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## Issue Note: A Holistic Assessment of the Treatment of Concessional Lending in Macroeconomic Statistics



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Prepared jointly by the SNA and BPM Update Editorial Teams  
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*This Issues Note discusses a holistic treatment of concessional lending in macroeconomic statistics. It was motivated by the discussion of GN F.15 “Debt Concessional”, which addresses low interest loans provided in a non-commercial context, at the March 2022 joint BOPCOM/AEG meeting. The majority view at that meeting was to continue to record concessional loans at their face/nominal value at inception with no further imputation and continuing to record the transfer element as a memorandum item/supplementary information (option A/A1). However, there were concerns that this would create an inconsistency with the recording of other concessional lending in the 2008 SNA and BPM6. This Issues Note addresses this concern. In summary, this Issues Note recommends to never record a transfer element in the central framework of the national accounts and external sector statistics, except in a very limited number of clearly defined cases. This is essentially in line with option A/A1 in GN F.15.*

### The Issue

- 1 On March 7, 2022, the Guidance Note (GN) F.15 on “Debt Concessional”, which has been prepared by the Financial and Payment Systems Task Team (FITT), was discussed at the joint meeting of the AEG and BOPCOM, for endorsement, taking into account the results from the global consultation.
- 2 The GN considers, amongst others, the recording of concessional loans provided in a non-market context. The following alternative options were presented:
  - Option A: No change in the updated BPM and SNA. This implies continuing to record concessional loans at their face/nominal value at inception with no further imputation and continuing to record the transfer element as a memorandum item/supplementary information;
    - Sub-option A1: No change in the updated BPM and SNA in the accounts but provide more detailed information (than currently requested) on the transfer element, notably the fair value of the loan and the entailed accrued interest in memorandum/supplementary information.
  - Option B: Record concessional loans at their face/nominal value at inception, but recognize the transfer element in the core accounts, spread over time, by increasing the stream of interest earned (D.41) on the loan using a suitable non-concessional rate together with a matching transfer expense (deficit neutral in every accounting period);

- Option C: Partition concessional loans at inception between a “genuine” loan element (F.4) and an explicit “transfer element”, followed later on by imputed interest receivable (D.41, of the same cumulated size over the lifetime of the loan) that capitalizes on the new nominal value/principal of the loan over time, to reach the face value before maturity (deficit neutral across the life of the loan).

3 The GN recommended Option C, which was also supported by the majority of the FITT members. Options A/A1 were rejected mainly because of the view that macroeconomic statistics must explicitly capture all transfers extended by government within the core accounts, thereby increasing transparency and accuracy of the accounts. Although both Option B and C would recognize the transfer element in the core accounts, members preferred Option C to Option B, because it would recognize the transfer element at the correct period (i.e., at inception) and provide the present value of the loans consistent with international accounting standards. Two members who did not support Option C, favoured Option A1 arguing that it ensures the compilers present more detailed information, enabling interested users to undertake a better assessment of the implications of the transfer element on the core accounts. Two other members preferred either Option B or C.

4 Looking at the outcomes of the global consultation, 47% supported Option C, 30% Option A/A1, and 15% of the respondents were undecided. Those favouring Option C considered it to be, conceptually, a better representation of economic reality. According to some of these respondents, loans provided under favourable conditions imply a “cost” for lenders and an economic benefit for borrowers, which can be regarded as a transfer at the time the transaction is made. Option C was also seen as the best approach to represent a more meaningful debtor/creditor financial positions, as it takes into account the time value of money. Respondents favouring Option C also commented that the use of present value for these loans would better align the macroeconomic statistics with International Public Sector Accounting Standards (IPSAS). In contrast, the supporters of Option A argued that the international statistical standards prescribe nominal valuation for loans, which should hold for concessional loans as well. These respondents also favoured Option A/A1 as there is not the risk of global asymmetries embedded in the complexities perceived in Option C. Undecided respondents noted practical difficulties in determining the transfer/grant-element and reporting burden as major issues regarding Option C, but some of them recognized its conceptual soundness. They also commented that different approaches may be desirable given the diversity of concessional loan agreements.

5 At the joint meeting of the AEG and BOPCOM, no consensus was reached on Option C, as recommended in the GN. There was a call for treating the valuation of all loans and the recording of all concessional loans alike consistently in both manuals. The treatment of other loans with favourable terms such as those granted by employers (as compensation of employees) or central bank loans (treated as subsidies) should also be maintained. All in all, the following was concluded: *“In spite of many recognizing that Option C was more sound on conceptual grounds for the statistical treatment of concessional lending, on*

*account of the practical challenges in its implementation, most members indicated their preference for Option A/A1 from a practical point of view. They argued that Option A (or A1) is consistent with the international statistical standards on valuation of loans (at nominal value), including concessional loans, and viewed it as a better approach in reducing global asymmetries. Moreover, Option A/A1 is considered appropriate from a compilation perspective, as calculating the loan value and an imputed transfer element at inception (Option C) could be difficult. In addition, some members noted that Option C would require clarifying how to calculate financial intermediation services indirectly measured (FISIM) in case of imputed concessionary interest. Option B received minority support”.*

6 Although the AEG and the Committee reached a majority decision supporting Option A/A1, after subsequent discussions between the two editorial teams, it was agreed—in line with the resolution mechanism between SNA and BPM to deal with inconsistencies—that the editorial teams would prepare an issues note taking a holistic view on the treatment of concessional loans (including employer-sponsored loans, student loans, inter-company loans, etc.) and aiming to ensure overall consistency in related recommendations within both Manuals, thereby also looking at possible inconsistencies in the treatment of the concessional element, by either recording the concessional element in full at the time of inception, or by recording a stream of (current) transfers over the relevant period of the concessional loan, in both the central framework and supplementary items.

### Concessional Lending in Current International Standards

7 Looking at the 2008 SNA, it is important to note upfront that the general principle for valuing transactions is the market price. Exchange values are considered the best approximation of such market prices, however with a couple of exceptions, one of them being concessional pricing (paragraph 3.134). Additional guidance for concessional loans is then provided for three cases: (i) loans provided by employers to employees at reduced, or even zero, rates of interest (paragraph 7.54); (ii) loans to central banks in the form of reserve deposits below market rates (paragraph 7.124), loans to central banks for the purpose of currency support at above market rates (paragraph 7.125), and loans by central banks to priority industries at below market rates (paragraph 7.126); (iii) loans issued by government on concessional terms (paragraph 22.123 – 22.125), the latter with a reference to the *Government Finance Statistics Manual 2011 (GFSM 2011)*, the *Eurostat Manual on Government Debt and Deficit (MGDD)*, the *External Debt Statistics Guide 2013*, and the sixth edition of the *Balance of Payment and International Investment Positions Manual (BPM6)*.

8 Regarding the treatment of concessional loans, the 2008 SNA notes that, from a conceptual point of view, the difference between the market interest rate and the

concessional rate of interest represents a transfer element.<sup>1</sup> However, while in the first two cases explicit guidance is provided on the recording of such a transfer element, by increasing the interest to the level of the market interest rate, with a concomitant current transaction (compensation of employees in the first case, and subsidies in the second case), no further guidance is provided in the third case. In respect of the latter, it is noted that the difference between the actual interest and the market equivalent interest could be seen as providing a current transfer but is concluded that “... *the means of incorporating the impact within the SNA and international accounts have not been fully developed, although various alternatives have been advanced. Accordingly, until the appropriate treatment of concessional debt is agreed, information on concessional debt should be provided in supplementary tables*” (paragraph 22.124 of the 2008 SNA, and also paragraph 12.51 of BPM6). Importantly, in all three cases, the (implicit) recommendation is to record the transfer element as a current transfer (which would be the more obvious choice in the case of applying option B in the above), and not as a capital transfer at inception (which would be the more obvious choice in the case of applying Option C in the above).<sup>2</sup>

9 On the other hand however, paragraph A2.68 of BPM6, states the following, when discussing the recording of debt reorganization through the Paris Club and the related possibility of providing supplementary items on concessional loans: “*The recording should be made as a one-off transaction at the point of loan origination equal to the difference between the nominal value of the debt and its present value (using a relevant market discount rate such as the CIRR). For a new loan, this approach would require information on the market interest rate at inception and the contractual interest rate—with the market interest rate as the discount rate and the difference the value of the transfer. This approach has the advantage of considering all the possible sources of transfers in debt concessionality—maturity period, grace period, frequency of payments, interest rate, and other applicable costs—and is consistent with nominal valuation of loans. ...*” The latter part of the text has been bolded by the authors, because it seems to run against the valuation of loans at nominal value, as defined in paragraph 3.88 of BPM6, which is consistent with the above definition of the 2008 SNA, although slightly more text is included in BPM6 to explain the relevant guidance.

10 The issue of debt concessionality was also included in the Research Agenda of the 2008 SNA, as follows: “*Further work is required to clarify whether concessional loans involve a subsidy on any service charge associated with interest payments or a transfer representing the difference between the market rate of interest and the agreed rate. If the latter, the next problem is whether the transfer should be paid period by period on an ongoing basis as a*

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<sup>1</sup> The guidance also notes that “... *the degree of concessionality can be enhanced with grace periods, frequencies of payments and a maturity period favourable to the debtor*” (paragraph 22.123)”. While this issue can be quite important for a full accounting of the transfer element, for reasons of simplicity, it is not explicitly referred to in the remainder of this note.

<sup>2</sup> Please note that GN F.15 does not prescribe the recording of neither a current transfer nor a capital transfer in applying Options B and C; see Annex VI of the GN.

*current transfer or as a one-off capital transfer at the time the loan is issued.*" (Paragraph A4.44). As such, in the Research Agenda, the recording of the transfer element, as a current transfer or as a capital transfer at inception, is left open.

11 Another issue in relation to the recording of concessional loans, already alluded to in the above, concerns its consistency with the method for valuing non-tradable loans. The SNA, and also the BPM, recommend a valuation of such loans at nominal value, which is defined, in paragraph 3.157, as *"... the amount the debtor owes to the creditor, which comprises the outstanding principal including any accrued interest"*. As also argued during discussion of the GN on "Debt concessionality", the recording of capital transfer at inception, with a concomitant revaluation of the loan, is considered to run against the recommended method for valuing (non-tradable) loans.

### The Way Forward

12 Considering the above circumstances from the point of view of consistency within and across statistical manuals, two issues need to be resolved. The first issue concerns when there should be an accounting for concessional lending, i.e., whether or not it is possible to arrive at a more exhaustive recording of concessional lending, thereby taking a holistic view regarding the possible extent of such lending. The second issue concerns the consistency in the recording of concessional lending (where it is agreed that concessional lending should be accounted for).

13 Before starting a discussion on the extent to which concessional lending should be recognised and accounted for, it is useful to list the most relevant cases, as follows:

- Concessional lending by governments: This may concern lending to households (e.g., student loans, loans to support households at the lower of the income and wealth distribution, loans to promote certain policies such as the transition to a more sustainable economy) as well as lending to corporations for similar purposes.
- Concessional lending between different governments or different government units.
- Lending by central banks, as explicitly included in the guidance of the *2008 SNA* (see above).
- Concessional lending by international organisations.
- Lending at favourable terms by households to family and friends.
- Concessional lending between affiliates of the same (multinational) corporation. In the case of multinational corporations, this may be motivated by reasons similar to the use transfer pricing more generally.
- Concessional lending by employers to employees, which seems to be most prominent in the case of financial corporations.

14 Considering the full extent of concessional lending, three options could be considered for recognising and accounting for concessional lending:

- Option 1 (equivalent to Option A in the GN): Never record a transfer element for concessional lending and accept the actual interest transactions paid/received.
  - Option 1A (equivalent to Option A1 in the GN): Provide information on the impact of concessional lending as supplementary items.
- Option 2: Apply an exhaustive and fully consistent recording of all forms of concessional lending, by either recording a continuous stream of current transfers to account for the difference between the actual loan interest rate and the market-equivalent interest rate at loan issuance (equivalent to Option B in the GN), or by recording the whole concessional element at the time of inception (Option C in the GN).
- Option 3: Apply Option 1 but apply option 2 to a limited number of exceptions (see below) to the general rule of not accounting for concessional lending.
  - Option 3A: Provide additional information on the impact of concessional lending as supplementary items.

Please note that the way of recording the concessional element also may become relevant in the case of Option 1A and Option 3(A).

15 **From a conceptual perspective, Option 2 may look conceptually appealing.**

**However, from a feasibility perspective, the application of this option looks far from being realistic.** For governments and international organisations, it may be possible to gather information on the extent of concessional lending from more or less centralised data sources. However, in the case of households and corporations, the collection of relevant information on a comprehensive basis would be extremely challenging. One could argue that in the latter cases, missing such source data is not that problematic, because it first and foremost concerns intra-sector transactions, thus not affecting the consolidated overview of the relevant sector (i.e., after netting out the intra-sector transactions). However, this does not hold for cross-border transactions for multinational enterprises, or for concessional lending by corporations to households, such as in the case of concessional lending to employees. It is also not valid in the case of breaking down households in various groups, in line with the objectives of compiling more information on the distribution of income, consumption, saving and wealth of households.

16 **Option 1 looks less attractive, because there may be good reasons for recognising and accounting a concessional element in some instances. Here, the most obvious example is concessional lending by employers to employees, to properly account for the costs of labour input into the production of goods and services. That would plea for recommending Option 3.** In doing so, it is proposed to not consider the borrowing by central banks at interest rates lower (higher) than market-equivalent interest rates, such as in the case of reserve deposits or for currency support, or lending by central banks at below market rates for priority industries as an exception to the rule of not accounting for concessional lending, mainly because of a lack of argumentation in favour of such an exception. Moreover, the relevant guidance for central banks is not included in some other

international standards and manuals, such as the *European System of Accounts 2010 (ESA 2010)* and the *Monetary and Financial Statistics Manual 2016 (MFSM 2016)*. It should be clear, however, that, although it would lead to a better alignment across macroeconomic standards, it would entail a change to the current SNA treatment (as outlined in paragraphs 7.124–7.126) and *GFSM 2011* (Box 6.2).

**17 In applying Option 3, it is recommended to include the provision of the transfer element in concessional lending as supplementary items, i.e., Option 3A. Taking into account the potential for collecting applicable source data, it is recommended to include, in line with the recommendations made in GN F.15, supplementary items for the most relevant cases, i.e., for concessional lending in a non-market context, thus restricting the supplementary items to concessional lending by governments, central banks, and international organisations.**

18 In regard to the second issue, i.e., how to record concessional lending, the choice basically comes down to (i) the recording of a continuous stream of current transfers versus (ii) a one-off capital transfer at inception. The first option is more consistent with the valuation of loans at nominal value (which is different from what paragraph A2.68 of *BPM6* seems to suggest). The second option—the recording of a capital transfer at inception and a concomitant revaluation of the loans—may better represent economic reality, but this can also be said of the valuation of (non-tradable) loans more generally. Although the nominal value of two (non-concessional) loans may be the same, for the creditor the value of a loan with an interest of say 4% represents a higher value than a loan with an equivalent nominal value with an interest rate of say 3%.

19 Another point of consideration in the choice between the options is the applicability for, and impact on, the recording of different types of concessional loans. The second option of recording a capital transfer at inception may be problematic when applying it, for example, to concessional lending by employers to employees, where the transfer element is recorded as part of compensation of employees. Having large one-off payments becoming part of current transactions looks counterintuitive. Moreover, recording the concessional element as a current transfer would have the advantage of not affecting disposable income and net lending/net borrowing of the accounts in the SNA; and b) current account and net lending/borrowing of external accounts.

**20 All in all, it is concluded that option (i), i.e., recording a continuous stream of current transfers, not only in the central framework, but also in the case of supplementary items, provides the best opportunities for a consistent accounting for concessional lending.**

**21** Against this background, the two editorial teams recommend the following:

- To never record a transfer element for concessional lending in the central framework of national accounts and external sector statistics, with the exception of a very limited number of clearly defined cases. This is basically in line with Option A/A1
- The above exceptions are limited to concessional loans provided by employers to employees, mainly because of a more accurate accounting for compensation of employees. In this respect, it is also recommended to remove the exception made for loans/deposits by central banks, as currently included in the *2008 SNA* and *GFSM 2011*.
- Supplementary items for the transfer element included in concessional lending are compiled for concessional loans provided in a non-market context, i.e., those provided by governments, central banks and international organizations.<sup>3</sup>
- In order to arrive at a consistent treatment of concessional loans,<sup>4</sup> the transfer element will always be recorded as a continuous stream of current transfers over the relevant period of the concessional loans (Option B in GN F.15).

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<sup>3</sup> In line with the guidance included in the *External Debt Statistics Guide 2013* (see paragraphs 6.22 and 6.23), namely that the concessional lending provided by the IMF is defined as concessional if it includes a grant element of at least 35 percent.

<sup>4</sup> Referring to concessional lending to employees and, in supplementary tables, to other concessional lending.