Work on Improving the Coverage of Illegal Economic Activities (IEAs) in External Sector Statistics

Prepared by the Eurostat

A. IEAs in National Accounts

GNI Recommendations for IEAs

On January 27th, 2012, the European Commission (EC) notified some transversal reservations[1] on the GNI calculation of Member States. Transversal reservation VI is on the inclusion of IEAs in the NA:

> *VI. Inclusion of illegal activities in national accounts*
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> *The ESA 95 provides that illegal activities (e.g., prostitution and production of drugs) fall within the production boundary of national accounts (see paragraphs 1.13(g) and 3.08, last paragraph). The sources and methods used need to be reviewed in order to ensure that illegal activities are properly included in the national accounts.*
>
> *A GNP Committee Task Force concluded its work and presented its results to the GNP Committee in December 2002. The Task Force encouraged Member States to develop studies and research, particularly concerning the three activities which should have the most significant impact on GDP/GNI:* ***drugs, prostitution, and smuggling of alcohol and tobacco****.*

EU IEAs Statistics in NA

By September, 2014,[2] all 27 Member States subject to transversal reservation VI had included estimates of the three stated types of IEAs within their estimates of GDP/GNI. During 2015, these methodologies and estimates were assessed by Eurostat leading to the lifting of transversal reservation VI in all cases.

Over the period 2007-2010, the average value added of IEAs in the EU27[34] is €55.4bn; this covers the three main types of IEAs (prostitution, trafficking and production of illicit drugs and smuggling of alcohol and tobacco products). Figures 1 and 2 show the value of IEAs in the EU27 by type of IEA and the contribution to EU27 GDP by type of IEA as a percentage, respectively.
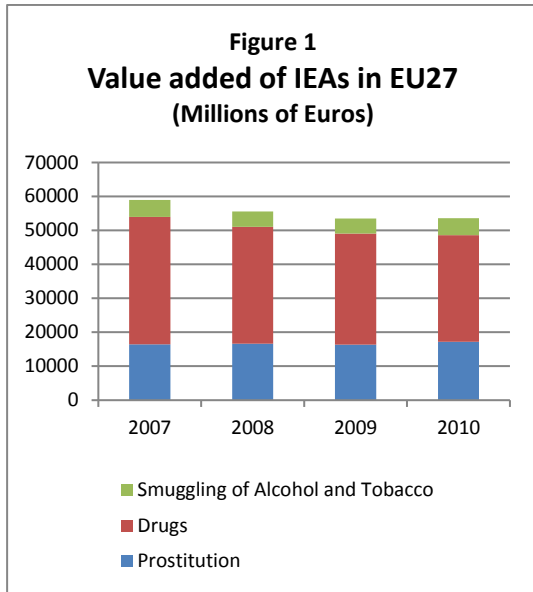
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[1] Transversal reservations are when the EC reserves its position on the accuracy of all EU Member States GNI estimates for EU Budgetary purposes due to non-compliance with the European System of Accounts. This is in contrast to a specific reservation where the EC reserves its position in regard to an individual Member State's GNI estimate compliance.
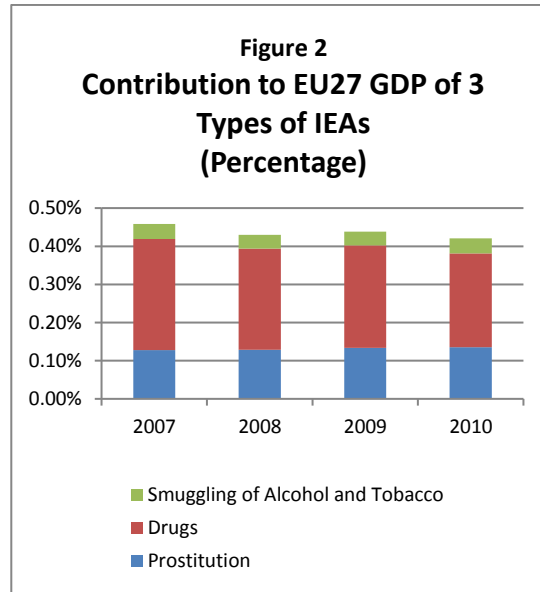
[2] While illegal activities should have been included in NA already according to the *European System of Accounts 1995* (*ESA 1995*), it was common practice in the majority of EU Member States to exclude them. The main reasons were concerns regarding the quality of the estimates and in particular that comparability of NA data between countries would be jeopardized. However, after discussion in the GNI Committee, it was concluded that IEAs have to be included in the NA of Member States with the *European System of Accounts 2010* (*ESA 2010*) revision.

[3] This estimate excludes Croatia as it did not join the EU until 1th July 2013.

[4] Classification of individual consumption by purpose (COICOP) household consumption for prostitution and narcotics data are also a source available with in-progress coverage. See additional information at http://ec.europa.eu/eurostat/statistics-explained/index.php/Glossary:Classification_of_individual_consumption_by_purpose_(COICOP).

Figure 1
Value added of IEAs in EU27
(Millions of Euros)

■ Smuggling of Alcohol and Tobacco
■ Drugs
■ Prostitution

Figure 2
Contribution to EU27 GDP of 3 Types of IEAs
(Percentage)

■ Smuggling of Alcohol and Tobacco
■ Drugs
■ Prostitution

Source: Eurostat

B. Consistency with Balance of Payments – Handbook on IEAs

In order to ensure consistent treatment of IEAs between National Accounts and Balance of Payments statistics the 2015 Balance of Payments Working Group (BOPWG) initiated the preparation of the *Handbook on IEAs* as part of Eurostat's endeavours to improve the implementation of the *European System of Accounts 2010* (*ESA 2010*), and the sixth edition of the *Balance of Payments and International Investment Position Manual* (*BPM6*). The *Handbook* aims to provide guidance on compiling illegal economic activities (IEAs) transactions in the context of the Gross National Income (GNI) recommendations. In addition it presents a starting point for methodological and practical investigations of IEAs which are beyond the scope of the GNI recommendations.

The Handbook includes information about data sources, presents basic models for estimation, and recommends practices how to classify IEAs in NA and BOP. In addition for BOP, it includes references to non-resident/resident identification and geographical breakdown.

The *Handbook* is intended to help the statistical compilers considering:

- that the non-inclusion of IEAs may lead to inconsistencies in the accounting and statistical frameworks,
- the difficulties in finding reliable data sources,
- the challenges in practical implementation of accounting and statistical standards, where the recommendation is to exhaustively record IEAs in NA and BOP,
- the impact of illegal trade on the financial assets and liabilities of a country,
- possible discrepancies between BOP disseminated by the countries which already included those IEAs transactions in their accounts and countries which did not yet include them, and
- the risk of double counting.

Box 1 - Structure of the *IEAs Handbook*

The *IEAs Handbook* is presented in three parts:

- Part I: Current Methodological Framework, Collection (data sources), Compilation/Estimation, and Reporting IEAs in the NA and BOP (Chapters 2- 3)

- Part II: Further Scope of IEAs in the NA and BOP (Chapter 4)

- Part III: Country Cases (Chapter 5)

Part I: Methodological Framework and Current Collection, Compilation/Estimation, and Reporting of IEAs Statistics in NA and BOP

- *Chapter 2* provides a definition, scope, reasons for the compiling of IEAs, and consequences of not recording IEAs. This chapter also presents a summary on the guidance of European conventions and methodological frameworks recommended for the compilation of IEAs statistics based on international statistical standards, including the relevant accounting principles required for the measurement of IEAs.

- *Chapter 3* presents initiatives developed for improving the collection and compilation of IEAs including the efforts to measure non-observed economy (NOE) by using Eurostat's Tabular Approach and the current recommendations, best practices and data sources for the compilation of statistics on three specific IEAs, i.e., prostitution services, production and trafficking of illegal drugs, and smuggling of tobacco and alcohol, in NA and BOP. This chapter also includes IEAs data for European Union (EU) and identifies difficult collection and compilation issues such as double counting and misclassification. It also provides recommendations for deriving the necessary resident-non-resident and geographical breakdowns required by BOP statistics.

Part II: Further Scope of IEAs in the NA and BOP

- *Chapter 4* sets out new aspects for further work in the area of IEAs statistics, such as trafficking of firearms, trafficking of humans, fencing of stolen goods or money laundering.

Part III: Country cases

- *Chapter 5* presents country cases of EU Member States: Bulgaria, Luxembourg, Ireland, Italy, the Netherlands, and Sweden, Italy, and non-EU Member States: Australia. Canada, Mexico, Serbia, and Ukraine.