

# **The production of financial corporations and price/volume measurement of financial services and non-life insurance services**

## **Summary conclusion**

### ***Recommendations/questions***

1. The work of the Task Force on Financial Services resulted in nine carefully worded recommendations covering the definition of a financial institution, the definition of financial services and the measurement of financial services in volume terms. These were:

### ***Financial institutions***

### ***Recommendations/questions***

- (a) A definition of financial corporations based on the nature of their output (financial services) instead of their activity. “Risk Management” and “Liquidity transformation” activities are added to “Financial intermediation” to better capture the nature of the activities of financial corporations.
- (b) That no FISIM is recorded for non-financial corporations. Only explicit financial services are recorded for such units.
- (c) That units which provide financial services exclusively with own funds would be considered financial corporations and will thus be productive in the sense of SNA if they provide loans to a range of clients and incur the financial risk of the debtor defaulting.
- (d) That units producing financial services for only one unit or a group of units are considered as financial corporations if they keep a complete set of accounts and are capable of acquiring assets and incurring liabilities on their own account.

## **Outcomes**

- (a) The AEG agreed with recommendation (a) on the definition of financial corporations and financial services. The service charge for money lenders can be compiled as the difference between the amount paid as interest and the reference rate times the amount of the loan.
- (b) The AEG agreed that, by convention, FISIM would be restricted to (i) financial corporations and (ii) loans and deposits<sup>1</sup>.
- (c) The AEG agreed that lending own funds may be a financial service and may include a service charge, though not financial intermediation activity. Incorporated money lenders should be treated as part of the financial corporations sector. Unincorporated

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<sup>1</sup> The service provided by money lenders, though calculated in the same way as FISIM, is not an intermediation service as such but should be regarded as an explicit fee for a lending service.

enterprises which provide loans to a range of clients other than just family and friends, and take on the financial risk of the debtor defaulting, as a principal activity, should be treated as unincorporated enterprises (money lender) in the (informal) household sector or as quasi-corporations if they have sufficient accounting information to qualify as a quasi-corporation.

- (d) Discussion of recommendation (c) was postponed to the discussion on units.

### *Financial services*

#### **Recommendations/questions**

- (e) That expected holding gains and losses should not enter into the measurement of financial services output.
- (f) That FISIM should be systematically allocated. It is primarily deposits and loans attract implicit charges and these instruments are included in the calculations of FISIM. The calculation of FISIM should be based on the formula  $(r_L^t - rr^t)y_L^t + (rr^t - r_D^t)y_D^t$ . In this formulation,  $y_L$  is the amount of loans,  $y_D$  the amount of deposits,  $r_L$  is the loan rate,  $r_D$  the deposit rate and  $rr$  is a reference rate. This implies a change to the 1993 SNA that recommended calculating FISIM as “the total property income receivable by financial intermediaries minus their total interest payable, excluding the value of any property income receivable from the investment of their own funds, as such income does not arise from financial intermediation” (paragraph 6.125)
- (g) That the reference rate used in the compilation of FISIM should be a risk-free reference rate that has no service element in it and that reflects the maturity structure of the financial assets and liabilities to which FISIM applies. A single rate should be used for transactions in the local currency, whereas different rates may be used for transactions in other currencies.
- (h) That with respect to market making and trading services, the measurement of the implicitly priced elements - margins on foreign exchange and buying and selling of all securities by all financial corporations - be made regardless of the purpose for which the securities and other instruments are being bought or sold.

#### **Outcomes**

- (e) The AEG agreed with the recommendation to not include expected holding gains/losses in the measurement of financial services output but noted this may have to be reviewed in the context of consistency.
- (f) The AEG agreed.
- (g) The AEG agreed that a single reference rate should be used but, when relevant, a country could choose to use multiple rates. The reference rate used in the compilation of FISIM should be a rate that has no service element in it and which reflects the risk and maturity structure of the financial assets and liabilities to which FISIM applies. It is recommended that different reference rates should be used for transactions in other currencies.

- (h) The AEG agreed that the margins on buying and selling of all securities by all financial corporations represent financial services. When there is a delay between purchase and sale of a security the margin at the time of each transaction should be used to eliminate holding gains/losses. The margin is calculated as the difference between the mid price and the buy/sell price.

*Measurement in volume terms*

**Recommendations/questions**

- (i) That in the absence of direct deflators for the output of implicitly priced financial services at current prices, the rate of change of the volume indicator should be derived using the rate of change of stocks of loans and deposits deflated by a general price index (e.g. the GDP deflator) or using a direct output indicator method.
- (j) That in the absence of a direct deflator of non-life insurance output, to compile a direct volume indicator using one of two methods described in recommendation (i), and obtain the price index as the ratio between the current price series and the volume series:

**Outcomes**

- (i) The measurement of the volume change in the output of financial intermediation should take into account the total output, including the direct charges. In the absence of direct deflators for the output of FISIM, one of the following approaches may be used:
  - (i) rate of change of the volume indicator can be derived using the rate of change of average stocks of loans and deposits deflated by a general price index (e.g. the GDP deflator) adjusted for quality change in the output of financial services
  - (ii) the output indicator method which involves breaking down the different characteristics linked to financial services (numbers and values of loans and deposits, savings, money transfers, etc). For each of the characteristics an appropriate volume indicator is to be derived. The volume indicators are then weighted together.
- (j) The AEG agreed to the recommendation on the calculation of a volume estimate of non-life insurance services.