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GFS Research Agenda

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I. STYLIZED FACTS:

1. The *System of National Accounts 2008* (*2008 SNA*) is the underlying manual for macroeconomic statistics. Updates of other main statistical manuals, including the *Government Finance Statistics Manual 2014* (*GFSM 2014*), have been aligned, as far as possible, with the comprehensive guidance in the *2008 SNA*.

2. However, the *2008 SNA* recognizes that a number of issues were not resolved at the time of the update. Consequently Annex 4 of the *2008 SNA* presents, as a research agenda, a list of issues that have emerged in the course of the update and where more extensive consideration is needed.

3. A number of the issues included in the *2008 SNA* research agenda have direct relevance to the general government or public sectors, and therefore research and decisions made in these areas are of interest to compilers and users of the government finance statistics (GFS), and require input from the GFS community.

4. Furthermore, during the preparation of the *GFSM 2014*, additional issues have emerged that may need to be clarified.

5. This paper highlights the key issues where further discussion and additional guidance may be required, and presents the starting point for a GFS specific research agenda. The paper also proposes a procedure for updating guidance between major revisions, based on a similar procedure used by the balance of payments compilers.

II. BACKGROUND INFORMATION:

A. GFS Relevant Issues identified in the *2008 SNA Research Agenda*

6. The *2008 SNA* research agenda includes 34 topics of which eight have a potentially significant impact on key GFS aggregates depending upon decisions reached.[1]

7. The GFS-relevant topics are indicated below.

Issues Arising from a Financial Crisis

8. The global financial crisis and its aftermath have thrown up the following issues that could be addressed in the next round of manual updates, or require further clarification. These issues arise from actions taken by governments and monetary authorities to address the crisis, which have, in some cases resulted in the blurring of fiscal and monetary policy in some countries. Short-term solutions have been adopted on a regional basis,[2] and *GFSM 2014* includes some guidelines on, for example, the treatment of restructuring agencies and financial protection schemes (see paragraphs 2.129 and 2.132). However, the practical application of these guidance is imperfect or incomplete in the following areas:

- Quantitative Easing—quantitative easing is becoming a routine, rather than exceptional tool for central banks. The impact of central banks acquiring large stocks of government debt is resulting in clear increases in flows between general government and the central bank above and below the line, as well as changes in the dynamics of public sector debt. In some cases, questions were even raised about whether government debt securities, used under these circumstances should be included in general government debt;

- Government guarantees for central bank monetary policy activities—blanket support, in the form of a guarantee from general government to the central bank, raises questions of risks and rewards and on whose balance sheet certain operations should be recorded;

- Stock lending/exchange of assets— the line between stock lending as a standard part of open market monetary operations and quasi-fiscal operations is becoming blurred. Where central banks borrow short term government securities to carry out these operations, issues arise as to whether these borrowed securities should be considered as part of general government debt;

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[1] The *2008 SNA* lists its research issues under four broad headings: basic accounting rules, the concept of income, issue concerning financial instruments, and issues involving nonfinancial assets.

[2] For example, the 2009 Eurostat decision on *The statistical recording of public interventions to support financial institutions and financial markets during the financial crisis*.

- In some countries, the independence of the central bank and the clear line between monetary and fiscal policy is blurred, in other countries, central banks have never been independent and have often acted in a quasi-fiscal way. It requires a further debate on whether a central government aggregate, including the fiscal operations of the central bank should become the norm rather than a supplementary set of data.

- Negative interest rates – the use of low or even negative interest rates, coupled with mandatory reserve requirements, raises real questions about how the resulting payments by financial intermediaries to the central bank should be treated as they will affect the public sector accounts.

Recognition of Social Security Entitlements as Liabilities

9. In the GFSM 2014 a distinction is drawn between social security scheme (7.194) entitlements for which no liability is recognized (see *GFSM 2014*, paragraph 7.194), employment-related pension entitlements for which liabilities are always recognized (see *GFSM 2014*) regardless of whether there are actually assets set aside to meet the entitlements, and employment-related nonpension benefit entitlements for which liabilities are recognized only when reserves to cover these entitlements actually exist (see *GFSM 2014* paragraph 7.195). This approach differs from the discussion in the *2008 SNA* in which a compromise was reached that pension entitlements of unfunded pension schemes sponsored by government under social security schemes would be recorded in a supplementary table (see *2008 SNA*, paragraph 17.193). Provisional criteria for determining whether the entitlements are shown in the main accounts or only in the supplementary table are described in the paragraph 17.194 of the *2008 SNA*.

10. The *2008 SNA* research agenda notes that work continues to refine these criteria and to find agreed methods to determine the value of these liabilities. If nonpension entitlements under social security schemes were also recognized as assets and liabilities an issue would arise for GFS compilers as to their sector classification within general government. The question would be whether these entities are involved in market activities in which case they would become more like public sector insurance schemes. In this regard, it should also be noted that the outcome of work by the International Public Sector Accounting Standards Board (IPSASB) on their Conceptual Framework (defining the concepts assets and liabilities) and on a standard on social benefits may further inform this debate.

Provisions

11. Unlike in business accounting, the statistical basis of recording does not record provisions, instead limiting the balance sheet to actual (outstanding) liabilities and their corresponding assets. This approach risks overstating the value of assets in the balance sheet of the creditor, whereas under business accounting rules, the value of assets can be “written down” through provisions. For governments engaged in concessional or policy lending, such write downs can be significant—for example, student loans or high-risk mortgage loans issued on favorable terms. *GFSM 2014*, paragraph 5.20 recognized that the amounts recorded as government revenue from social contributions and taxes should include only amounts that are realistically expected to be collected, and requires an adjustment to both revenue and the accounts receivable for excess amounts. However, the same approach is not followed in recognizing assets associated with other amounts receivable such as loan repayments.

Debt Concessionality

12. Debt concessionality—the provision of loans or other instruments at below (or above[3]) market rates, typically for policy reasons (to give preferential treatment to a particular creditor or group of creditors—is particularly relevant to transactions that governments enter into. 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. In the IMF's *Balance of Payments and International Investment Position Manual*, sixth edition (*BPM6*), for cross-border debt concessionality it is advised that if significant these transfers be shown on a supplementary basis on a present value basis (*BPM6* paragraphs A2.67-2.70). Implicit subsidies are already recognized in the *GFSM 2014* in the case of concessional borrowing of employees (*GFSM 2014* §6.17) and central bank concessional transactions (*GFSM 2014* Box 6.2). Determining the consistent treatment of all concessional debt would need to be discussed again.

Leases to Use or Exploit Natural Resources

13. The *GFSM 2014* provides guidelines on recording licenses and permits to use natural resources in Appendix 4, Box A4.1. These guidelines are based on the *2008 SNA* guidelines. Current guidelines make a distinction between: payments treated as sales of assets; payments considered the payment of taxes; and payments that are treated as rent. Which treatment is applied affects GFS aggregates: sales of assets are not recorded as parts of government revenue at all, versus recording payments as taxes impacts the level of taxes/fiscal burden, and payments of rents that do not impact the fiscal burden but increase property income. The classifications of these transactions have significant impacts and changes to the treatment could significantly impact GFS aggregates for countries reliant on income from the exploitation of natural resources. However, it was found that in practice, making the distinction is not that easy. Therefore, further practical guidance on making these distinctions should be developed.

Distinction Between Current Maintenance and Capital Repairs

14. The *GFSM 2014,* paragraphs 8.25-8.27 draws a distinction between ordinary maintenance and repairs to fixed assets and major renovations, reconstructions or enlargements, but acknowledges that the distinction is not clear-cut. These guidelines are based on the *2008 SNA* guidelines. Institutional units classified as public sector are typically the owners of significant assets

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[3] For example, the UK government recently issued a number of "Pensioner Bonds", which paid above the prevailing market rate for UK government gilts.

subject to significant routine maintenance, such as road networks or other public infrastructure, and any change to the treatment will potentially impact estimates for expense, gross and net operating balances, and investment in nonfinancial assets data. Further practical guidance on making these distinctions should be developed.

Treatment of Private-Public Partnerships (PPPs)

15. PPPs are discussed in some detail in *GFSM 2014,* Appendix 4, and the guidance is based on similar guidance in the *2008 SNA*. The *2008 SNA* research agenda recognizes that work is ongoing on accounting standards, through the work of the International Accounting Standards Board (IASB) and IPSASB. Both standard setters have released their standards on Service Concession arrangement for respectively the operator (IFRIC 12) and the grantor (IPSAS 32). Broadly, the existing guidance in *GFSM 2014* decides on the treatment of assets built under PPP arrangements on the basis of economic ownership determined by the majority of risks and benefits.[4] The IPSAS 32 approach focuses on control of the asset, while aspects of the risks and rewards are used to determine control of the asset. The outcome using the statistical guidelines and the accounting standards could arguably leads to differences in treatment of PPP related assets. Therefore, some scope exists to further reduce the differences and clarify the guidance on how to treat these PPPs in the GFS. Further clarification on the interpretation of the notion of "majority" of risks and rewards should also be developed.

Treatment of Reinvested Earnings

16. The *2008 SNA* and *BPM6* recommends that the retained earnings of a foreign direct investment enterprise should be treated as if they were distributed to foreign direct investors in proportion to their ownership of the equity of the enterprise. These earnings are then reinvested by those owners as additions to equity in the financial account. This amount is in addition to any actual distributions made out of the distributable income. This approach is also adopted for the earnings of investment funds. A similar treatment could be adopted for other types of entities, where control exists, particularly public corporations. When these corporations are controlled by government units, retained earnings could be said to represent a deliberate investment decision of the owner and recorded as a transaction in reinvested earnings.

B. Other GFS Research Issues Identified

17. In the context of the update of the *GFSM 2014*, and in close collaboration with the IMF country teams and the GFS compilers, a number of additional issues have been identified that could require further clarification. As a starting point for discussions on the GFS research agenda, this paper includes seven of these issues.

[4] This is also the approach taken in Eurostat's *Manual on Government Deficit and Debt*.

Delineation of the Public Financial and Nonfinancial Corporations

18. The *GFSM 2014,* Chapter 2 provides detailed guidance on how to identify public sector entities, based on a set of indicators of control. The manual also includes guidance on how to delineate public sector units between non-market units (classified to the general government sector) and market entities (classified as public corporations). For entities involved in nonfinancial activities, this is often done using a partly quantitative approach looking at economically significant prices as determined by the relationship between sales and production costs, as well as other qualitative factors. For these entities, there remains an ongoing debate about what proportion of production costs need to be met by sales to consider an entity a market producer. For entities engaged in financial activities, it is less clear that a quantitative approach can be applied, and indeed the manuals arguably often take a functional approach to the classification of some entities—such as financial supervisory bodies—classified as financial auxiliaries despite, in many cases, their clearly nonmarket nature.

19. In addition, applying the measure of economically significant prices in the case of financial institutions need to be explored more fully. For some public sector entities engaged in financial activities, it is not clear that they are engaged in market activities—for example, government bailout operations during the financial crisis created numerous institutional units for which the market/nonmarket criteria did not work well. Many entities benefit from significant government guarantees for some or all of their assets and liabilities, or transfer all of their profits automatically to government. Some units are mainly or wholly funded by their parent government, some units only invest in government or other public sector units. Some units clearly charge non-economically significant prices (such as many deposit protection schemes or provident funds). Further guidance is therefore required on how to delineate between general government units and public units engaged in financial activities.

Application of Rerouting

20. The *GFSM 2014,* paragraph3.28 allows for the rerouting of transactions to better reflect the underlying economic reality. However, the guidance is limited on how widely to apply the rerouting principle. In a mixed economy, government, through regulatory or legislative measures, is widely involved in forcing transactions to take place that would otherwise not do so. In some cases, these mechanisms are introduced as direct substitutes for direct taxes and subsidies, such as renewable obligations in energy markets. Further guidance is required to determine how and when rerouting should be applied for GFS.

Terminal Costs

21. The *GFSM 2014* advises that costs of decommissioning fixed assets are to be included as acquisition of nonfinancial assets and written off over the asset life as part of cost of ownership transfer. If an asset is disposed of before the costs of ownership transfer are completely written off, the remainder of these costs should be recorded as another change in the volume of assets (see *GFSM 2014*, paragraphs 6.60 and 10.68). This treatment was adopted to avoid treating such decommissioning costs, incurred at the end of the life of an asset, as the acquisition of a nonfinancial asset, recorded against an asset without value. See also *2008 SNA*, paragraph 10.161.

22. The treatment of decommissioning costs has potentially significant implications for the general government and public sectors in many countries, especially in cases where they operate, or inherit, assets with particularly costly and problematic decommissioning processes—such as nuclear power stations or other "dirty" industrial facilities. Further practical guidance on what and how to record such costs in GFS should be developed.

Discount Rates

23. In the context of social security entitlements, or pension entitlements, the *GFSM 2014* requires these entitlements to be calculated at their net present value. The choice of the discount rate can have profound consequences on the reported size of these entitlements and the resulting government or public sector gross debt (in the case of pension entitlements). More guidance is required on the choice of the appropriate discount rate to use.

Equity of Government Units

24. In some countries, extrabudgetary units and lower level units of government at the state or local level are created by and controlled by the central government. In some cases, these entities have a positive net worth. In these cases, it is possible to argue that equity assets for the central government and matching equity liabilities for the extrabudgetary unit or lower level of government should be recorded, reflecting the residual claim of central government on these subordinate government units. This is currently done in a small number of countries, but could arguably be more widely adopted.

25. In cases where public units have been partly privatized, or cases such as non-market joint ventures, by convention classified as government units, this may also give rise to equity liabilities for government.

Valuation of Nonfinancial Assets of Public Sector Units

26. While conceptual guidelines on valuation of nonfinancial assets are clearly spelled out, in *GFSM 2014,* paragraphs 7.20-7.33 practical guidelines on determining the value of asset in the absence of public records creates several difficulties in the development of full balance sheets for public sector units. More specifically, public sector assets such as infrastructure, heritage assets, and specialized equipment often pose valuation challenges. More guidance is required on valuation techniques for various types of assets. In particular, further debate could be usefully informed by developments in the accounting standards on valuation and collaboration with the International Valuations Standards Council may be beneficial.

Leases

27. The ISASB and the Financial Accounting Standards Board (FASB) are deliberating a new lease standard to be issued during 2015. In accordance with current thinking on these leases, the divide between operations and financial leases will disappear, and all leases will be considered to be creating assets and liabilities. The premise is that all types of leases provides a source of financing and should be reported on a lessee's balance sheet. Current standards lead to most leases not being reported on a lessee's balance sheet which represents significant missing information on economic value. It is argued that the current treatment of leases make comparisons between entities difficult and obscure asset and risk exposures. Should proposed changes in the treatment of leases be adopted in the accounting world, there is a case to open up the same debate during the next round of manual updates.

C. Procedure to Update Methodological Guidelines

28. The IMF staff and the IMF Committee on Balance of Payments Statistics have developed procedures for updating methodological guidelines between major revisions of manuals.[5] It is proposed that similar procedures be adopted for GFS.

29. Under these procedures, updates can be divided into four types: editorial amendments; clarifications beyond dispute; interpretations; and changes.

- **Editorial amendments** refer to wording errors, apparent contradictions, and, for non-English versions of the GFS *Manual*, translation errors. These corrections affect neither concepts nor the structure of the GFS system. IMF staff will draft these amendments, which will be brought to the GFSAC electronically for information. An errata sheet will then be produced, and the amendments will be publicized on the website.

- **A clarification beyond dispute** arises when a new economic situation emerges or when a situation that was negligible when the *Manual* was produced has become considerably more important, but for which the appropriate treatment under existing standards is straightforward. IMF staff will draft these clarifications, based on existing recommendations, and after electronic consultation with GFSAC members, they will be publicized on the website and by other means, as needed.

- **An interpretation** arises when an economic situation arises for which the treatment under the Manual may not be clear. Several solutions on how to treat the situation may be proposed, because it is possible to have different interpretations of the Manual. In this case, IMF staff, in consultation with the GFSAC will draft preliminary text that will be sent to panels of experts, and to the Inter Secretariat Working Group on National Accounts (ISWGNA) (if also relevant to the

[5] *BPM6* sets out various types of issues that can arise and the actions to be taken to provide clarification. Please see *BPM6* paragraphs 1.37-1.42.

SNA). IMF staff will propose a final decision, in consultation with the GFSAC. Interpretations will be publicized on the website and by other means.

- **A change** to the GFS framework arises when an economic situation occurs in which it becomes apparent that the concepts and definitions of the GFS framework are not relevant or are misleading and will require change. In such a situation, parts of the *Manual* may need to be substantially rewritten to reflect the needed changes. In such a case, IMF staff, in consultation with the GFSAC, will prepare proposals that will be disseminated widely to panels of experts, the ISWGNA (if also relevant to the SNA), and all IMF member countries. The GFSAC will advise how such changes should be incorporated into the framework, whether promulgated immediately through a booklet detailing the amendments to the *Manual* or by issuing a new *Manual*. Information will be produced and provided to all countries with changes also publicized on the IMF website and by other means.

III. POINTS FOR DISCUSSION:

- Do GFSAC members agree with the issues discussed in the paper? Are there additional issues where further clarification or methodological guidance is required?
- Do GFSAC members agree to have guidance on addressing these issues, similar to that set out in the *BPM6*, paragraph 1.37 to 1.42?
- Given resource constraints and competing demands, which are the priority research areas to be discussed and resolved?