Issue 40 Goods for processing
As earlier commented Statistics Norway does not support the recommendation to treat goods sent abroad for processing on a net basis. We think this recommendation pays too much attention to the wish to avoid imputed ownership changes, relative to the need to describe actual production activities for those units doing the processing in question.

The most important argument in support of the new proposal is that the institutional model is based on the fundamental nature of transactions as arrangements between two parties where the ownership of economic resources or values changes from one party to the other. In addition, net recording is probably more consistent with the payments between the involved parties and also more in line with the records found in their accounting books. However, these arguments seem to be based on more practical than principal considerations.

Choosing gross or net recording of processing is a question of what kind of map over the production activities we want the Supply and Use tables of the National Accounts to present to its users, which in turn will depend on what analytical needs they have.

The starting point in constructing the National Accounts is the notion of *institutional* units and the economic relationship between them based on the concept of ownership to resources or economic values. Ownership can be thought of in an institutional perspective as a *strict legal* concept, but also in a non-institutional *economic perspective* in terms of "right to use" disconnected from strict legal ownership. Normally those two sides of ownership coincide, but in some cases the two perspectives clashes and the latter perspective has been recommended.

Financial leasing is such a case, where the institutional model would imply gross fixed capital formation of leased assets in the financial enterprises sector. Instead the *real sector* model is used implying gross fixed capital formation in the sector *employing* the assets in its production activities. The justification is obviously to accommodate production and productivity analyses, i.e. the industry based production of goods and services combining raw materials, man-power and fixed capital, in a consistent manner.

Another example is found in the geographical allocation of *freight* recorded on the Rest of the World Account or the Balance of Payments. According to the institutional model freight is to be allocated to the country in which the legal *contract counterpart* is resident. In many cases this will be a different country from the country to which the goods physically are transported. By convention however, the freight services are deemed consumed by the goods importing country, another case of choosing the real sector model[1] in favour of the institutional model.

Returning to the case of processing, the institutional model or net recording would mean that country B according to National Accounts do not produce goods and do not consume raw materials in its production. Thus the National Accounts of country B will describe services production activities (processing) employing employment and a fixed capital stock scaled towards goods production. The opposite will be the case for country A, the National Accounts will show production of goods without necessary employment or fixed capital stock.

Another point is that the link between production data of the National Accounts and *environmental* data might be meaningless without having the national Accounts giving a physical description of the process of producing goods and services.

[1] This is a parallel case to the recording of transport margins as part of the purchaser's value of the goods.

Finally, it can be mentioned that the WTO[2] negotiators are requesting data according to the real sector or product flow model. The reason being that in the bilateral legal trade agreements between countries separate rules are employed for merchandise trade and for trade in services, and it is paramount to avoid countries escaping the rules prevailing on the goods sector by referring to the statistical convention of treating goods production on contract basis as services.

The problem of recording of processing in the National Accounts and Balance of payments statistics might also be seen as part of a more general question of how to view and treat manufacturing units in statistics when their physical goods production is moved abroad, keeping only development and distribution activities left in the first country. The questions are both how to *record income and costs*, i.e. gross or net recording, and how to *classify* units when such structural changes take place.

Our view is that gross recording is the most appropriate method that serves the user needs best. From this follows that units engaged in processing (country B) are to be classified accordingly in the manufacturing industry.

If, however, net recording will be recommended, the classification question must be addressed. Units engaged in processing and recorded net must be kept separate from ordinary goods producing units. A symmetrical recording of the parent enterprise (country A) would imply that also this unit is kept separate from ordinary goods producing manufacturing units, and classified in accordance with the services activities it is engaged in (research and development, marketing etc.).

A disturbing fact is however that the NACE[3] committee in Eurostat has decided that parent companies keeping the legal rights to goods produced physically abroad are to be classified as manufacturing units. If this decision is maintained it must be made clear that such units is kept separate from other manufacturing units[4] by the introduction of a new type of industries to be called *manufacturing services or industrial services*[5].

The main question is what information should be found in the Supply and Use tables of the National Accounts. In our opinion information according to the real sector model, i.e. technological and physical based information needed to analyse production and productivity in a meaningful way, is to be preferred. This implies gross recording of processing in the National Accounts and Balance of Payments.

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[2] World Trade Organisation.
[3] The European industry classification
[4] A separate coding of such units has already been introduced in the Norwegian business units register.
[5] If such a category is not introduced in the NACE, the National Accounts should consider to introduce it independently.