the AEG agreed to adopt the concept “predominant center of economic interest”.

159. *Question 3: Does the AEG prefer the continuation of the existing exceptions for students, patients and ships’ crews? Does the AEG prefer the one-year criterion?* All AEG members were in favor of using the one-year criterion for determining residence. Some members questioned maintaining exceptions for patients or ships’ crews. Most expressed the view that they were indifferent to the exceptions given to patients or ships’ crews, but were strongly in favor of keeping the exception for students, as users want to see the exports of educational services. Regarding ships’ crews, some members expressed the view that these should be treated in relation to the concept of “predominant center of economic interest” of the crews (i.e. households), not of the ship operators. In conclusion, the AEG favored the one-year criterion rather than a discretionary approach, with the existing exceptions of students and patients and with clarifications of the situation of ships’ crews.

160. *Question 4: Does the AEG agree with the supplementary presentation approach proposed in the Annotated Outline for the revision of BPM5?* The AEG supported the supplementary presentation as it is important for those countries that are sources or hosts of large numbers of migrant workers.

## **18. Treatment of multiterritory enterprises (decision)**

161. This session was chaired by Ivo Havinga, UNSD, and Robert Dippelsman, IMF, presented the issue (document No. SNA/M2.04/21).

162. Multiterritory enterprises are single enterprises that are run as a seamless entity having substantial operations in two or more economic territories, so that separate branches can not be identified. The criterion for assigning residency to a multiterritory enterprise has been specified only for an enterprise that operates mobile equipment in several jurisdictions, including ships, aircraft and railways. There is a need to prescribe guidelines generalized to all kinds of activities. At present, there is no guideline for the treatment of enterprises operating under joint jurisdictions of more than one economic

territory (like hydro-electric schemes on border rivers, pipelines running through more than one territory, etc.). With progressive increase in the number of such enterprises, there is a need to prescribe guidelines in the matter.

163. These issues have been discussed first by the BOP Technical Expert Group (BOPTG) and subsequently by the BOP Committee (BOPCOM). The two groups made the following recommendations for the considerations of the AEG:

(i) In the case of multiterritory enterprises, BOPCOM proposes to apply the general principles in BPM5 (at present limited to mobile transport enterprises) to all kinds of activities and to consider other possible factors for splitting (e.g. some operational factors such as shipping tonnage, rather than just equity shares). The complexities of practical implementation should be acknowledged in the revised manual.

(ii) For enterprises operating in the joint jurisdiction zone, which have not been addressed in the present manual, guidance and examples should be provided in the revised one, but flexibility should be allowed in the implementation.

(iii) For enterprises operating both in multiterritory zones and joint jurisdiction zone, the revised manual should indicate the need for collaboration between the compilers of the territories concerned. The implications for other economies, when compiling partner data, should also be noted in the manual.

164. The AEG expressed the view that all attempts should be made to establish the parent-branch relationship for dealing with multiterritory enterprises. [Comment: This multiterritory enterprise issue could disappear if the later decision on branches is not reworded. If no decision-making or record-keeping is needed to qualify as a separate institutional unit, because any production is enough to identify a branch, then operations by multiterritory enterprises in each territory will (almost?) always qualify as separate branches.] One should resort to the present proposal only when establishing such a relationship does not become possible. The task of splitting entities is a complex one. As for the partner data, implications could be in several areas, like BOP, employment, consumption, to name a few.

165. A suggestion was made during the discussions that it would be worthwhile to examine the international accounting standards (IAS) as to how the division of the head office and branches is dealt with.

166. Some members wanted more examples and practical experiences to be part of the guidelines as the split has to be examined on a case-by-case basis. It was suggested



that a group of countries dealing with such problems provide their experiences to be used in developing guidelines.

167. The AEG discussed the issue and reached the following conclusions:

(i) In principle, the group was in agreement that the treatment of multi-territory enterprises should be extended to all kinds of activities when the parent-branch relationship cannot be established.

(ii) International accounting standard board (IASB) recommendations may be examined to see whether some guidelines on the subject exist.

(iii) The problem of joint jurisdiction zones was recognized and the AEG agreed that these need to be examined on the case-to-case basis. Work in this area is required in the affected countries.

## **19. Holding companies, special purpose entities and trusts: clarification of their status as units and residence (decision)**

168. This session was chaired by Ivo Havinga, UNSD, and Robert Dippelsman, IMF, presented the issue (document No. SNA/M2.04/22).

169. Special purpose entities, international business companies, special purpose vehicles and shell companies are the terms used to cover legal structures that have little or no employment, limited operations or limited physical presence in the jurisdiction in which they are created. Such entities are referred herein as SPEs. These are typically used as devices to hold assets and liabilities and do not necessarily undertake production.

170. The issues are whether SPEs are separate institutional units; the determination of their residency; harmonization of the internationally accepted definitions of such entities; and their classification by institutional sector and economic activity. These issues have been deliberated upon by the BOP Technical Expert Group (BOPTTEG) and the BOP Committee (BOPCOM). The two groups made the following recommendations for the consideration of the AEG:

(i) Does the AEG agree that SPEs incorporated in the economic territory, separate from its owners, should be treated as a separate institutional unit?

(ii) Does the AEG agree that SPEs should be treated as resident in their territory of incorporation?

(iii) Does the AEG agree with the approach of separately identifying SPEs on the basis of national definitions, as needed, but not having a standard definition or SPE sub-sector?

171. The AEG noted that SPEs are incorporated by the non-residents and these are treated as separate institutional units in line with general principles, although the SNA does not discuss these cases. One may not insist on the requirement of having a full set of accounts by these entities and in cases where significant production takes place, the problem should be reckoned with to reflect the economic realities.

172. As regards proposal iii, members were of the opinion that efforts should be made to evolve an internationally accepted definition of SPEs and it should not be left open to countries to define them. The group requested some indicative guidelines on the identification of SPEs across manuals, although an internationally standard definition of SPE is not available in light of national diversity.

173. It would be worthwhile to liaise with the working group (OECD Task Force) on financial services.

174. The discussion on this issue concluded with the following observations:

In principle, the AEG agrees with the proposal that SPEs, incorporated in the economic territory separate from its owners, should be treated as a separate institutional unit and be treated as resident in their territory of incorporation, except for SPEs created by government. The issue of SPEs owned by a government but incorporated in another economy should be coordinated with TFHPSA.

## **20. Recognition of branches (decision)**

175. This session was chaired by Ivo Havinga, UNSD, and Robert Dippelsman, IMF, presented the issue (document No. SNA/M2.04/23).

176. The criteria for identification of branches had been discussed extensively by the Balance of Payments Technical Expert Group (BOPTEG) and Direct Investments Technical Expert Group (DITEG). The two groups had agreed on the following recommendations:

- (i) The physical presence criterion would apply only to those industries that require physical presence. For activities (such as financial intermediation and operational leasing) that can be undertaken without physical presence, such a criterion is not required for determining the existence of an institutional unit.
- (ii) Being subject to income tax laws, rather than paying income taxes as in *BPM5*, should be taken as an indicator.
- (iii) Some flexibility is needed, so that the criteria would be used as indicators with compiler's discretion. Not all of the criteria need to be met.
- (iv) The criterion of having separate income statements and balance sheets was considered to be the strongest factor, and would usually be decisive.
- (v) The group noted the importance of where decisions are made and observed that separate accounting could be a reflection of it.

177. The presentation briefly pointed out the current statistical treatment of this complicated issue, when an institutional unit has substantial operations outside its home economy for which no separate legal entity is created. A "branch" – notional resident institutional unit of that economy – needs to be created for statistical purposes. The *BPM5* and the 1993 SNA have similar criteria for identifying the operations of an unincorporated branch as a separate institutional unit.

178. The following points were presented for approval of the AEG:

- (i) Does the AEG agree with the recommendation that physical presence only be required for activities other than financial intermediation?
- (ii) Does the AEG agree that being subject to income tax laws should be taken as an indicator of a branch rather than a requirement?
- (iii) Does the AEG agree that all criteria should be taken as indicators of a separate branch, while noting that availability of separate accounts be given a very strong weight?

179. The AEG agreed unanimously on the first point. It is essential to have significant economic activity rather than a physical presence of financial intermediaries to be recognized as a branch.

180. The group strongly supported the second point stating that being a subject to income tax laws should be taken as an indicator of a branch rather than a requirement.

181. Regarding the third point, the majority of the AEG members considered the criterion for availability of separate accounts too restrictive. They expressed preferences for taking into account the production in the economy and focusing on the identification of this unit rather than seeking its full set of accounts. All criteria should be considered as indicators for a separate branch but not all criteria have to be met.

Even if the entity does not have a full set of accounts, if it engages in significant amount of production from a physical base in the territory over an indefinite or long period, it should be treated as a branch.

182. With the qualification on the third criteria, the group suggests noting that this is a qualification of the BOPCOM conclusion, so further consultation will be needed.

## **21. Goods sent abroad for processing (decision)**

183. This session was chaired by Ivo Havinga, UNSD, and Robert Dippelsman, IMF, presented the issue (document No. SNA/M2.04/24).

184. A change in the treatment from gross to net was recommended by BOPTEG and approved by BOPCOM. This proposal was presented to the AEG for decision.

185. BOPCOM agreed that the value added in goods for processing without change of ownership of the goods should be treated as services in international statistical guidelines, on both conceptual and practical grounds. The current treatment on a gross basis for goods for processing involves imputations of contra entries in change in financial accounts and balance sheets. The identification and measurement of goods for processing is difficult.

186. It was noted that *BPM4* treated the value added in goods for processing as a service and that gross recording of goods for processing in *BPM5* was an effort to be consistent with the national accounts. It was also mentioned that, within the national accounts community, more focus is being given now to the treatment of goods for processing as services. On the other hand, there were suggestions that there should be a presumption against reversing changes made for *BPM5* from *BPM4*. The group indicated a need for consultation with national accounts and international merchandise trade statisticians.

187. The question raised was: *Does the AEG agree with the recommendation that goods sent abroad for processing should be treated as services?*

188. A slight majority of the AEG members supported the net treatment and provided the following arguments in favor:

- (i) Goods received by the manufacturer for processing are not recorded in business accounts of the processors, who do not know their values.

Imputations of values and consequent imputation of contra liability in financial accounts is difficult.

- (ii) There is no change in ownership of the goods.
- (iii) The treatment is compatible with manufacturing services inside the country where the output of the processor is the processing service provided and can be classified as production under contract for a fee.
- (iv) This net treatment is appropriate where processing for a fee is an increasingly common phenomenon in the global market place.

189. Others argued against the change because:

- (i) Conceptually it is difficult to understand that manufacturers can produce services.
- (ii) I-O table compilers like to maintain consistency with merchandise trade statistics and reflect significant transformations in the economy.
- (iii) GAT and GATS have different agreements for goods and services, and trade negotiators want to monitor them.
- (iv) Goods sent abroad for processing are normally recorded on the gross basis by customs and appear as such in merchandise trade, unless they are subject to special custom regime where goods sent in and out temporarily are not subject to taxes. The different recording of goods in merchandise statistics and BOP/national accounts creates problems for users.

190. The AEG observed that the issue paper asked for a clearer definition of goods sent abroad for processing. In BOP and SNA context this concept refers typically to goods sent abroad for processing and then re-imported. Also it was clarified that in processing on a fee basis, processors do transform the goods but do not own material inputs or the resulting output.

191. The AEG did not reach a consensus on the issue though slightly more members supported the net treatment.

192. Finally, the AEG decided that the IMF and UNSD will prepare a paper to explore all aspects of the issue, with pros and cons. After that it will be sent simultaneously to the AEG and BOPCOM for written consultation.

## **22. Treatment of activation of guarantees (information)**

193. This session was chaired by Brian Newson, Eurostat, and Manik Shrestha, IMF, presented the issue (document No. SNA/M2.04/25).

194. Liabilities can be guaranteed by a third party. Guarantees are arrangements whereby the guarantor commits to pay or assume the liability of another entity (the original debtor), if certain conditions are met (such as inability of the original debtor to pay). Guarantees may include repayments of principal and/or interest payments. A debt guarantee involves three institutional units: original creditor, original debtor, and guarantor. Activation of a debt guarantee creates a new liability and the guarantor now becomes the new debtor. This raises issues on how to treat flows between the original debtor and creditor and between the original debtor and the guarantor (the new debtor).

195. The AEG was asked the following questions:

*(i) Does the AEG agree with the retention of the current treatment of guarantees (that a guarantee is a contingency until it is activated)?*

*(ii) Does the AEG agree with the recommendation that all flows arising from the activation of guarantees be treated as other changes in volume of assets?*

196. Several AEG members argued that there are degrees of contingencies among the different guarantees that should be studied case by case.

197. Several members spoke against the use of other changes in volume of assets when guarantees are activated and suggested the use of transactions in the form of capital transfers.

198. It was decided to defer the decision on question i until the AEG has been given more information on the different types of guarantees in order to decide whether they are liabilities or not. On question ii, all members agreed that all flows arising from the activation of guarantees should be recorded as transactions in the form of capital transfers. It still leaves open the question of which of the two benefiting parties is the recipient of the transfer – the creditor or the guaranteed party or both.

199. The AEG suggested that IMF would provide further information and to inform BOPCOM accordingly.

200. Moreover, the coordination with the TFHPSA needs to be maintained.

### **23. Repurchase agreements, securities lending, gold swaps and gold loans: an update (information)**

201. This session was chaired by Brian Newson, Eurostat, and Robert Dippelsman, IMF, presented the issue (document No. SNA/M2.04/26).

202. A securities *repurchase agreement (repo)* is an arrangement involving the sale of securities at a specified price with a commitment to repurchase the same or similar securities at a fixed price on a specified future date. A repo viewed from the cash provider is called a *reverse repo*. When the funds are repaid (along with an interest payment) the securities are returned to the “cash taker”. The provision of the funds earns the cash provider interest that is related to the current interbank rate and not the property income earned on the security “repoed”. Full, unfettered ownership passes to the “cash provider” but the market risk — the benefits (and risks) of ownership, such as the right to holding gains (and losses), and receipt of the property/investment income attached to the security — are retained by the cash taker as if no change of ownership had occurred, in the same manner as when collateral is usually provided. “Full, unfettered ownership” means that the cash provider acquires ownership of the security and may sell it. In some countries the repo market is large. Banque de France has estimated the repo market to approximately 40 percent of the total outstanding French government bonds.

203. *Securities lending without cash collateral* is similar to a repo, except that no cash changes hands. The borrower obtains full and unfettered ownership in the same way, and instead of cash provides the lender with collateral, usually securities. The lender of the securities does not acquire full and unfettered ownership of the securities received as collateral. The lender of the securities receives a payment from the borrower, called a “fee”.

204. Repos are usually undertaken as a liquidity management tool, and they are often used by central banks as part of their monetary policy. The benchmark interest rate in some countries is the repo rate, like in the United States.

205. In the 1993 SNA and *BPM5*, it was recommended that repos/reverse repos should be treated as collateralized loans. One rationale given at the time was that the cash provider did not often have the right to on-sell a security acquired under a reverse repo. However, the right to on-sell has become almost universal. It is this development that has caused one difficulty in the measurement of repos, in that, if the recipient of the security that has been repoed (or lent) on-sells the security, it will be double counted as owned by both the original owner and the purchaser. The solution to the double counting is that the recipient of the security which on-sells should show its “short position” as a negative asset in the instrument involved being recorded.

206. In view of the problems that repos and securities lending both pose for statistical measurement – that the ownership change is not recognized, and the two parties can claim ownership to the same security at the same time – the IMF Committee on Balance of Payments Statistics has given extensive consideration to the issue. The conclusion the Committee reached was that repos should be recorded as collateralized

loans, and that if the security acquired under a repo were on-sold outright, it should be recorded as a negative asset in the instrument being on-sold. For securities lending no transaction should be recognized; if the security borrowed is on-sold, it should be recorded as a negative asset, in that instrument, by the party that borrowed the security. Following the work of the Committee, the Intersecretariat Working Group on National Accounts reached the same conclusion.

207. As part of the Committee's consideration of these transactions, however, several countries agreed to participate in a survey of financial institutions, to find out more about their internal recording practices for repos and securities lending. The result, among other things, was that a significant minority of respondents record repos in what has come to be known as the "four-way-approach", that is, they record them as both collateralized loans and as transactions in the underlying security at the same time. The Committee continues to explore to what extent such an approach could be used for statistical purposes.

208. *Gold swaps* are usually undertaken between monetary authorities. The gold is exchanged for foreign exchange deposits (or other reserve assets) with an agreement that the transaction be unwound at an agreed future date, at an agreed price. *Gold loans or deposits* are undertaken by monetary authorities to obtain a non-holding gain return on gold which otherwise earns none. The nature of gold swaps and gold loans/deposits is similar to that of repos and securities lending, in that the market risk toward the underlying asset remains with the original holder. The statistical implications of gold swaps and gold loans/deposits are complex and have not been fully worked through. Work is still being undertaken by the IMF Committee on Balance of Payments Statistics to address the implications.

209. Few AEG members took the floor on this issue. One member mentioned that his country does not follow the SNA recommendation but records repos as transactions in assets. The obligations to reverse the transactions are recorded as forward positions. If the "four-way-approach" were approved for the SNA, it could be a second best solution for them. Another member pointed out that an increasing number of countries use the "four-way-approach".

210. The AEG concluded that it took note of the problem without offering any solution. The AEG encouraged the IMF to develop the issue further and present a proposal for a forthcoming meeting.



## **24. Treatment of debt instruments (Debt instruments indexed to a foreign currency and Interest on index-linked debt instruments) (information)**

211. This session was chaired by Brian Newson, Eurostat and Manik Shrestha, IMF, presented the issue (document No. SNA/M2.04/27).

212. Two papers were presented under this item as work-in-progress, since they were considered by BOPTEG but not yet submitted to BOPCOM.

213. For the purpose of defining and measuring interest, three categories of arrangements are distinguished: domestic-currency-denominated debt instruments, foreign-currency-denominated instruments, and debt instruments indexed to a foreign currency. Currently, the international statistical manuals treat the effect of exchange rate variations on debt principals differently, depending on whether the instrument is denominated in a foreign currency or indexed to a foreign currency. The former is treated as holding gains, whereas the latter is deemed interest.

### **24.1 Debt instruments indexed to a foreign currency**

214. The first paper on *debt instruments indexed to a foreign currency* raised the question whether there are sufficient differences between a debt denominated in foreign currency and a debt with both principal and coupons linked to a foreign currency to warrant a difference in treatment. If not, the question arises as to what treatment to adopt for the debt instruments with both principal and coupons linked to a foreign currency: the foreign-currency denominated instruments or the index-linked instruments.

215. The IMF recommends that debt instruments with both principal and coupons indexed to a foreign currency should be treated as though they are denominated in that currency. Thus the proposal removes an obvious anomaly by recommending identical treatment for instruments that have economically equivalent characteristics.

216. The AEG noted that this was a work in progress going in the right direction. Regarding next steps, after the BOP Committee's review in June next year, the issue will be brought back for decision to the AEG. Members requested that the full issue paper includes a worked-out numerical example. Several AEG members supported the identical treatment proposed by the IMF.

## 24.2 Treatment of interest on index-linked debt instruments

217. The second paper on *treatment of interest on index-linked debt instruments* focuses on how interest accruals should be determined for the accounting period when principal is indexed. It deals with the case where interest is unknown due to the fact the redemption value of the debt is unknown. The SNA treats the change in the value of the principal outstanding due to the movement in the relevant index as interest over the life of the instrument in addition to any other interest due for payment arising from coupon payments. In practice, the SNA suggests that the movement in the relevant index in the period may be used to estimate interest, while the External Debt Statistics Guide uses the most recent relevant observation of the index and recommends revision of back data to be undertaken when accrued interest costs are known with certainty. The backward revision is something that people are unhappy about. Four alternative broad approaches were examined by BOPTTEG for dealing with indexation of debt instruments: (1) three variations of the current SNA method consistent with the debtor approach; (2) an interpretation of the debtor approach based on yield-to-maturity at the time of issue; (3) an application of the creditor approach; and (4) an embedded derivative approach.

218. Members of the AEG had different views on the merits of these approaches, several of them supporting the yield-to-maturity interpretation of the debtor approach and some giving consideration to the embedded derivative approach. It was mentioned that this discussion is linked to the more general issue of distinguishing holding gains from income.

219. Some members requested that the debts indexed to a stock index should also be looked at as they may accept zero interest with expected capital gains when SNA seems to be based on price index linked.

220. It noted with satisfaction that the ISWGNA already initiated commissioning an issue paper on the underlying principle in dealing with interest under high inflation, which may cross-cut with the issue of interest on index-linked debt instruments. AEG members would like to see worked-out examples when this issue comes back to them for decision.