Joint Thirty-Seventh Meeting of the IMF Committee on Balance of Payments Statistics and Seventeenth Meeting of the Advisory Expert Group on National Accounts

Inter-secretariat Working Group on National Accounts

Remote Meeting
October 26–November 1, 2021

BOPCOM—21/04
SNA/M3.21/04
For discussion

C.4 Merchanting and Factoryless Producers; Clarifying Negative Exports in Merchanting; and Merchanting of Services

Prepared by the Current Account Task Team (CATT)

INTERNATIONAL MONETARY FUND

C.4 Merchanting and Factoryless Producers; Clarifying Negative Exports in Merchanting; and Merchanting of Services[1]

This Guidance Note (GN), jointly produced by the Current Account Task Team (CATT) and the Globalization Task Team (GZTT), focuses on a range of aspects related to global production arrangements and on their recording in the National Accounts (NA) and the balance of payments. In particular, it aims at (A) disentangling the transactions related with global manufacturing arrangements and factoryless goods producers (FGPs); (B) providing some clarifications on the treatment of merchanting transactions, in particular the rationale behind the recording of transactions exclusively on the exports side in the economy of the merchant; and (C) clarifying existing guidance on the definition and treatment of "merchanting of services". Regarding (A), this GN proposes that (i) FGPs be classified in the manufacturing sector and be deemed to produce and sell goods rather than distribution services; (ii) the industrial classification of FGPs should not depend on the affiliation with the contractor responsible for transforming the goods; (iii) international transactions involving final goods within global manufacturing arrangements be recorded gross; and (iv) one additional standard (or supplementary) component(s) be added to the balance of payments goods account to explicitly cover transactions related to goods traded as part of a global manufacturing arrangement (with a further breakdown proposed on a supplementary basis). Regarding (B), this GN clarifies the rationale behind the treatment of merchanting transactions and does not advocate for changes in the current standards. Finally, on (C), this GN suggests that, while "pure" merchanting transactions cannot involve services from a conceptual view, transactions in which an intermediary arranges the supply of a service between a producer and a consumer do exist in practice and should be distinguished from services subcontracting, where the principal maintains the control on the production process. The GN proposes to assimilate these 'intermediation services' to the services provided by agents (as defined in the Balance of Payments and International Investment Position Manual, sixth edition*, paragraph 3.10) and suggests recording the intermediation fees (explicitly or implicitly) as a supplementary "of which" item under trade-related services. On the related issue of bundling of services, this note suggests that the bundled services should not be considered as a new product and as such (i) the package components should be separately recorded in the international accounts; and (ii) the output of a service arranger should be measured by the value of the service fee realized on services which are purchased for resale.*

SECTION I: THE ISSUE

BACKGROUND

1. **Although globalization is not a new phenomenon from a statistical perspective, national accounts (NA) and the balance of payments compilers around the world increasingly struggle in capturing the activities related to this phenomenon in macroeconomic statistics.** Clearly, the deepening of globalization in general, combined with an unprecedented expansion of the activities of multinational enterprises (MNEs) in particular, require a closer examination of the various aspects of

[1] Prepared by Mr. Jens Walter (Germany), Mr. Casper Winther (Denmark), Mr. Sören Burman (Denmark), Mr. Michael Connolly (Ireland), Mr. Rodolfo Ostolaza (OECD), Ms. Antonella Liberatore (OECD), Ms. Jennifer Ribarsky (IMF), and Ms. Silvia Matei (IMF)

recording the production processes under "factoryless goods production" arrangements and other issues arising from globalization.

2. **The *System of National Accounts, 2008* (*2008 SNA*) and the *Balance of Payments and International Investment Position Manual, sixth edition* (*BPM6*) have not given prominence to these phenomena.** Global production is not mentioned explicitly in the *2008 SNA*, while *BPM6* includes additional information on global manufacturing that is, however, not sufficiently detailed.

3. **More recently, important strides into understanding the nature of transactions related to global production—including the identification of the typology of various global production arrangements—have been made.**[2] However, further guidance is needed to better conceptualize the global production arrangements in general and the transactions involved within the SNA and balance of payments framework.

4. **In the context of the update of the international statistical standards (ISS), this task has been assigned to both the Globalization Task Team (GZTT) and the Current Account Task Team (CATT).** Considering the synergies and close interdependence in the coverage of these topics, it was decided to merge the work of the two teams and to prepare a common Guidance Note (GN) that would better reflect the conceptual context, typology and recording of various global production arrangements in the SNA and BOP in a harmonized, holistic approach. The joint team draws on the work undertaken by previous expert groups and the aforementioned methodological guides with the intent of providing clarifications to concepts and treatment of global production in the new set of SNA and BPM.

5. **This GN focuses on a range of aspects related to global production arrangements and makes suggestions for their treatment in the SNA and BOP.** In particular, it aims at (A) disentangling the transactions related with global production arrangements and factoryless goods producers (FGPs); (B) providing some clarifications on the treatment of merchanting transactions, in particular the rationale behind the recording of transactions exclusively on the exports side in the economy of the merchant; and (C) clarifying existing guidance on the definition and treatment of "merchanting of services".

ISSUES FOR DISCUSSION

A. Goods Traded Within a Global Manufacturing Arrangement and Factoryless Goods Producers (FGPs)

6. **Global production arrangements are not sufficiently addressed in the *BPM6* or the *2008 SNA*.** The *BPM6*, Box 10.2 covers briefly the "recording of global manufacturing arrangements", while paragraph 10.42 discusses the borderline in recording transactions under a merchanting arrangement vs. the processing type arrangement. However, neither the *BPM6* nor the *2008 SNA* covers explicitly the treatment of FGPs. To clarify the various types of global production arrangements, *the Guide to Measuring Global Production* (*GMGP*) provides a typology of the various types of arrangements using

---

[2] These efforts culminated with the preparation of the Guide on "The impact of Globalization on National Accounts" (https://unece.org/DAM/stats/publications/Guide_on_Impact_of_globalization_on_national_accounts__web_.pdf), also referred to as *Globalization Guide*, and the "*Guide to Measuring Global Production*" (or *GMGP*), (https://unece.org/DAM/stats/publications/2015/Guide_to_Measuring_Global_Production__2015_.pdf)

the *BPM6*, the *2008 SNA,* and the *International Standard Industrial Classification of All Economic Activities, Revision 4* (*ISIC Rev. 4*) as a starting point.

7. **The distinction between a manufacturer who outsources part of the transformation to contractors while maintaining ownership of the materials (processing type of transaction) and a distributor simply buying and reselling goods (e.g., plain merchanting type transaction) is not contentious.** Compilers consider such treatment reasonably clear, but it becomes more contentious when the principal[3] provides critical inputs such as intellectual property products (IPP) services (i.e., the blueprints of the products)—which may explain a significant portion of the value of the final good—controls the production process, and controls the output, even if the principal does not have ownership of the material inputs during the transformation.

8. **While *BPM6* paragraph 10.42 [4] does not explicitly address factoryless goods production, the *GMGP* interprets "the merchant who is the organizer of a global manufacturing process" as the current guidance in the FGP case.** Accordingly, the revisions to the *BPM6* and the *2008 SNA* should provide explicit guidance on cases where the value from these additional IPP related services is much larger than the value related to distribution services, and explicitly address specific cases of factoryless goods production.

9. **The *GMGP* argued that the supply of IPP, crucial to the transformation of a given good, should be considered as an input to the production in line with material inputs.**[5] This would imply that the activity of principals engaged in so-called FGP arrangements would be aligned with the principals engaged in the so-called processing arrangements, and would thus recommend that they are to be classified as manufacturing, even if there is no ownership of the material inputs during the transformation. The Advisory Expert Group on National Accounts (AEG) at its 2013 meeting agreed with this recommendation stating **"*factoryless producers—supplying intellectual property capital and marketing services and controlling the production process while using contract manufacturers to produce goods—are to be considered goods producers and should not be classified in distributive services*."**[6]

10. **The 2019 meeting of the technical subgroup (TSG) of ISIC recommended no changes in the current guidance on the classification of the principal in ISIC based on the ownership of input materials as discussed in paragraphs 136–145 of the *ISIC Rev.4* because no firm recommendations for improvement were available noting that the identification of FGPs was difficult.** However, the TSG recommended that the text in the ISIC manual could be further clarified that

---

[3] The term "principal" is used for the companies organising and controlling the global production arrangements.

[4] "If the physical form of the goods is changed during the period the goods are owned, as a result of manufacturing services performed by other entities, then the goods transactions are recorded under general merchandise rather than merchanting. In other cases where the form of the goods does not change, the goods are included under merchanting, with the selling price reflecting minor processing costs as well as wholesale margins. In cases where the merchant is the organizer of a global manufacturing process, the selling price may also cover elements such as providing planning, management, patents and other know-how, marketing and financing. Particularly for high-technology goods, these nonphysical contributions may be large in relation to the value of materials and assembly."

[5] Paragraph 2.69 of UNECE (2015), *Guide on Measuring Global Production*.

[6] https://unstats.un.org/unsd/nationalaccount/aeg/2013/M8-5.PDF

the recommendations of the classification of FGPs in *ISIC Rev.4* apply to the cases where the FGP utilizes a non-affiliated contractor, either abroad or in the resident economy.[7] It should be noted that the distinction between affiliated and non-affiliated entities was not part of the recommendation of the *GMGP* and the AEG. The *GMGP* did not recommend making a distinction between affiliated and non-affiliated entities in the case of contract manufacturers, but to treat the FGP production arrangements consistently across the board. However, it should be noted that in the case of affiliated entities, the transfer pricing might have significant impact in the goods transactions.

11. **As a consequence of the AEG recommendation to treat FGPs (that do not own material inputs) as producers of goods, the *GMGP* proposed that the output of the principal be recorded gross, and that the expenses paid to the contractor be considered as an input to production.** This would result in a consistent treatment for global manufacturing arrangements where the principals own some or all of the material inputs along with the IPP (a so-called processing setup) and arrangements where only the IPP is owned by the principal (a so-called FGP setup).

12. **The *GMGP* also discusses whether or not the output of the contractor should be considered as a good or a service, and thus if the import of the principal should be recorded under goods or services,[8] however without a firm resolution.**[9] The current treatment of the output of the contractor in a processing setup is as service, even if the contractor supplies some of the material input (recorded as manufacturing services on physical inputs owned by others). If the activity of the contractor in a FGP setting is considered to be the same, regardless of whether or not the principal owns some or all of the material inputs, then one could argue that the production of the contractor is a service. However, this would imply that if the output of the contractor (that owns the material inputs) is considered a service, while the output of the principal is considered a good, we would have a paradoxical situation where the principal's production of goods is undertaken with the input of services only.

13. **The distinction between goods and services, and between goods and services providers may become more and more blurred.** Nowadays most high-tech products have goods (the hardware) and services (software, research and development (R&D)) components which are hard to disentangle. Similarly, the output of companies engaged in global production chains may be related to goods or services. Nonetheless, the output of the contractor should rather be recorded in goods and not in services if the contractor supplies the material inputs that it transforms into manufactured products, while the IPP and the production process are under the control of the principal.

14. **Recording the output of the contractor as a good or a service depends on whether or not we consider a given global manufacturing arrangement as processing—as commonly understood—or as an FGP arrangement (where IPP and the management of the production process are provided by the principal).** If the contractor supplies (and thus owns) the material inputs during the transformation, and the transfer of ownership of the final goods to the principal (who generally

[7] https://unstats.un.org/unsd/classifications/ExpertGroup/TSG-ISIC2019/Summary_Report_TSG-ISIC_2019.pdf

[8] The activity of contractors is considered as manufacturing in both cases and are classified within the manufacturing industry.

[9] The task force responsible for drafting of the *GMGP* did not agree on whether or not the output of the contract manufacturer in an FGP arrangement should be classified as goods or services, but the majority supported treating the output as goods. The discussions are further described in paragraph 2.87 to 2.96 in the *GMGP*.

provides only the IPP) is done after the transformation, we consider this as a FGP type arrangement, and thus the output of the contractor will be considered a good. If, however, the principal owns some or all of the material inputs along with the IPP during the transformation, the output of the contractor is considered as a service (even if the contractor supplied some of the material inputs during the transformation).

15. **Table 1 shows the output of both the principal and the contractor, depending on the type of global production arrangement they are involved in.** The table illustrates that, for the output of a contractor to be considered as a service, it should be involved in a processing type arrangement. Annex I illustrates the recording of transactions for global manufacturing arrangements in the production account in the NA and in the balance of payments using three case scenarios. These cases closely follow the example of the production of an athletic shoe, used in the *GMGP*. It also shows the flows of goods and services typical for a processing arrangement and those typical for an FGP arrangement.

Table 1. Output of the Principal and Contractor by Production Arrangement

Type of Arrangement	Output: Services	Output: Goods
Processing		
Principal		X
Contractor	X	
FGP		
Principal		X
Contractor		X

16. **Annex II proposes a decision tree to help the compilers, while identifying these transactions, to classify them in relation to processing, FGP type arrangements, and merchanting.**

17. **In order to distinguish the trading activities within a global manufacturing arrangement (both processing and FGP type arrangements) the GN proposes that a distinct sub-item called "Goods traded within a global manufacturing arrangement" is introduced under the balance of payments standard component of Goods.**

18. **Cases 1–3 in Annex I show that if a principal changes from one type of arrangement to another (e.g., from a processing arrangement to a FGP type arrangement), it could result in different figures recorded in goods, even if the physical flows of goods are unchanged.** In order to shed light on the goods flows related to global manufacturing a further breakdown of the new item "Goods traded within a global manufacturing arrangement" could be introduced to distinguish between the flows of the final goods and those of material inputs (in line with the change of ownership principle) in a global manufacturing arrangement.[10] This additional breakdown would only be applicable for the country in which the principal is resident.

[10] Some of the final goods purchased abroad after manufacturing abroad might be returning to the domestic economy of the principal and should be adjusted in the transition between merchandise trade and balance of payments statistics to avoid double counting of imports. This should be addressed in more detail in the chapter discussing the transition from ITGS to BPM/SNA concepts, as well as in the GN B.10 *Auxiliary Reconciliation Tables*.

Suggested Options for Recording the Global Production Arrangements

19. **Considering the challenges of identifying these transactions and their distinction from the "pure" merchanting activities, as well as the practical aspects of data collection, two options that introduce relevant indicator(s) but as *supplementary items* to the balance of payments standard components, are proposed.**

20. **Option 1: One supplementary component under General merchandise.** Under this scenario, all sales/purchases of goods related to global manufacturing arrangements by the principal (e.g., both processing and FGP arrangements) would be recorded indistinguishably (on a gross basis) under the proposed supplementary item, covering:

a. On the exports side: all sales of *input materials* and *final* goods by the principal

b. On the imports side: all purchases of *input materials* and *processed* goods by the principal

21. **Option 1, as illustrated in Table 2, proposes a simplified approach to recording transactions related to global manufacturing arrangements by the principal (e.g., both processing and FGP arrangements) that takes into account countries' source data limitations.** However, to the extent some inputs acquired/sold under these arrangements meet the definition of merchanting, such transactions may be reclassified from merchanting, thus causing potential breaks in series. Further detail could nevertheless be proposed for development in the Trade manuals and/or followed separately by interested countries outside the BPM Standard classification.

Table 2. Option 1 (All Processing and FGP Arrangements are Reported by the Principal and Lumped Together in "*of Which Goods Traded Within the Global Manufacturing Arrangements*" Category Under General Merchandise)

1.A.a Goods (P61/P71)
- 1.A.a.1 General merchandise on a BOP basis
  - *Of which:* 1.A.a.1.1 *Re-exports*
  - *Of which: 1.A.a.1.2 Goods traded within a global manufacturing arrangement*
- 1.A.a.2 Net exports of goods under Merchanting
  - 1.A.a.2.1 Goods acquired under merchanting (negative credits)
  - 1.A.a.2.2 Goods sold under merchanting
- 1.A.a.3 Nonmonetary gold

22. **Option 2: Supplementary components distributed between the general merchandise and the net export of goods under merchanting.** Under this scenario, supplementary items are proposed separately for:

a. General merchandise on a BOP basis (covering the final/processed goods and those input goods procured from other countries by the principal), and

b. Net exports of goods under merchanting (covering the input goods procured by the principal from third parties and sold to the contractor).

23. **Option 2, as shown in Table 3, proposes a distinct supplementary recording of the net export of material inputs that are procured by the principal abroad and sold to a contractor abroad and is recorded as an of which item under Net exports of goods under Merchanting.** This option would avoid the break in the time series mentioned above.

Table 3. Option 2 (Separate Supplementary Components in the Goods Account)

1.A.a Goods (P61/P71)
- 1.A.a.1 General merchandise on a BOP basis
  - *Of which:* 1.A.a.1.1 *Re-exports*
  - *Of which: 1.A.a.1.2 Goods traded within a global manufacturing arrangement*
- 1.A.a.2 Net exports of goods under Merchanting
  - 1.A.a.2.1 Goods acquired under merchanting (negative credits)
    - *Of which: 1.A.a.2.1.1 Input goods acquired from the third parties by the principal within a global manufacturing arrangement*
  - 1.A.a.2.2 Goods sold under merchanting
    - *Of which: 1.A.a.2.2.1 Input goods sold to the contractor within a global manufacturing arrangement*
- 1.A.a.3 Nonmonetary gold

24. **Global production arrangements affect more than just the goods and services account.** Another aspect of global manufacturing arrangement, which is out of scope for this GN, is the outsourcing of all inputs, including the IPP, to an affiliated enterprise abroad. This is leaving the "principal" (who outsourced everything) with no trade flows related to the global manufacturing arrangement, but the recipient of income from the activity of affiliates abroad. Thus, one cannot draw conclusions on the effects of globalization on a single economy by looking only at goods and services since MNEs can move the ownership of goods and IPP between countries in a global production arrangement, to better fit their strategical goals. To get the full picture, the activity of domestics MNEs in other countries have to be taken into account as well. Therefore, the figures on global production arrangements should be supplemented with the figures from direct investment income from MNEs. An analysis of the manufacturing groups in Denmark showed that roughly one third of the earnings of production abroad was generated in affiliates, and thus recorded as primary income and not as goods and services.[11]

25. **GN C.2 *Goods, Services, and Investment Income Accounts by Enterprise Characteristics* has proposed a presentation of selected balance of payments items by enterprise characteristics such as size, ownership (including a distinction of MNEs), and activity.** However, to get a better picture of the effects on globalization of an economy, an alternative presentation of the balance of payments items related to the globalization should be defined, including the relevant goods and service items. This GN presents an alternative to the breakdown proposed by the GN C.2 (Annex III). The proposed breakdown includes "Trade within a global manufacturing arrangement" as an "Of which" item of the "Goods and services" item and includes "Direct investment" as an "Of which" item under the item "Investment income" for the ownership groups "MNE" and "Controlled from abroad". As in GN C.2, these additional breakdowns are proposed as supplementary items to be reported on a voluntary basis.

[11] https://www.dst.dk/analysepdf/32695

B. Clarifying Negative Exports in Merchanting

26. **According to *BPM6*, paragraph 10.44 (a) and 10.45 the purchase of goods for merchanting has to be recorded as a negative credit in the international accounts.** The reason for treating it as a negative export rather than an import is not readily explained neither in the *BPM6* nor the *2008 SNA*. More clarification was requested by compilers on the reasoning of the current treatment.

27. **It is important to recall that, under the former *BPM5* and *1993 SNA*, the trade margin derived from "merchanting" was recorded as an export of services in net terms by the economy where the merchant resides.** No external flow of goods was recorded in that economy notwithstanding that there is a change of ownership for those goods concerned. As this recording was a clear deviation of the basic change of ownership principle, it was decided that, under the *BPM6* and the *2008 SNA*, "merchanting" activities should be recorded under goods with both gross and net values shown, with net amounts included in the goods aggregates.

28. **The idea to follow the change of ownership principle is also expressed by paragraph 10.43 in the *BPM6*: "Goods under merchanting are recorded in the accounts of the owner in the same way as any other goods it owns."** However, from this, it is still not clear why a net recording in the aggregates was preferred over gross reporting. An argument in favor of net recording is given by the *GMGP* (paragraph 10.16) stating that "…a net recording of merchanting of goods in the balance of payments is particularly motivated by the possible existence of speculative trade (gold, grain) and the huge expansion of imports and exports that may result from…" gross recording.

29. **However, it could be argued against that commodity trading usually takes place via (financial) derivatives rather than the exchange of the underlying commodities.** Therefore, inflation of export and import figures due to arbitrage should be negligible, hence the gross recording would be favored. Other reasons may also play a role, such as the fact that the margin earned by merchants can be seen as a service in the country of the merchant (see *2008 SNA*, paragraph A3.158): "The *2008 SNA* recommends that goods acquired by global manufacturers, wholesalers and retailers and those cases of commodity dealing being settled in the commodity should be recorded as negative exports on acquisition and positive exports on disposal. The difference between the two appears in exports of goods but appears as the production of a service in the merchant's economy, analogous to trade margins applied to domestically traded goods." Expressed in another way, the recording of the acquisition and sale of goods as negative and positive credits under "net exports of goods under merchanting" under the goods triggered to keep the continuity with the former service item (merchanting) while simultaneously adhering to the conceptual rule of gross recording of goods import and export.

30. **Furthermore, goods under merchanting are recorded only for the merchant's economy of residence.** For the other countries, the export or import should be classified in the customs documents of these countries as general merchandise, not differently than any other export or import. Treating the purchase of goods for merchanting as a negative export assures a global balance of the accounts. The team (proposing the current treatment) recognizes the existing challenges posed by this recording and the potential bilateral asymmetries generated in the overall trade. Nevertheless, if these purchases were considered as imports and exports in the merchant's country, the global flows of the traded goods would be double counted.

31. **The above discussion makes it clear that not a single explanation was the reason for the current treatment, but a number of considerations.** This is best summarized in an email exchange cited here from the IMF's Committee on Balance of Payments Statistics Meeting (BOPCOM) paper 06/31 "*BPM5* Update: Goods for Processing and Merchanting" discussed at BOPCOM in October 2006 in Frankfurt reporting from the AEG: "There was considerable discussion leading up to this agreement among AEG members, as the various issues that were raised in the paper were debated in some depth. The outcome was a compromise among those that were concerned about the implications of gross reporting for the trade data, those concerned about the change of ownership principle and those that saw a service being provided".

C. Merchanting of Services

32. **Merchanting of services is not conceptualized in the *2008 SNA* and the *BPM6*.** However, merchanting of services is mentioned in *BPM6* paragraph 10.160 in the context of subcontracting.[12] While *BPM6* does not provide a clear definition of subcontracting, the arrangement is likened to the concept of "outsourcing". More clarity comes from paragraph 137 of the *ISIC Rev. 4*. Here, the term outsourcing is also used as a synonym of subcontracting: "Outsourcing is a contractual agreement according to which the principal requires the contractor to carry out a specific production process". It becomes clear from the ISIC that outsourcing/subcontracting cover a wide range of arrangements, including (a) cases where the principal completely sub-contracts the production process/service delivery, (b) cases where only a part of the production process is subcontracted, and (c) cases where several parts are subcontracted and bundled by the principal before selling them to the consumer.

33. **In all cases above, *BPM6* recommends the gross recording of the transactions.** It is argued in paragraph 10.160 of the *BPM6* that this treatment is applicable because it is assumed that the arranger buys and sells the services. A quite similar view is reflected in the activity classification of a principal in *ISIC Rev. 4* (paragraph 142). It is stipulated that in all cases of outsourcing of services—including the complete production—the principal is classified as if he is carrying out the production process itself (i.e., according the appropriate service industry and not in section G (Wholesale and retail trade) like a merchant). However, without reverting the *BPM6* guidance, the *Globalization Guide* (Chapter 6) and the *GMGP* (Chapter 10) both recognize the issue of merchanting of services as an area for future work and open the door to a possible change in the recording standards.

34. **Building on the above-mentioned literature, this GN questions whether the currently recommended treatment for subcontracting/outsourcing/services merchanting is appropriate in all cases.** It is using the simplified scenarios (a), (b), and (c) to illustrate the various lines of reasoning.

Case (a): Full Outsourcing

35. **This case comes closest to the idea of "merchanting of services".** The crucial question with regard to "service merchanting" is if it is adequate to view the economic relation of the counterparts in the case of outsourcing/subcontracting and "service merchanting" as identical, thus justifying a similar treatment? It can be argued from the definition given in the *ISIC Rev. 4* that outsourcing/subcontracting is

[12] The *Manual on Statistics of International Trade in Services 2010 (2010 MSITS)* mentions service merchanting in paragraph 3.62.

different from what is defined as merchanting in the case of goods[13] by the relevant international standards. Subcontracting is related to a bilateral relationship between the principal and a contractor. The relation between them is in most cases oriented towards a longer-term cooperation, where the principal will most often maintain a direct contact with the customer and carry the risk and responsibility of supplying the service. In contrast, merchanting is a trilateral relationship where the intermediary, the producer and the consumer together form a kind of triangle of service-related transactions in which the involvement of the intermediary in the provision of the service is quite limited (see Figure 1 below). For this reason, "service merchanting" should not be seen in the same way as subcontracting.

36. **Equally important in this context is that one of the essential conditions which define merchanting (of goods), the change of economic ownership, cannot be applied to services.** From a pure conceptual point, ownership rights and services do not (in general) go together according to the international standards. The *2008 SNA*, paragraphs 6.17 and 6.21 clearly state that services "are not separate entities over which ownership rights can be established. They cannot be traded separate from their production". Paragraph 10.8 of the *BPM6* and Box I.1 of the *MSITS 2010* echoes this definition.

37. **As the production of a service generally coincides with its consumption, it can be concluded from the current rules that a service cannot be traded like a good.** The service is always directly delivered from the producer to the consumer. This view is supported by paragraph A 5.4 of the *BPM6 Compilation Guide* which stipulates that for compiling balance of payments statistics by partner country, the partner attribution should be based on the economy of residence of the provider and the recipient of the service. The time of recording is the time the service is provided (*BPM6*, paragraph 3.47). It follows from the above that from a pure conceptual view following the current standards, services cannot be traded in the same way as goods and "pure" merchanting transactions cannot involve services.[14]

38. **Nevertheless, transactions in which an intermediary arranges the supply of a service without being engaged in the actual provision of the service do exist in practice.** Such transactions could be assimilated to those defined in *BPM6* paragraph 3.10, when "one unit (an agent) arranges for a transaction to be carried out between two other units in return for a fee from one or both parties to the transaction". The recommended treatment in these cases is to record in the accounts of the agent only the fee charged for the facilitation of the services rendered.

39. **Importantly, the services intermediated by Digital Intermediation Platforms (DIPs) would naturally fall under this category.** Provisional guidance on the treatment of these transactions implies that DIPs never acquire ownership of the goods and services they intermediate, and therefore only the intermediation fees should be recorded in the balance of payments (OECD-WTO-IMF *Handbook of Digital Trade*, section 5.2). However, this refers only to explicit fees while, in practice, there could be implicit charges in both digital and conventional intermediation activities.[15]

[13] Goods never enter the economy of the merchant and the goods are not transformed.

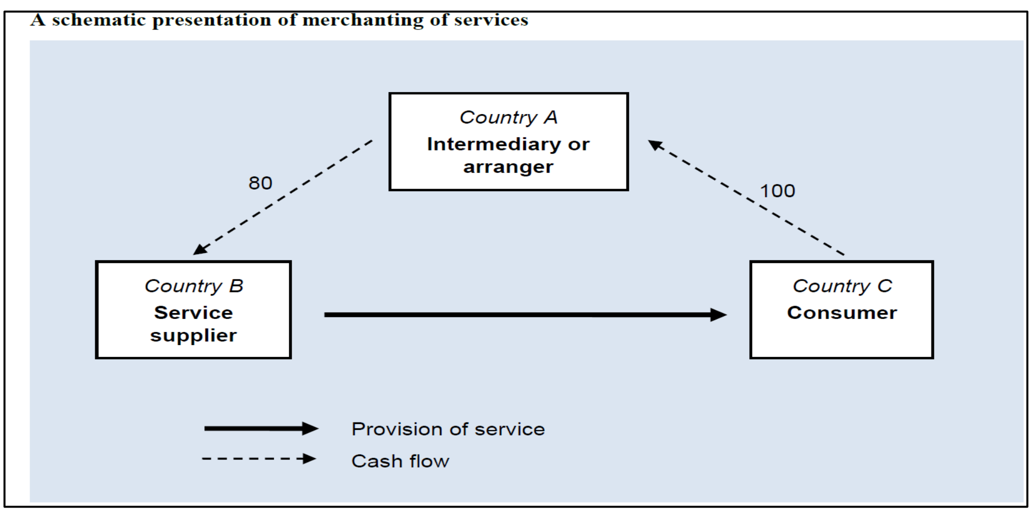
[14] Except for some knowledge-based products, which are storable like software or blueprints.

[15] Moreover, the arranger (intermediary) can charge fees to the consumer, to the actual service provider, or to both parties, either explicitly or implicitly. Future guidance on this should also be considered.

40. **In the case of implicit intermediation fees, the difference between the value of the service acquired and the value of the service sold would constitute the basis for the recording.** This difference would reflect the fee obtained by the intermediary, which, in practice, behaves as an agent even when not working for an explicit commission (*GMGP*, paragraph 10.15 and 10.34). In addition, as services are in general not separate items over which ownership rights can be established, the difference stemming from purchase and resale and the explicit fee of an agent can, in practice, be considered the same thing. **Therefore, the services intermediated without involvement could be recorded under trade-related services as a supplementary "of which" item,** and not (like subcontracting) under the relevant service category. This treatment, which is in line with the line of argument provided in the *Globalization Guide* (paragraph 6.37), would acknowledge that the arranger neither produces nor consumes the service. Users would be better informed of the real character of these flows compared to the current gross recording. An illustration of the recommended recording for the revised *Extended Balance of Payments Services Classification 2010* (*EBOPS 2010/* (*MSITS 2010*)) following the new breakdown of services as proposed by the GN C.6 *Trade in Services Classifications* is provided in Annex IV.

41. **However, the suggested recording has a disadvantage when it comes to the practical question on how to collect the relevant information in the case of implicit fees.** From Figure 1, it becomes clear that compilers have to consider both the monetary flows and the service provision. The chart shows that a service is provided by Country B directly to Country C. In contrast, the financial flows consider the role of Country A as an intermediary. Particularly, if the compilation is done based on firms' financial records, Country B may record an export to A (rather than to C) and Country C may record an import from A (rather than from B). Only Country A knows the actual (implicit) intermediation fee.

Figure 1. A schematic Presentation of Merchanting of Services



Source: Guide to Measuring Global Production.

42. **Both countries, B and C, require additional information for a proper recording.** To determine the actual direction of the service provision, it can be assumed that countries, at least thanks to guidance provided by the *BPM6 Compilation Guide* (paragraph A 5.4), already tackle the problem of divergent financial and real flows in the context of country allocation in their guides for the reporters. In addition, as for the provision of service, both the producer and the consumer must come together and

know that a third party is involved and a transaction with the agent has to be recorded separately. Certainly, the amount of the implicit fee is unclear for either. Therefore, the compilers would have to make some overall adjustments, possibly based on reports of agents or intermediaries resident in the reporting country. In case surveys are used to collect trade in service data, a separate question or transaction code could also be considered to distinguish these triangular transactions.

43. **Finally, although the discussion in the former paragraphs focuses on services where production and consumption coincide, the suggested concept could also be applied to services where production and consumption do not occur at the same time (so called knowledge-capturing products like IPP, information, music, etc.** (see *2008 SNA*, paragraph 6.22)). Due to their dual character, these services can be traded like goods and ownership rights could be established. In consequence, for these services/goods it is possible to conclude that they fulfil the criteria of merchanting and should be recorded according to paragraph 26.21 of the *2008 SNA* or paragraph 10.44 of *BPM6* (i.e., overall, on a net basis). Such a treatment, however, would require a fundamental discussion on the delineation of goods and services in all related statistics, which would go far beyond the scope of this GN. The suggested solution above would therefore ensure a common net treatment of all services, assuming that services are always intermediated and not traded.

Case (b): Partial Outsourcing

44. **When only part of the production process is subcontracted, or, more generally, when the principal maintains control over the production process (e.g., by ensuring its quality) and keeps a relationship with the client, the gross recording of the transactions in the relevant service category remains appropriate.** Such treatment is justified given the decisive overseeing role of the principal in the transformation process. For example, the complexity of large software development projects can be such that dedicated software developers must be subcontracted to take care of particular parts of the project. The principal is responsible for bringing the different parts (its own- and third-party developments) together and takes the full responsibility of the final product sold to its customer. Under such conditions, the principal cannot be considered to act as an intermediary, and, therefore, the purchase of software development services needs to be recorded as an intermediate consumption in the production process.

Case (c): Bundled Products

45. ***Some of the companies involved in the intermediation of services not only intermediate a single service like a flight but bundle several services (e.g., flight + hotel).*** Typical examples for bundled services are package tours, where tour operators combine several services for their clients. The client buys the package and pays a single price for it. Here, the question arises if the activity of the tour operator could be seen as if it just assembles different services for its customer or does it transform the acquired services and sell them as different products to the consumer. In the latter case, it would be necessary to record both, the acquisition of the services, like transport and accommodation, and the sale of the tour, gross in the international accounts. The *European System of National and Regional Accounts in the European Union, 2010* (*ESA 2010*) (paragraph 3.61 and 3.62) takes this precise position: "The output of tour operator services is measured by the full expenditure made by travelers to the tour

operator" and "… tour operator services create a new product called a tour, which has various components of travel, accommodation and entertainment".[16]

46. **Some doubts can be raised against the view expressed in the *ESA 2010*.** First, because the services acquired by the tour operator (transportation or accommodation) cannot be considered to be consumed by it when "producing" the tour. This would be essential when considering that it transforms these services into a new product. In fact, these services are consumed (and recorded in the international accounts) by the traveler weeks or months after the tour was booked and payments were made to the tour operator. It is therefore difficult to argue that under the current rules a production activity can be derived using the bundled services as inputs that are transformed. It seems more logical to separate the transaction into (i) one component that reflects the arrangement service of the tour operator and (ii) the other components, such as transportation, which are produced by the airline and consumed by the traveler at a later stage. Just as in the *2008 SNA* (paragraph 3.68), the output of the tour operator in this sense is measured by the value of the service (fee) realized on services which are purchased for resale.

47. **This view also shared by the drafting team—to treat the arrangement service separately from the other components of the package—is already confirmed by the *2008 SNA*.** In Table 29.1 (*2008 SNA*), in the context of the Tourism Satellite Accounts, a footnote states that "The value of … consumption products, is net of the gross service charges paid to travel agencies, tour operators and other reservation services". Consumption products here means tourism characteristic products, consisting beside other of accommodation, transportation, etc. (i.e., these products are seen separately and not as part of the service charge received by the tour operator or travel agency).

48. **A similar view is expressed in *BPM6* (paragraph 3.17), which recommends unbundling two or more different transactions.** More explicitly, concerning services, paragraph 10.77 states that passenger services include fares that are a part of package tours. *BPM6 Compilation Guide* (paragraph 3.234) is even more clear by indicating that compilers must solve the problem of splitting the expenditure in the case of package tours into passenger fares and the other travel components. Both remarks clearly point into the direction that the service bundle in a package is not seen as a product in its own right.

49. **Further, the *International Recommendations for Tourism Statistics 2008* also take a clear view in this regard.** In paragraph 6.62, it is stated: "All components of a package tour, including the value of the service of the tour operator and of the travel agency, are considered as directly purchased by visitors". The *Tourism Satellite Account: Recommended Methodological Framework 2008* (*TSA*) echo this in paragraph 3.22: "In the case of package tours, three levels of services should be 'unbundled': the services themselves (for example, transport, accommodation), the services provided by the tour operator, and the margin of the travel agency (usually different from the tour operator) selling the tour".

50. **Finally, also the Central Product Classification (CPC) (version 2.1) in subclass 85540 "Tour Operator Services" can be interpreted in the way that only "arranging, assembling, and marketing**

[16] While detailed explanations are not provided in the *ESA 2010*, past discussions note that it is the fact that the tour operator takes responsibility for the bundling of services (hotel, flights, transfers, etc.) and for the interaction between the parties (make adjustments to the package as necessary in response to changing events, or refund in full if the tour does not take place), which leads to considering it a discrete product.

services" are assigned to this subclass and not transportation, accommodation, etc.[17] The latter services are understood as parts of other (service) products and are provided by entities other than those in *ISIC Rev.4* class 7912 corresponding to subclass 85540.

51. **The recommendation of the drafting team to record the arrangement service (commission of agent) separately from the services purchased for resale for bundled services is consistent with the current proposals made by GNs C.1 *Recording of Transactor-Based Components of Services (Travel, Construction, and Government Goods and Services n.i.e.) in the Balance of Payments* and C.7 *Treatment of Travel Packages, Health-Related Travel, and Taxes and Fees on Passengers' Tickets*, whose finalization is pending confirmation of decision by this GN.** A separate treatment of all service elements of a bundle fosters the supplementary reporting recommended for travel by GN C.1. It further underpins the proposal of GN C.7 to (i) unbundle package tours and (ii) record the transactions between the traveler and the providers of the single service components according to the residency principle.

SECTION II: OUTCOMES

A. Goods traded within a global manufacturing arrangement and factoryless goods producers (FGPs)

52. **The drafting team proposes that the activities related to FGP should be classified as manufacturing.** The reasoning is that the inputs related to IPP can be seen as equivalent to material inputs, which means that the production of FGPs is similar to that of companies with processing arrangements and are seen as manufacturing activities instead of wholesale activities. This would imply that the principal of a FGP arrangement will be purchasing goods (intermediate goods in the NA) from contractors and selling goods instead of distribution services. Transactions involving final goods in the global manufacturing arrangements should thus be recorded gross (output of the principal includes the input of the contractor and the value of the IPP used). This is contrary to the current net recording of FGP transactions.

53. **The output of the contractor in a global manufacturing arrangement should be recorded as a good when the contractor takes ownership of the material inputs (*where IPP and the management of the production process are provided by the principal*—FGP type arrangement), and as a service when the material inputs are owned by the principal (*with no significant input of IPP*—typical processing arrangement).**

54. **The drafting team further proposes that the definition of FGP activity not to be dependent on whether or not the contractor responsible for the transformation is an affiliated enterprise or not.** The activity of the principal engaged in a FGP type arrangement should be classified as undertaking manufacturing activity, regardless of any affiliation with the contractor responsible for transforming the goods.

[17] See also the former UN Alphabetical index for CPC Ver.2 (https://web.archive.org/web/20150911234653/http://unstats.un.org/unsd/cr/registry/regcia.asp?Cl=25&Lg=1&Co=P)

55. **Finally, the drafting team proposes that the balance of payments standard component of goods is adjusted to cover the transactions related to goods traded as part of a global manufacturing arrangement as a distinct item.** Two options where the additional component(s) related to global production arrangements are recorded as supplementary items under the goods are proposed.

B. Clarifying Negative Exports in Merchanting

56. **This GN clarifies that, for the current treatment, not a single explanation was causative.** The treatment is rather a **compromise** among experts, those that were concerned about the implications of gross reporting for the trade data, those concerned about the change of ownership principle, and those that saw a service being provided. In conclusion, the team is not proposing any changes to the current *BPM6* recording but suggests including complementary explanations in the relevant manuals.

57. **However, comments from the CATT and GZTT members suggested additional changes on different grounds.** [18] The drafting team of this GN supports these suggestions unanimously, but also agrees that they go beyond the scope of the current GN. The idea should be taken up again in the context of the drafting the updates of the current standards.

C. Merchanting of Services

58. **This GN has clarified that the current mention of merchanting of services in the context of subcontracting/outsourcing (*BPM6,* paragraph 10.160) is misleading because the latter refers to a bilateral relationship between the principal and a contractor, which is oriented towards a longer-term cooperation.** The idea of "merchanting of services", in contrast, is a trilateral relation (i.e., the intermediary, the producer, and the consumer together form a kind of triangle of service-related transactions). Further, and more important, the note came to the conclusion that "merchanting of services", from a pure conceptual view, is impossible as services cannot be traded in the same way as goods and "pure" merchanting transactions cannot involve services because no ownership rights can be established on services according the current international standards.

59. **Acknowledging that the production of a service generally coincides with its consumption, services are always directly delivered from the producer to the consumer.** Therefore, services can only be intermediated by a third person against a fee. The suggested treatment of this intermediation service is to assimilate them to those defined in *BPM6* paragraph 3.10, when "one unit (an agent) arranges for a transaction to be carried out between two other units in return for a fee from one or both

[18] Foremost, the inclusion of the so called "inverse merchanting", which occurs whenever a merchant resident in Country A purchases goods from a resident of Country B and resells these goods to another resident of Country B without the goods leaving Country B. In such cases, the goods transaction in B, which are not recorded in *International Merchandise Trade Statistics Compilers Manual* (*IMTS*) as goods, as they are not moving across the border, should be separately identified, and included in the balance of payments. More generally, it was proposed that *BPM6*, Table 10.2 (reconciliation between *IMTS* and balance of payments) should be enhanced to cover all goods transactions in the reporting country changing ownership between a resident and a non-resident without crossing the border. Furthermore, as merchanting is linked to *IMTS* recording in the country of the seller and the final buyer, and their (customs) records usually do not provide the geographical information about the country of purchase/sale (but instead the country of origin/destination), a correction of the geographical attribution is necessary to reflect the change of ownership principle. Therefore, *BPM6* Box 10.1 should explicitly mention this correction under the example of the recording of merchanting.

parties to the transaction". This treatment is suggested for cases where explicit or implicit intermediation fees should be perceived/recorded.

60. **The drafting team proposes that these fees be recorded under trade-related services, as a supplementary "of which" item in the international accounts of the partner countries.** This treatment would acknowledge that the arranger neither produces nor consumes the service, and users would be better informed of the real character of these flows compared to the current gross recording.

61. **Regarding bundling of services, this GN suggests that the services that are combined in a package, such as in the tour operators, should not be recorded as a new product in the international accounts (as recommended by the *ESA 2010*) but instead to record the package components separately in the international accounts.** By doing this, the output of a service arranger (e.g., the tour operator) is measured by the value of the service fee realized on services which are purchased for resale. This treatment is in line with other international recommendations such as the *2008 SNA*, the *TSA* and the CPC (version 2.1).

Questions for Discussion:

1) *Do the Committees agree with the recommendation to record FGP transactions gross, instead of the current net treatment?*
2) *Do the Committees agree with the recommendation of treating the output of a contractor as services only in the processing-type arrangements, and as goods in FGP-type arrangements?*
3) *Do the Committees agree with the recommendation of considering the definition of FGP activity independent of whether the contractor is an affiliated enterprise or not?*
4) *Do the Committees agree with the recommendation to expand* BPM6 *coverage of goods to show distinctly the transactions related to goods traded as part of global manufacturing arrangements as supplementary item under general merchandise (with the option to record possible trade with materials inputs in the FGP setup under merchanting as well (Option 2?))*
5) *In the Committees' opinion, is the decision tree (Annex II) a supportive tool?*
6) *Do the Committees agree with the reasoning behind the recording of negative exports in merchanting of goods? If not, please specify why.*
7) *Do the Committees agree with the recommendation that from a pure conceptual view, "merchanting of services" (as gross recording) is impossible? However, services can only be intermediated by a third person against an explicit or implicit fee.*
8) *Do the Committees agree with the recommendation to record this intermediation fees (net), under trade related services as a supplementary "of which" item?*
9) *Do the Committees agree with the recommendation that bundling of services, such as tour operators, should not be recorded as new products, but instead the components should be separately recorded?*

REFERENCED DOCUMENTS

Advisory Expert Group on National Accounts (AEG), 2013, "Global Production Factoryless Goods Producers". https://unstats.un.org/unsd/nationalaccount/aeg/2013/M8b-4.pdf

_______, 2013, Conclusions of Meeting, https://unstats.un.org/unsd/nationalaccount/aeg/2013/M8-5.PDF

_______, 2014, "Global Production Factoryless Goods Producers". https://unstats.un.org/unsd/nationalaccount/aeg/2014/M9-32.pdf

_______, 2014, Conclusions of Meeting, https://unstats.un.org/unsd/nationalaccount/aeg/2014/M9-5.PDF

International Monetary Fund, 2009, *Balance of Payments and International Investment Position Manual, sixth edition*. https://www.imf.org/external/pubs/ft/bop/2007/pdf/BPM6.pdf

Organization for Economic Cooperation and Development*, 2005, Measuring Globalisation: OECD Economic Globalisation Indicators, OECD*

United Nations Economic Commission for Europe, 2015, "Guide to Measuring Global Production" http://www.unece.org/index.php?id=42106

_______, 2011, "The Impact of Globalization on National Accounts" http://www.unece.org/fileadmin/DAM/stats/groups/wggna/Guide_on_Impact_of_globalization_on_national_accounts_FINAL21122011.pdf

United Nations, European Commission, IMF, Organisation for Economic Co-operation and Development, World Bank, 2009*, System of National Accounts (SNA) 2008* https://unstats.un.org/unsd/nationalaccount/sna2008.asp

United Nations, 2008, *International Standard Industrial Classification of all Economic Activities Rev. 4*, https://unstats.un.org/unsd/publication/seriesm/seriesm_4rev4e.pdf

_______, 2013, International Merchandise Trade Statistics: Compilers Manual, Revision 1

https://unstats.un.org/unsd/trade/publications/seriesf_87Rev1_e_cover.pdf

_______, 2019, "Summary report of the Technical Subgroup on the International Standard Industrial Classification of All Economic Activities". https://unstats.un.org/unsd/classifications/ExpertGroup/TSG-ISIC2019/Summary_Report_TSG-ISIC_2019.pdf

United Nations, Eurostat, IMF, Organisation for Economic Co-operation and Development, World Tourism Organization, World Trade Organisation, 2016, *Manual on Statistics of International Trade in Services 2010 Compiler's Guide* https://unstats.un.org/unsd/publication/seriesm/seriesm_86rev1e.pdf

Annex I. Goods Traded Within a Global Manufacturing Arrangement

This annex shows the suggested treatment of different global manufacturing arrangements in both the production account (NA) and the balance of payments, using the example of the production of an athletic shoe, taken from the *Guide to Measuring Global Production*.

Table AI.1. Breakdown of Value of the Athletic Shoe	
Material inputs	30
Material inputs, Soles	*10*
Material inputs, Other materials	*20*
Compensation of production workers	20
Compensation of managers for managing production	2
Other purchased services associated with production of the shoe	3
Return on the IPP	30
Compensation of sales workers	15
Purchased services associated with selling the shoe	4
profit on selling the shoe	6
Total value of shoe	110

Case 1: "Processing Arrangement"

- A principal in Country A sends material input (soles and other materials) to a contractor in Country B. The principal retains ownership of the material input and the rights to the IPP during the transformation process.
- The principal instructs the contractor how to assemble the shoe. The contractor transforms the material inputs into an athletic shoe and invoices the principal for contract manufacturing services.
- The principal sells the athletic shoe to a final customer in Country C.

Table AI.1.1. Production Account, Countries A and B		
Proposed ISIC - classification	Principal/Country A Manufacturer	Contractor/Country B Manufacturer
Output	**110**	**20**
Goods, Athletic shoe	110	0
Contract manufacturing	0	20
Intermediate consumption	**57**	**0**
Material inputs, Soles	10	0
Material inputs, Other materials	20	0
Contract manufacturing	20	0
Other services	7	0
Value added	**53**	**20**
Compensation of employees	17	20
Taxes less subsidies on production and imports	0	0
Gross operating surplus	36	0

Recording in Balance of Payments and International Merchandise Trade Statistics (IMTS)

- For balance of payments, the sale of the athletic shoe is recorded as export of goods for Country A and import of goods for Country C.
- The contract manufacturing is recorded as import of services for Country A and export of services for Country B.

Table AI.1.2. Balance of Payments International Transactions	Country A	Country B	Country C	Total
Exports	**110**	**20**	**0**	**130**
Goods	**110**	**0**	**0**	**110**
Goods, Athletic shoe	110	0	0	110
Services	**0**	**20**	**0**	**20**
Services, Contract manufacturing	0	20	0	20
Imports	**20**	**0**	**110**	**130**
Goods	**0**	**0**	**110**	**110**
Goods, Athletic shoe	0	0	110	110
Services	**20**	**0**	**0**	**20**
Services, Contract manufacturing	20	0	0	20

- For the IMTS, the movement and value of goods is recorded at the time of crossing the border. Material inputs are moved from Country A to Country B at the value of 30, and the final goods are moved from Country B (on behalf of principal in Country A) to Country C at the value of 50.

- The material inputs sent from Country A to Country B are not included in the balance of payments for either of the two countries since there is no change of ownership.

- The final goods sent from Country B to Country C are not included in the balance of payments exports of Country B (but in the balance of payments exports of Country A). The imports in Country C are included in balance of payments.

Table AI.1.3. ITGS and Transition to Balance of Payments	Country A	Country B	Country C	**Total**
ITGS Exports of goods	*30*	*50*	*0*	*80*
Adjustment for material inputs sent	-30	0	0	-30
Adjustment related to goods sent directly from contractor to customer	110	-50	0	60
Balance of Payments, exports of goods	**110**	**0**	**0**	**110**
ITGS imports of goods	*0*	*30*	*110*	*140*
Adjustment for material inputs received	0	-30	0	-30
Balance of Payments, imports of goods	**0**	**0**	**110**	**110**

Case 2: "FGP Arrangement"

- A principal in Country A retains ownership of the rights to the IPP during the transformation process. The contractor supplies all material inputs, which it purchases in Country B.

- The principal instructs the contractor how to assemble the shoe. The contractor transforms the material inputs into an athletic shoe and invoices the principal for contract manufacturing (including the expenses for material inputs).

- The principal sells the athletic shoe to a final customer in Country C.

Table AI.2.1. Production Account, Countries A and B		
Proposed ISIC- classification	**<u>Principal</u>/Country A** **Manufacturer**	**<u>Contractor</u>/Country B** **Manufacturer**
Output	**110**	**50**
Goods, Athletic shoe	110	0
Contract manfuacturing	0	50
Intermediate consumption	**57**	**30**
Material inputs, Soles	0	10
Material inputs, Other materials	0	20
Contract manufacturing	50	0
Other services	7	0
Value added	**53**	**20**
Compensation of employees	17	20
Taxes less subsidies on production and imports	0	0
Gross operating surplus	36	0

Recording in Balance of Payments and International Trade in Goods Statistics (IMTS)

- For balance of payments, the sale of the athletic shoe is recorded as export of goods for Country A and import of goods for Country C.
- The purchase of contract manufacturing is recorded as import of goods for Country A and export of goods for Country B.

Table AI.2.2. Balance of Payments International Transactions	Country A	Country B	Country C	**Total**
Exports	**110**	**50**	**0**	**160**
Goods	**110**	**50**	**0**	**160**
Goods, Athletic shoe	110	0	0	110
Goods, Contract manufacturing	0	50	0	50
Imports	**50**	**0**	**110**	**160**
Goods	**50**	**0**	**110**	**160**
Goods, Athletic shoe	0	0	110	110
Goods, Contract manufacturing	50	0	0	50

- For IMTS the movement and value of goods is recorded at the time of border passage. The final goods are moved from Country B at the value of 50 and with the value of 110 to Country C.
- The sale of goods to Country C have to be added to the export of Country A.
- The purchase of goods from Country B have to be added to the import of Country A.

Table AI.2.3. ITGS and transition to Balance of Payments	Country A	Country B	Country C	**Total**
ITGS Exports of goods	*0*	*50*	*0*	*50*
Adjustment for goods sold after manufacturing abroad	110	0	0	60
Balance of Payments, exports of goods	**110**	**50**	**0**	**160**
ITGS imports of goods	*0*	*0*	*110*	*110*
Adjustment for goods purchased after manufacturing abroad	*50*	*0*	*0*	
Balance of Payments, imports of goods	**50**	**0**	**110**	**160**

Case 3: "FGP Arrangement Where the Principal Supplies Materials"

- The principal in Country A purchase material inputs (Other materials) in Country C and sells this, along with material inputs, soles (acquired in Country A) to the contractor in Country B. The principal retains ownership of the rights to the IPP during the transformation process (but not ownership of the material inputs).
- The principal instructs the contractor how to assemble the shoe. The contractor transforms the material inputs into an athletic shoe and invoice the principal for contract manufacturing (including expenses for material inputs).
- The principal sells the athletic shoe to a final customer in Country C.

Table AI.3.1. Production Account, Countries A and B		
	Principal/Country A	Contractor/Country B
Proposed ISIC- classification	**Manufacturer**	**Manufacturer**
Output	**110**	**50**
Goods, Athletic shoe	110	0
Net gain from trade in material inputs*	0	0
Contract manufacturing	0	50
Intermediate consumption	**57**	**30**
Material inputs, Soles	0	10
Material inputs, Other materials	0	20
Contract manufacturing	50	0
Other services	7	0
Value added	**53**	**20**
Compensation of employees	17	20
Taxes less subsidies on production and imports	0	0
Gross operating surplus	36	0

* This item is calculated as the revenue from trade in material inputs minus the purchases of material inputs.

Recording in Balance of Payments and International Trade in Goods Statistics (IMTS)

- For balance of payments, the sale of the athletic shoe is recorded as export of goods for Country A and import of goods for Country C.
- The trade with material inputs bought abroad (other materials) will be treated as merchanting and the material input coming the economy of the principal (soles) will be recorded as exports. The material goods are recorded as import for Country B. The purchase of material inputs (Other materials) from Country C is recorded as export of goods from Country C.
- The purchase of contract manufacturing is recorded as import of goods for Country A and export of goods for Country B.

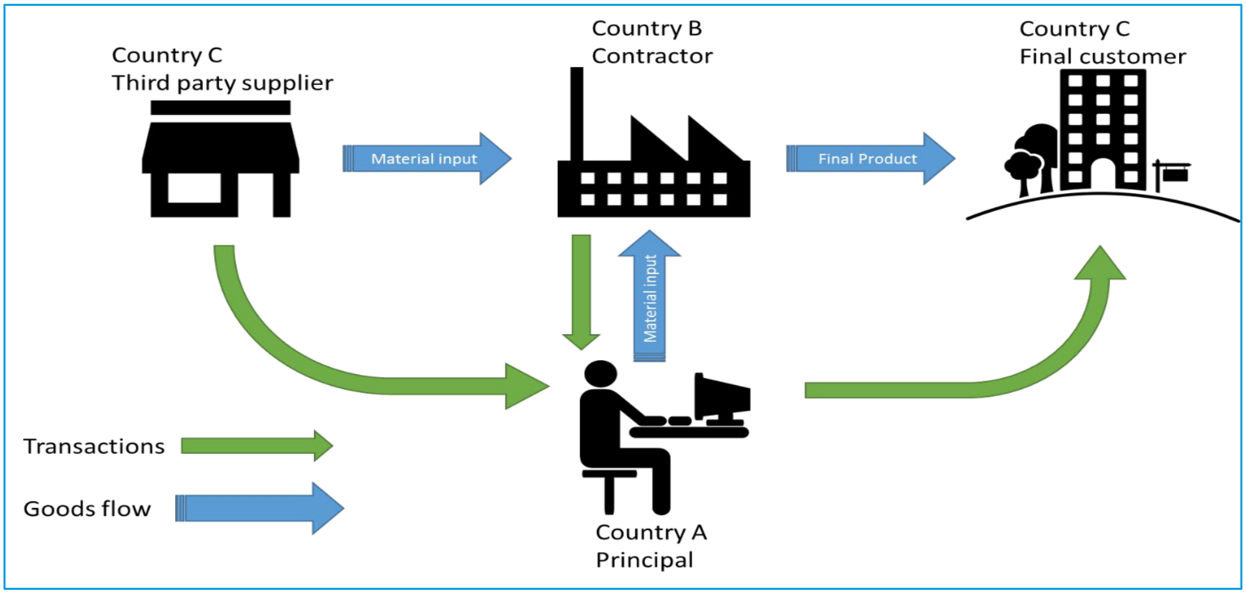
Table AI.3.2. Balance of Payments International Transactions	Country A	Country B	Country C	**Total**
Exports	**120**	**50**	**20**	**190**
Goods	**120**	**50**	**20**	**190**
Goods, Athletic shoe	110	0	0	110
Goods, Net merchanting	0	0	0	0
Goods, sales of Other materials	20	0	0	20
Goods, cost of Other materials	-20	0	0	-20
Goods, Material inputs (Soles)	10	0	0	10
Goods, Material inputs (Other materials)	0	0	20	20
Goods, Contract manufacturing	0	50	0	50
Imports	**50**	**30**	**110**	**190**
Goods	**50**	**30**	**110**	**190**
Goods, Athletic shoe	0	0	110	110
Goods, Material inputs (Soles)	0	10	0	10
Goods, Material inputs (Other materials)	0	20	0	20
Goods, Contract manufacturing	50	0	0	50

- For IMTS the movement and value of goods is recorded at the time of border passage. The final goods are moved from Country B at the value of 50 and with the value of 110 to Country C. The material inputs (soles) are moved from Country A to Country B with the value of 10 and the material inputs (other materials) are moved from Country C to Country B with the value of 20.
- The sale of goods after manufacturing have to be added to the export of Country A.
- The purchase of goods after manufacturing have to be added to the import of Country A.
- The net export on material input purchased abroad for contract manufacturing abroad is added to the export of Country A (zero in this case).

Table AI.3.3. ITGS and transition to Balance of Payments	Country A	Country B	Country C	**Total**
ITGS Exports goods	*10*	*50*	*20*	*80*
Adjustment for net export of material goods purchased abroad for contract manufacturing abroad	0	0	0	0
Adjustment for goods sold after contract manufacturing abroad	110	0	0	110
Balance of Payments, exports of goods	**120**	**50**	**20**	**190**
ITGS imports goods	*0*	*30*	*110*	*140*
Adjustment for goods purchased after contract manufacturing abroad	50	0	0	*50*
Balance of Payments, imports of goods	**50**	**30**	**110**	**190**

Figure AI.1 and Table AI.4 below show the flows of goods and transactions typical for a processing arrangement and their recording in the balance of payments. Figure AI.2 and Table AI.5 show the same for a FGP type arrangement. Another specific aspect of the FGP type arrangement relates to the goods transactions for the delivery of the material inputs. Case 3 above shows an example where the principal is acquiring all the material inputs, but these are sold to the contractor before their transformation. One could argue that transactions, such as those undertaken before the transformation, can be treated as distinct from the global production arrangement, and should thus be recorded as regular merchandise trade (or merchanting and merchandise trade as in Case 3). Nonetheless, the drafting team believes that such transactions are part of the FGP type arrangement and could be recorded separately as distinct item(s), in order to provide the needed information for compilers and users. This would also help distinguishing the global manufacturing arrangements and support policy analyses.

Figure AI.1. The Flows of Goods and Transactions in a Processing Type Arrangement

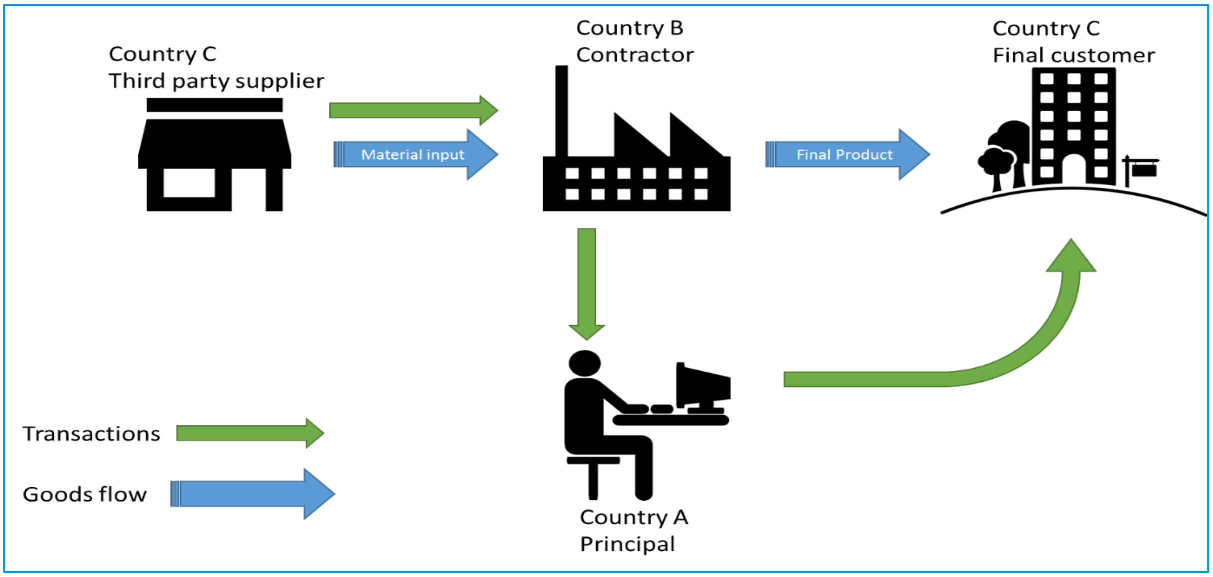


Source: Created by the drafting team using Internet clipart

Table AI.4. Balance of Payments Transactions in a Processing Arrangement

Table 2. Balance of Payments transactions, processing type arrangement	Item	Import	Export
Principal			
Sale of final goods (full value of good, including embedded value of IPP)	General merchandise on a balance of payments basis; of which Goods traded within a global manufacturing arrangement		X
Purchase of material inputs	General merchandise on a balance of payments basis; of which Goods traded within a global manufacturing arrangement	X	
Purchase of manufacturing services	Services	X	
Adjustment for goods crossing the border (ITGS)			X
Contractor			
Sale of manufacturing services	Services		X
Adjustment for goods crossing the border (ITGS)		X	X
Third party supplier			
Sale of material inputs	General merchandise on a balance of payments basis		X
Final customer			
Purchase of final goods	General merchandise on a balance of payments basis	X	

Figure AI.2. The Flows of Goods and Transactions in a FGP Type Arrangement



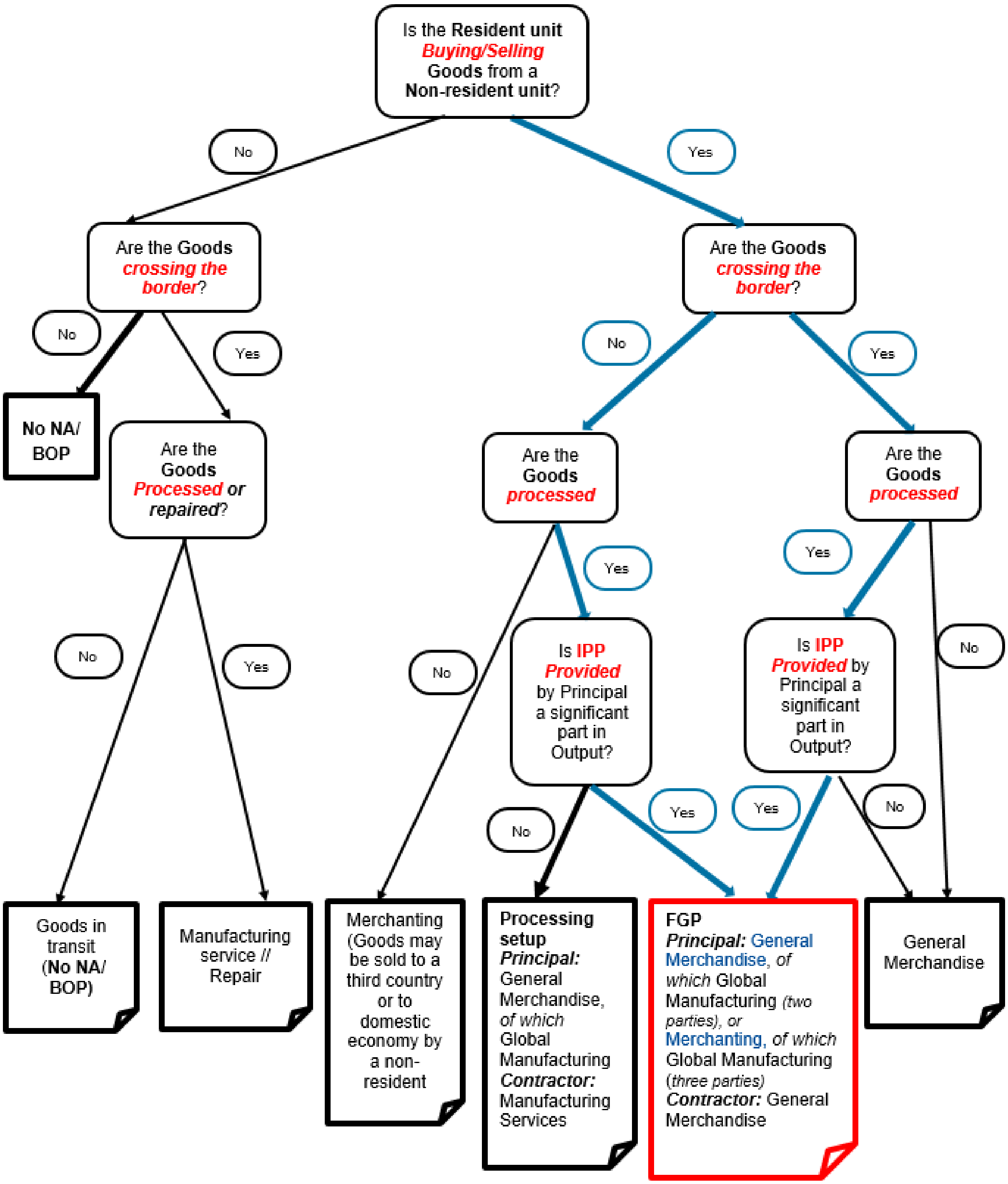
Source: Created by the drafting team using Internet clipart

Table AI.5. Balance of Payments Transactions in a FGP Type Arrangement

Table 3. Balance of Payments transactions, FGP Type Arrangement	Item	Import	Export
Principal			
Sale of final goods (full value of final good including embedded value of IPP)	General merchandise on a balance of payments basis; of which Goods traded within a global manufacturing arrangement		X
Purchase of processed goods from contract manufacturer (value excludes the embedded IPP)	General merchandise on a balance of payments basis; of which Goods traded within a global manufacturing arrangement	X	
Contractor			
Sale of processed goods (value excludes the embedded IPP)	General merchandise on a balance of payments basis		X
Purchase of material inputs	General merchandise on a balance of payments basis	X	
Third party supplier of material inputs			
Sale of material inputs	General merchandise on a balance of payments basis		X
Final Customer			
Purchase of final goods	General merchandise on a balance of payments basis	X	

Annex II. Decision Tree

In the chart below, the FGP-related transactions are identified by following the (blue) thick arrows. The defining characteristics for FGPs are (i) all cross-border transactions in both input materials and processed/final goods involve change of ownership; (ii) a processing is always taking place; and (iii) IPP of significant value in the output is provided by the principal.



Source: Adapted from the Eurostat's Manual on goods sent abroad for processing by the drafting team

Annex III. Alternative Proposed Presentation to GN C.2 *Goods, Services, and Investment Income Accounts by Enterprise Characteristics* Identifying Trade within a Global Production Chain

	Encouraged	Encouraged					
	Total	By trading partner		By product / service		By industry	
		Top 5 partners	Rest of the world	Top 5 products	The other products	Top 5 industries	The other industries
(S)TEC Balance of Payments Statistics							
1.A Export of goods and services							
Of which Trade within a global manufacturing arrangement							
By enterprise's ownership							
Domestically controlled							
MNE							
Other							
Controlled from abroad							
Unknown							
Export of goods and services, total							
1.A.a Goods, BOP basis							
By enterprise's ownership							
Domestically controlled							
MNE							
Other							
Controlled from abroad							
Unknown							
By enterprise's size							
SME							
Independent							
Part of a group							
Large enterprises							
Unknown							
1.A.b Services, BOP basis							
By enterprise's ownership							
Domestically controlled							
MNE							
Other							
Controlled from abroad							
Unknown							

By enterprise's size				
SME				
Independent				
Part of a group				
Large enterprises				
Unknown				
1.B.2 Receipts of investment income				
By enterprise's ownership				
Domestically controlled				
MNE				
Of which 1.B.2.1 Direct investment				
Other				
Controlled from abroad				
Of which 1.B.2.1 Direct investment				
Unknown				
By enterprise's size				
SME				
Independent				
Part of a group				
Large enterprises				
Unknown				

	Encouraged	Encouraged					
	Total	By trading partner		By product / service		By industry	
		Top 5 partners	Rest of the world	Top 5 products	The other products	Top 5 industries	The other industries
(S)TEC Balance of Payments Statistics							
1.A Import of goods and services							
Of which Trade within a global manufacturing arrangment							
By enterprise's ownership							
Domestically controlled							
MNE							
Other							
Controlled from abroad							
Unknown							
Import of goods and services, total							
1.A.a Goods, BOP basis							
By enterprise's ownership							
Domestically controlled							
MNE							
Other							
Controlled from abroad							
Unknown							
By enterprise's size							
SME							
Independent							
Part of a group							
Large enterprises							
Unknown							
1.A.b Services, BOP basis							
By enterprise's ownership							
Domestically controlled							
MNE							
Other							
Controlled from abroad							
Unknown							
By enterprise's size							
SME							
Independent							

Part of a group				
Large enterprises				
Unknown				
1.B.2 Expenditures of investment income				
By enterprise's ownership				
Domestically controlled				
MNE				
Of which 1.B.2.1 Direct investment				
Other				
Controlled from abroad				
Of which 1.B.2.1 Direct investment				
Unknown				
By enterprise's size				
SME				
Independent				
Part of a group				
Large enterprises				
Unknown				

Annex IV. Example of Recording of the Intermediation of Services in the Revised *EBOPS*

Consistent with the proposed breakdown of services made by the GN C.6, the following recording the intermediation of services in the *EBOPS* is suggested in the table below:

Table AIV.1. Example of Recording of the Intermediation of Services in the Revised *EBOPS*

<table>
<tr><th>13.1</th><th>SJ34</th><th>Trade-related services</th><th>Comments</th></tr>
<tr><td>13.1.a</td><td></td><td>Trade-related services
of which: transport services</td><td rowspan="3">Covers fees of DIPs intermediating services (in the relevant category); or
the difference between selling and buying values, in case of implicit fees</td></tr>
<tr><td>13.1.b</td><td></td><td>Trade-related services
of which: accommodation services</td></tr>
<tr><td>13.1.c</td><td></td><td>Trade-related services; of which: services n.i.e.</td></tr>
<tr><td>13.1.d</td><td></td><td>Trade-related services
of which: sale of goods</td><td>Covers traditional trade-related services (fees, commissions) + fees of DIPs intermediating goods</td></tr>
</table>