Minutes

ISWGNA Meeting
IMF, Washington DC
November 1-2, 2007

Participants:
Eurostat: Gallo Gueye and Christian Ravets
IMF: Kim Zieschang (Chair) and Lisbeth Rivas
OECD: Charles Aspden
UNSD: Ivo Havinga
UNECE: Not present
World Bank: Barbro Hexeberg
1993 SNA Update Project: Carol Carson (Project Manager), Anne Harrison (Editor)

1. Comments on Chapters 3-5, 16,and 17 Adds for chapters 7, 8 and 9 and other substantive issues

Please see the attached note from the Editor on these topics.

2. Codes

ISWGNA:NA agreed with the coding system prepared jointly by Eurostat, the OECD, the IMF and UNSD. Mr. Aspden (OECD) would incorporate the agreed minor changes to the coding system and will have them ready by Friday November 9 for circulation among ISWGNA:NA.

3. Steps towards first deliverable

The following was agreed on the remaining work for the first deliverable:

The Editor will complete drafting and provide to the ISWGNA chapters 3-17 by the end of 2007 and chapters 1-2 to the ISWGNA by early 2008. The final draft chapters 3-17 will be accessible by the end of 2007 and Chapter 1-2 by the end of January 2008 from both the SNA part of the UN Update Project website and also from the Statistical Commission (SC) part. The document will be issued in white paper in May 2008.

Regarding the longitudinal review of the chapters during the month of January 2008, the meeting divided the review by issue and by chapter as follows:

Issue by issue review:
- Non-financial assets (OECD)
- Government and public sector (Eurostat/IMF)
- Financial services (IMF/Eurostat)
- Financial institutions (IMF)

- Rest of the world (IMF)
- Units (UNSD)
- Informal and illegal (UNSD)
- Other, interest under high inflation (World Bank)

Chapter by chapter review:
- 3,4,5,14,15, and 16 (World Bank and assistance by IMF on chapter 16)
- 6,7,8,9, and 10 (UNECE)
- 11,12,13, and 17 (UNSD)

The ISWGNA: NA agreed to indicate in February next year where it would be useful to have external contributions of text for the second deliverable. In addition, the meeting agreed that the several factors that should be considered in giving the title to the volume be reviewed. It was also suggested that the management group consider whether the translation of the document be done by regular translations staff or whether, as for the *1993 SNA* persons with knowledge of or links to national accounts staff be approached to see if they could assist with the translations.

4. Management (MG) meeting November 4

The Project Manager previewed the issues to be covered during the MG meeting.

5. Implementation strategy

The Chair made a presentation on the implementation strategy to introduce the paper on this topic. He mentioned that the main limitations of developing countries to implement the *1993 SNA* and its revision is the lack of resources to compile the necessary source data as well as expertise to retain staff. Based on country feedback in regional meetings, international organizations and other providers of technical cooperation will need to coordinate better to meet these remaining needs. He also suggested using a common framework and language across countries to implement the revision of the *1993 SNA*. This common language would apply to structuring system-wide approaches to statistical capacity building such as the National Strategies for Development of Statistics (NSDSs).

The chair informed the meeting that approximately four pages on the Implementation Strategy for Economic Statistics founded within the SNA would be prepared for the ISWGNA report to the Statistical Commission by the end of November. The document will cover the most important issues of the revision that need harmonization among the different macroeconomic statistics, such as goods for processing and the links to *BPM6*, debt and the public sector and their links to the *GFSM*, as well as FISIM, insurance, pension funds, the informal sector, and capital services. The meeting also agreed that the text should give some additional space to the implementation of the updated SNA in OECD countries, in addition to its current focus on the foundations for SNA implementation in developing statistical systems such as building institutional capacity, developing source data, and implementing and maintaining supply and use tables.

6. SNA News and Notes

The meeting agreed to include an article on the impact of the *1993 SNA* Rev.1 and on the implementation strategy in the next SNA News and Notes.

7. Next teleconference

The next teleconference of the ISWGNA:NA will be on November 14, 2007 at 9:30 am Washington time and the following teleconference will take place on November 26 at 9:30 am Washington time.

8. To-do list

Action	By when	Responsible	Status
Report on the High Level Group considering future directions for the national accounts	End October	UNSD	Done
Outline of Chapters 1 and 2	October 19	Anne Harrison (Editor)	Done
AEG comments on Editor's proposals for Chapters 1 and 2	November 30	AEG members	Pending
Timeline for delivery of the implementation strategy to UNSC	October 15	Kim Zieschang (IMF)	Done
Timeline for preparing the report to the UNSC	October 19	UNSD	Done
Processed comments on Chapters 3, 4, 5, 7 Add. 1, 8 Add. 1, 9 Add. 1, 15, 16, and 17	October 12	Agencies and editor	Done
Revised codes to the Editor by end-September	September 28	Christian Ravets (Eurostat) Charles Aspden (OECD) Kim Zieschang (IMF) Ivo Havinga (UNSD)	Done
Chapter 6: Disposition of comments on treatment of central bank output	End-August 2007	Kim Zieschang (IMF)	Done
The Project Manager will prepare a draft letter to the ECB about ECB's comments on the mapping of taxes from the classification in the GFSM and the OECD's Revenue Statistics	End-July 2007	Carol Carson (Project Manager)	On hold
Chapter 12. Draft text on the properties of the "general price index" for distinguishing real and nominal holding gains in the holding gains and	End-September 2007	Ivo Havinga (UNSD) Kim Zieschang	Done

Action	By when	Responsible	Status
losses account for the research agenda.		(IMF)	
Update of the Full Set of Consolidated Recommendations (44 issues document) to incorporate changes and UNSC decisions	When possible	Anne Harrison (Editor)	Pending
Prepare a document for discussion on insurance	Before Paris	Anne Harrison (Editor)	Done
Organize an informal meeting with the AEG members present at the OECD meeting	Mid-September 2007	Kim Zieschang (IMF) Charles Aspden (OECD)	Done
Develop an example on insurance that includes the compilation of the complete set of accounts with data from the books of insurance companies.	First draft March 2008	Ivo Havinga (UNSD) and Christian Ravets (Eurostat)	Pending
Send the note prepared by the ETFP on the treatment of changes in pensions to the Editor	November 20	Gallo Gueye (Eurostat)	Pending
UN Statistical Commission Report	November 26	Carol Carson (Project Manager) Kim Zieschang (Chair) Ivo Havinga (UNSD)	Pending
Room document on Implementation Strategy	January 31	Kim Zieschang (Chair) Ivo Havinga (UNSD)	Pending
SNA News and Notes Contributions	December 15	Ivo Havinga (UNSD)	Pending
Check the treatment of annuities with specialist	November 23	Ivo Havinga (UNSD)	Pending
PDF files on Editor comments	November 19	All	Some Pending
Provide comments on the Implementation Strategy document	November 17	All	Pending

Items marked as 'Done' in this to-do list will be omitted in the following to-do list.

Substantive points from ISWGNA meeting November 1-2, 2007 Washington

The main part of the discussion was based on the attached document describing the main points emerging from an analysis of the comments on chapters 3, 4, 5, 16 and 17 and the add 1's for chapter 7, 8 and 9.

Chapter 3: stocks, flows and accounting rules

Benefits. It was agreed to use the definition of economic benefit in the WB glossary and then extend it to follow the last part of Charlie Aspden;s suggestion. This will not be flagged as a definition, though.

Liabilities It was agreed to add a sentence making clear there are no non-financial liabilities in the System.

Shares It was agreed to remove the phrase that shares are an asset "by convention" and make clear the exception concerned the liability implied by holding shares.

Allocation of taxes between levels of government It was agreed to adopt the GFSM2001 text as a replacement for all except the first sentence of para 3.68

Chapter 4 Institutional units and sectors

Residence Para 4.15 will be restored to the SNA. The SAS type case will be mentioned explicitly. The use of tax law as one indicator of determining the centre of predominant economic interest will be kept.

Holding companies The ISWGNA confirmed these should be financial auxiliaries not captives. In places the text needs to make use head office rather that holding company and ensure compatibility with ISIC. The holding company of a group of non-financial corporations stays in the financial corporations sector.

Artificial subsidiaries No better term that artificial subsidiaries could be found for the phenomenon being described in paras 4.52 to 4.54. Although such units may be established legally, they do not qualify as institutional units because they do not have the freedom to set their level of output and prices independently of their parents. The text will include a sentence making explicit that this section is not a discussion about ancillary activities. The ISWGNA confirmed that ancillary activities are a limited set of services and not any good or service delivered only to the parent or other units in the same enterprise group.

Quasi-corporations It is agreed that quasi-corporations require the existence of full accounts including balance sheets. Otherwise, unincorporated enterprises remain in the sector of their owners including government when appropriate.

Financial sub-sectoring A sentence will be added making clear that insurance corporations and pension funds are treated as financial intermediaries. It is confirmed that credit insurance corporations and guarantee banks must have differentiated pools of reserves to meet claims so para 4.104(j) will be dropped.

Chapter 16: Prices and Volumes

Introducing road charging This will be treated as a special case of a new product.

Services prices Reference will be made to the OECD/Eurostat manual.

PPP detail. The proposal was accepted.

Chapter 17.1 Insurance and annuities

Diagram The revised diagram proposed by the editor was accepted , noting that the phrase "private" should be replaced by "other employment related".

Tables It was agreed to leave the tables as they are (subject to arithmetic checking) but the possibility of preparing more extensive tables and explanations will be kept on the table for incorporation in another document, possible the handbook on financial services that UNSD is preparing.

Annuities Ivo Havinga offered to contact a friend who is an actuary to see if either of the two numerical examples accurately reflect industry practices.

Chapter 17.2 Standardised guarantees

It was agreed it was an unnecessary refinement to introduce "expected calls" into the formula for calculating the output of services connected with standardized guarantees.

Chapter 17.3 pensions

The ISWGNA discussed coordination with the on-going work of the ECB/Eurostat task force to ensure that if any divergence with the SNA text emerged, the ISWGNA would be alerted promptly.

Defined contribution scheme payouts The ISWGNA agreed the text should be changed. When DC benefits must be taken in the form of an annuity, the two transactions currently specified of receiving a lump sum and reinvesting it will not be shown; a reclassification would be recorded instead.

If an annuity yields a fixed income (or one determined by indexation) then the whole of the amount received will be recorded as property income.

ABO/PBO The ISWGNA discussed the way in which various changes in pension regimes should be recorded in the System under ABO and PBO schemes and reached the following conclusions.

Under an ABO scheme based on final salary, when an individual receives a promotion, this entails an increase in the accumulated to date liability of the employer towards the employee. The ISWGNA were firmly of the opinion that this should not be regarded as a retrospective revision to compensation of employees over the time the employee had been working for that employer. They also agreed that there should not be a one-off increase in compensation of employees to capture this increase in benefits either. This left the only options as either a capital transfer payable by the employer to the employee or an entry in other volume changes. The ISWGNA noted the symmetry with the way any impact on pensions should be recorded in the case of a demotion and suggested this was similar to an "uncompensated seizure" and this argued in favour of an other volume change rather than a capital transfer that must be entered into voluntarily by both parties.

but the ISWGNA believed the "cohort effect" would dampen any potential large up-swings in liabilities.

Under both ABO and PBO, when an employer changes the conditions of the pension schemes, the consequences should be recorded as other volume changes.

Under PBO changes in the level of liabilities of the employer due to changes in structure of the work force and consequent changes in the expectations of promotions (such as management delayering, for example) should be recorded as other volume changes.

Eurostat staff will discuss this specific points with task force staff and report back to the ISWGNA if the task force has any disagreements with the proposals.

Segregated (largely) unfunded schemes The Editor's proposal was accepted. If a scheme is run in such a way that a separate scheme exists but it is significantly underfunded, this should be treated as normal but with responsibility for paying only that part of pensions corresponding to the proportion of contributions payable that it actually receives. The remaining part should be treated as a scheme run by and not segregated from the employer.

Chapter 17.4 Financial services

It was confirmed (again) that the material in chapter 17 covers more than considerations relating to chapter 11 and it was not advisable to locate all the material in this part of chapter 17 in chapter 11.

Chapter 17.5 Contracts, leases and licences

The ISWGNA discussed the possibility of generalising the text on mobile phone licences. This will not be easy but the Editor and Gallo Gueye will have bilateral discussion in the coming weeks to see if some acceptable generalisation can be put forward.

Chapter 7 Add 1

Most of the comments received were editorial in nature. Some of the suggestions from the IMF are not altogether clear. The Editor will speak to those who made the comments to better understand the position.

Israel suggested including a direct quote for the previous annex on the treatment of interest under high inflation. The ISWGNA preferred to have a lower key reference to the fact that the separation of interest into a real element and an element to compensate holding gains and losses was a matter on the research agenda.

Chapter 8 add 1

The Editor will consider reversing the order of section 1 and 2 so as to describe first how social benefits are treated and then what is excluded from social benefits. Furtehr clarity is needed to explain why non-pension benefits need to be distinguished between those that are funded and those that are unfunded.

Chapter 9 Add 1

Few comments were received. Some consideration needs to be given to whether the changes indicated belong in chapter 8 or 9.

Other substantive issues

Output of central bank The proposed text was agreed subject to two amendments. In the first paragraph, add before the last sentence: “However, it is frequently the case that the interest rates offered by the central bank are not determined by market forces but by policy considerations. In this case, it is not appropriate to consider the difference between the interest charged and paid by the central bank and interest calculated using a reference rate as market production of financial intermediation services.” At the end of the second new paragraph, add “ in cases where separtion of market and non-market output is not made, the whole of the output should be treated as non-market and valued at the sum of costs.”

Harmonisation with ISIC Ivo Havinga raised the following issue.

> Para 5.4 of the draft Chapter 5 of the SNA makes a mention that definitions, ... are consistent with the definitions in the fourth revision of the International Standard Industrial Classification of All Economic Activities (ISIC, Rev.4), published by the United Nations. But there are differences in the text of the SNA chapter 5 and of the ISIC Introduction draft (10 October 2007 version), which are mentioned below:
>
> **1. Horizontal integration of activities**
> SNA Chapter 5 (para 5.20): defines an establishments within integrated enterprises as "A horizontally integrated enterprise is one in which several different kinds of activities that produce different kinds of goods or services for sale on the market are carried out in parallel with each other." This is similar to the definition of an enterprise with multiple independent activities which is denied in the ISIC introduction text (para 103).as "If a unit is engaged in several types of independent activities, but the unit itself cannot be segregated into separate statistical units (when, for example, manufacture of bakery products is combined with manufacture of chocolate confectionery)
>
> ISIC Introduction defines (para 108) the horizontally integrated activities as "Horizontal integration occurs when an activity results in end-products with different characteristics. This could theoretically be interpreted as activities carried out simultaneously using the same factors of production. ....In this case , it will not be possible to separate them statistically into different processes, assign them to different units or generally provide separate data for these activities. ... Another example would be the production of electricity through a waste incineration process. The activity of waste disposal and the activity of electricity production cannot be separated in this case....".
>
> **2. Recommendation for classification of the vertically integrated enterprises**
>
> The SNA Chapter (para 5.24) states " Despite the practical difficulties involved in partitioning vertically integrated enterprises into establishments, it is recommended that when a vertically integrated enterprise spans two or more sections of the ISIC, at least one establishment must be distinguished within each section. ISIC sections correspond to broad industry groups such as agriculture, fishing, mining and quarrying, manufacturing, etc."
>
> Whereas the ISIC Introduction text (para 106) states "In ISIC Rev.4, vertical integration should be treated like any other form of multiple activities, i.e. a unit with a vertically integrated chain of activities should be classified to the class corresponding to the principal activity within this chain, i.e. the activity accounting for the largest share of value added, as determined by the top-down method". The ISIC recommendation will always identify only one establishment in a vertically integrated enterprise even if its activities span over two or more sections of the ISIC.
>
> Both are international standards and need to be harmonised.

The ISWGNA agreed that the wording of ISIC on horizontal integration should be incorporated into the SNA description. On vertical integration the SNA takes a different line, suggesting that separation into establishments is desirable. The SNA should explain the ISIC position and make clear that SNA is deliberately different. However, the whole subject of the treatment of establishments in the SNA could be put on the research agenda since developments in input-output tables and the proposals on goods for processing suggest a new look at the existing conventions would be beneficial.

Franchise fees In connection with the BOPCOM meeting, the question of the treatment of franschise fees had been raised. Since franchises are now specifically mentioned as part of marketing assets and thus non-produced assets, it would seem that franchise fees should be treated as property income rather than services. However it was noted that the units managing franchise fees do indeed provide services as well as permit the use of the franchise. Although conceptually the franchise fee thus includes an element of services and an element of some form of property income (rent) in practice it is not likely that such a separation could be made and as a result the whole of the franchise fee may be treated as a service. Two notes were made. The first is that franchise fees have until now been treated in BPM as services, so this proposal does not lead to a change. Secondly, if such a separation were regularly possible, then it would be possible to derive a value for the franchise and its treatment as a produced asset could be reconsidered sympathically.

Insurance claims as capital transfers BOPCOM had again raised the question of whether the AEG recommendation to permit some insurance claims to be recorded as capital transfers could be reversed. The ISWGNA understood their position but felt it was not possible to go further than agreed at the meeting in Paris when the subject was debated at length.

Anne Harrison

8 November 2007

Chapter 3: Stocks, flows and accounting rules

5 Issues: Discussion of benefits (around para 18)

Definition of an asset (around para 29)

Financial claims and liabilities (around paras 31-33)

Financial assets and shares (para 35)

Rules for allocating taxes between various levels of government (para 68)

None of these are major substantive issues but rather turn on the exact use of words and phrases. I have listed some of the key points and assuming that we agree what the key points are, I will prepare new text and circulate it to the ISWGNA to give you an opportunity to respond as to whether you think I have answered the comments adequately

Benefits

When I originally proposed text about the definition of an asset, I suggested talking in terms of 'rewards" as in risks and rewards that we associate with assets. I pointed out that benefit might be confused with social benefit (and with social insurance and pension benefits) but was told, no, benefit was the word to use. However, several comments query the use of the word and the meaning given to it.

Charlie suggested explaining its normal English language meaning and then go on to explain how it is used in the System as follows:

"In normal English usage benefits are things are things one receives or confers on someone else. In the national accounts its meaning has been extended to include what one gives up to acquire something else. Hence benefits are defined as follows. *Benefits are the rewards for providing services, such as those of capital and labour, to production and also the means of acquiring goods and services for production, consumption or accumulation in the current period or in future periods.*"

However, his interpretation of normal English usage does not match the dictionary definitions which are: advantage, government assistance, extra employee assistance or performance for charity. However, there is a definition of an economic benefit as "denoting a gain or positive utility arising from an action. It implies a comparison between two states." This is in the World Bank glossary of economic terms but I also met it elsewhere with an EU citation.

Questions: 1 Do I continue to work with benefit or revert to rewards?

2. If I use benefit are you happy with the definition found for economic benefit which can then be followed by an explanation that they can be used to acquire goods and services now or in future?

Definition of an asset

The text needs to be extended to cover risk, demonstrable value and contingent liabilities.

Financial claims and liabilities

Miscellaneous comments about whether we need to define financial claims. The concept is embedded in the BPM6 and well as 1993 SNA and I believe we should keep it.

Do we say "liabilities " or "financial liabilities"? It may be worth stating explicitly that there are no non-financial liabilities in the System. To me if we talk about non-financial assets and financial assets and liabilities, liabilities are by implication financial and since they appear only in the financial account this is no bad way to refer to them. Does anyone feel strongly that I should ensure financial is never attached to liabilities?

There need to be a bit more on contingent liabilities with examples.

Shares

The text of shares being assets by convention needs tidying. They are assets; it is the liability aspect that carries conventional overtones because there is no predetermined payment due on them as there is on securities.

Rules for allocating taxes between various levels of government

I have consulted with Charlie and with Cor Gorter. I suggest we replace para 3.68 with paras 5.25 to 5.28 from GFSM2001. They read as follows:

> **5.25** In general, a tax is attributed to the government unit that (a) exercises the authority to impose the tax (either as a principal or through the delegated authority of the principal), (b) has final discretion to set and vary the rate of the tax, and (c) has final discretion over the use of the tax proceeds.
>
> **5.26** Where an amount is collected by one government for and on behalf of another government, and the latter government has the authority to impose the tax, set and vary its rate, and determine the use of the proceeds, then the former is acting as an agent for the latter and the tax is reassigned. Any amount retained by the collecting government as a collection charge should be treated as a payment for a service. Any other amount retained by the collecting government, such as under a tax-sharing arrangement, should be treated as a current grant. If the collecting government was delegated the authority to set and vary the rate as well as decide on the ultimate use of the proceeds, then the amount collected should be treated as tax revenue of this government.
>
> **5.27** Where different governments jointly and equally set the rate of a tax and jointly and equally decide on the distribution of the proceeds, with no individual government having ultimate overriding authority, then the tax revenues are attributed to each government according to its respective share of the proceeds. If an arrangement allows one government unit to exercise ultimate overriding authority, then all of the tax revenue is attributed to that unit.

5.28 There may also be the circumstance where a tax is imposed under the constitutional or other authority of one government, but other governments individually set the tax rate in their jurisdictions and individually decide on the use of the proceeds of the tax generated in their jurisdictions. The proceeds of the tax generated in each respective government's jurisdiction are attributed as tax revenues of that government.

Does the ISWGNA agree with this proposal?

Chapter 4: Institutional units and sectors

5 issues: The definition of residence

The definition of holding companies

“Artificial subsidiaries”

Quasi-corporations

Financial sub-sectoring

As for chapter 3, most of the points refer to drafting not substantive issues.

Residence

There are five comments that touch on this. I have shown them to Rob Dippelsman to see how we can accommodate the comments and still keep SNA and BPM in line.

We think the old para 4.15 is a helpful summary and should be restored.

We can add something about the SAS type case.

The Swiss comment that defining centre of predominant interest in terms of tax law is circular we have some problems with. Does anyone think this is a significant problems and if so what do we do about it?

Holding companies

Do holding companies come under financial auxiliaries or captive financial institutions. At present the text says auxiliaries. Only Netherlands has queried this. What is the ISWGNA view?

Australia is still unhappy about having a holding company of a non-financial group in the financial institutions sector. I think this is reopening an issue. Do you agree?

“Artificial subsidiaries”

I am very uncomfortable with a heading called “ancillary corporations” over text that explains these do not exist in the SNA. Further, the situation being covered, for example when an artificial unit is established to supply labour to the parent organization, is not undertaking an ancillary activity as defined in the system. In trying to find a different term, I came up with ‘artificial subsidiary”. This has given rise to two quite separate sets of comments.

The UNSD would like to keep to the 1993 text but rather assumes the case being dealt with is one where the services being provided are ancillary in nature.

The other concern is that the tem “artificial subsidiaries” could be interpreted to cover SPEs and out-sourced units.

I think there are two questions to answer:

1. Is the previous text clear and unambiguous?

2. If not, and a change of terminology is desirable, do we keep “artificial subsidiaries” and make clear it is not meant to cover SPEs and out-sourcing or find a new term? If so what?

Quasi-corporations

The paras concerned are 4.40 and 4.139. I think this is the same problem we encountered in chapter 6. Netherlands suggests that market activities within government should always be treated as quasi-corporations. My understanding that is this is so if the full set of information including balance sheets is available, but if not the activity is an unincorporated enterprise within government. Perhaps 4.139 needs to reinforce the need for full information including balance sheets?

Having said that, we do treat overseas branches as quasi-corporations regardless of whether they have a full set of accounts including balance sheets. Do we need to do anything to explain this apparent inconsistency?

Financial sub-sectoring

Not all readers immediately appreciate that we treat insurance and pension funds as financial intermediaries. Extra text should be added to make this clear.

A question is raised about whether the units described in para 4.104 (j) actually exists. “These are credit insurance corporations and guarantee banks that do not have differentiated pools of reserves to meet claims” I will pursue with colleagues within the IMF before we meet.

Chapter 5: Establishments and industries

There are many comments but none requiring ISWGNA input.

Chapter 16: price and volume measures

3 issues: “Introducing road charging”

Services prices

PPP detail

Introducing road charging

The ECB asks for guidance on how to deal with the introduction of charges for services previously provided free such as introducing road charging. My sense is that this is just a special case of a new product. Is this right? Would it be sensible to include a sentence about this?

Services process

Several commentators mention the desirability of including reference to the OECD/Eurostat guide for PPIs for services. Sounds a good idea.

PPP detail

Two complementary suggestions on section D. first, introduce the idea that the PPP process has two stages, one below basic heading where no weighting is done, one between basic headings that does include weighting. Secondly, drop the detail on CPD which applies only to the below basic heading level. Do you agree?

Chapter 17.1 Insurance and annuities

4 sets of Issues: Problems associated with equalization provisions and capital transfers

> Introduction of a diagram showing the relationship between the different sections
>
> Problems with the tables
>
> Problems associated with annuities

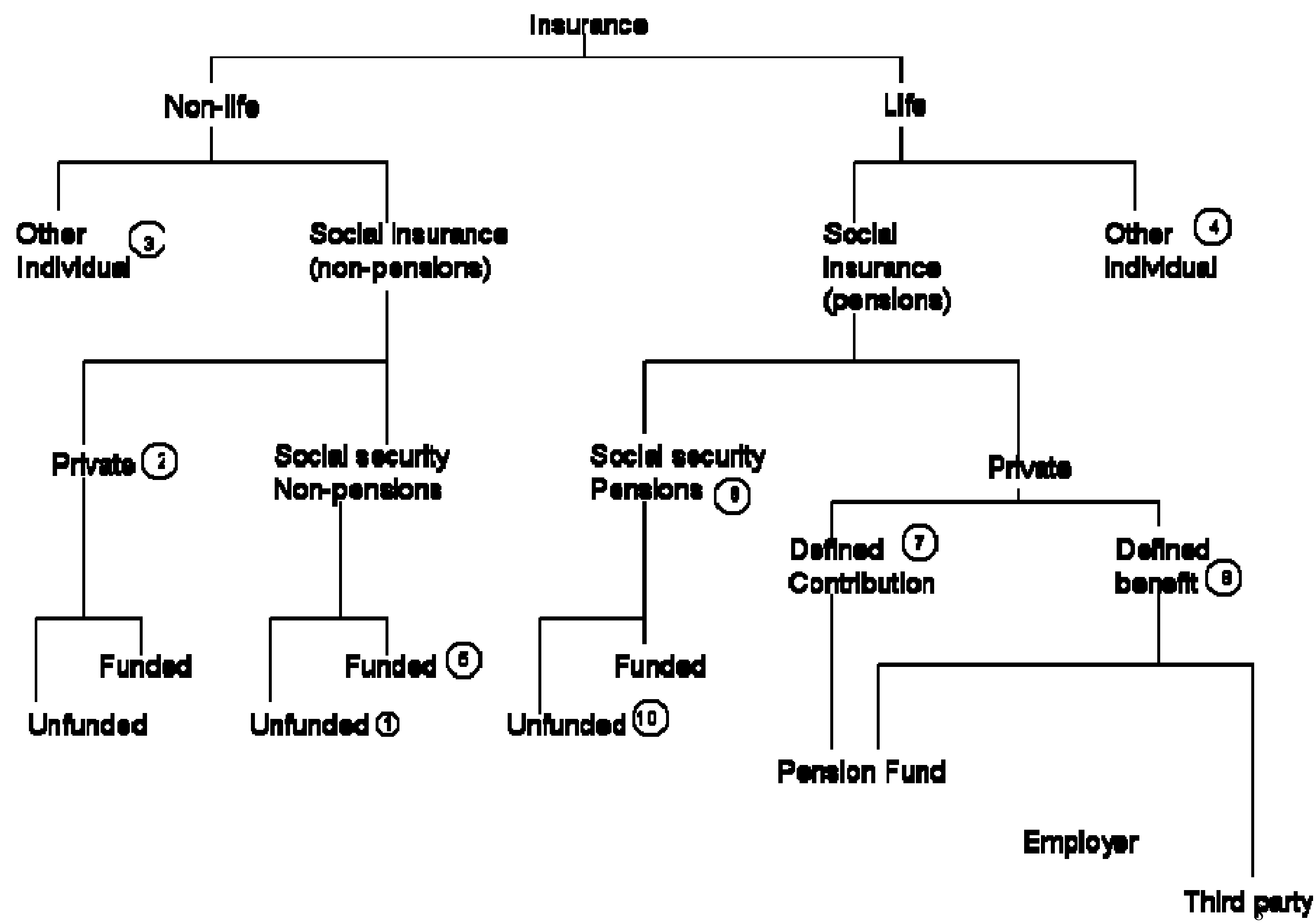
All of these are significant. We spent time and effort sorting out the first at the meeting in Paris. I have prepared a diagram in response to the second issue (discussed below). We should discuss how to approach the other two items given the time constraints we face.

Diagram

A number of people suggested introducing an updated version of figure A.IV.1 in annex IV. I have no problem with this and suggest the figure on the next page (8). It is similar to that in the SNA but as well as incorporating changes to show pension liabilities, I have inserted numbers in circles that show the relevant table number for that entry . (Table 9 does not belong in this sequence hence there is no entry for 9 in this figure.)

UNSD have suggested repeatedly that the figure could be simplified along the lines of the figure on page 9. As many times as they suggest it, I point out that while simpler, it is unfortunately not accurate. We cannot ignore the fact that especially in the US but increasingly in other countries, individual policies may count as social insurance policies. This means there are links indicated by arrows on page 10 that upset the simple picture. Furthermore, since there are significant differences between life and non-life insurance and, in parallel, between pensions and other social benefits, I think a figure that highlights this difference first and then distinguishes between social insurance and other direct insurance rather than vice versa is more satisfactory for the reader. We could also change the order of the text but that would move farther away from the 1993 annex and require some time.

Question: What are the ISWGNA views on a figure on insurance schemes?


Insurance
Non-life
Life
Other Individual 3
Social Insurance (non-pensions)
Social Insurance (pensions)
Other Individual 4
Private 2
Social security Non-pensions
Social security Pensions 9
Private
Defined Contribution 7
Defined benefit 8
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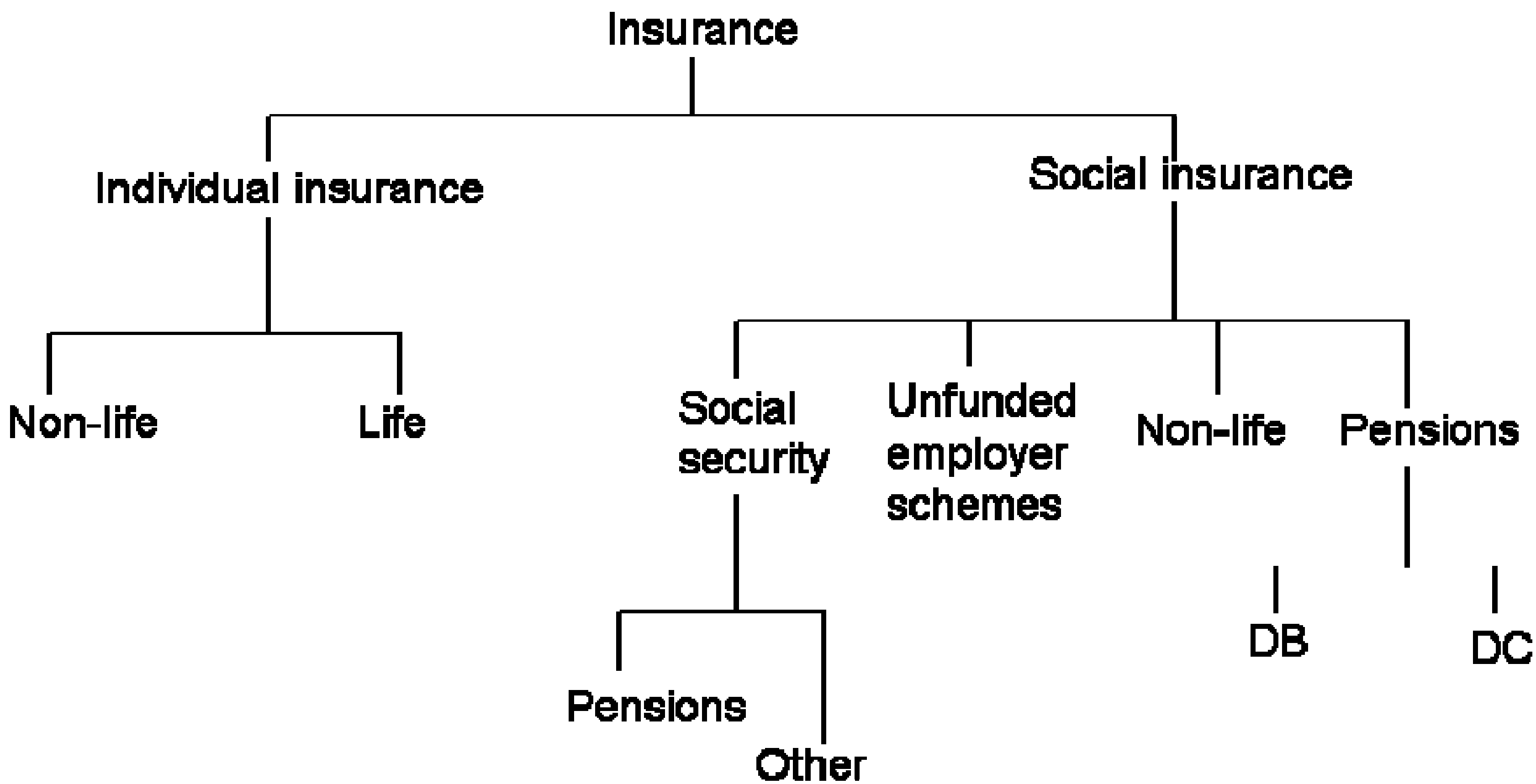
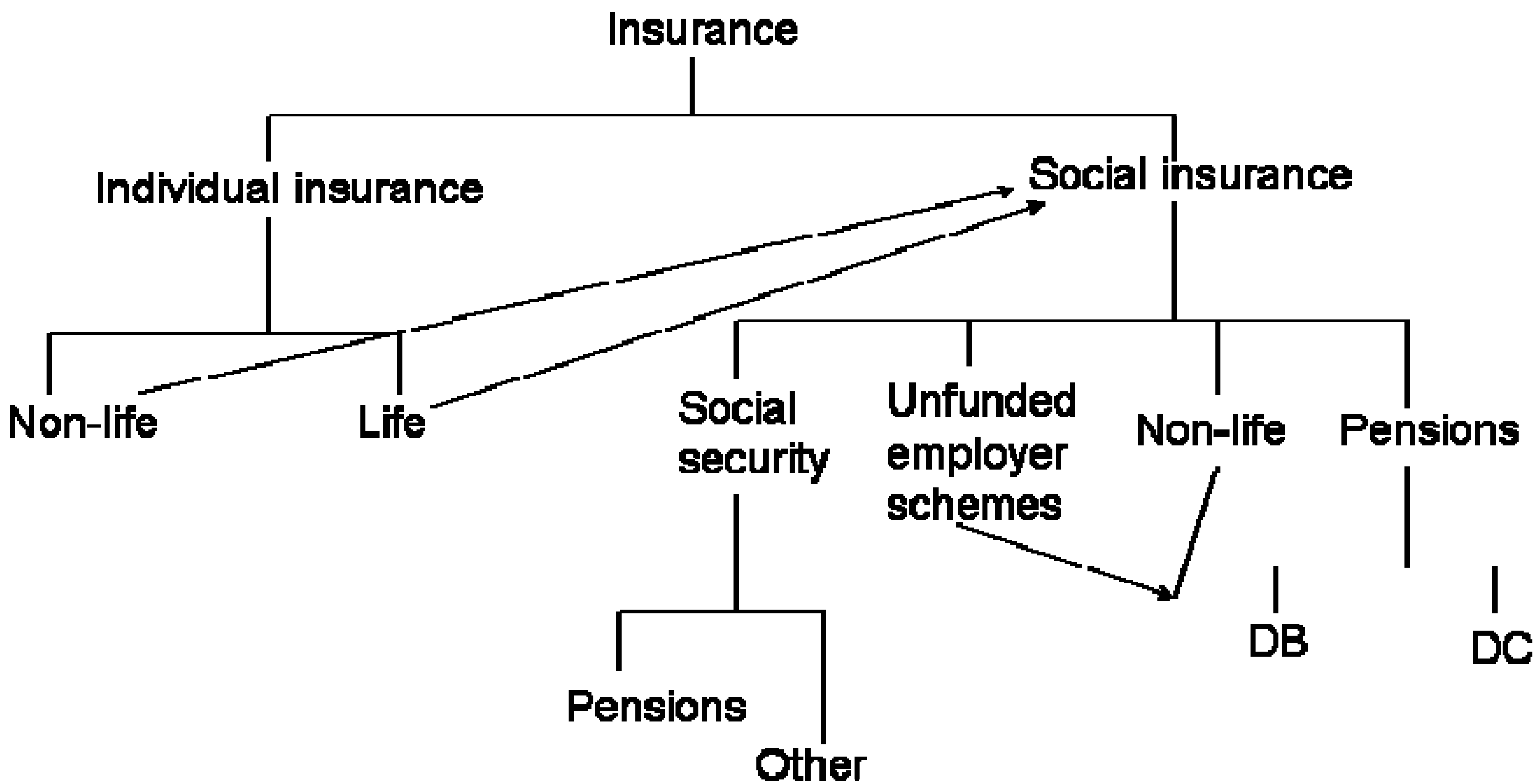
Unfunded
Funded 5
Unfunded 1
Funded
Unfunded 10
Pension Fund
Employer
Third party


Insurance
Individual insurance
Social insurance
Non-life
Life
Social security
Unfunded employer schemes
Non-life
Pensions
Pensions
Other
DB
DC


Insurance
Individual insurance
Social insurance
Non-life
Life
Social security
Unfunded employer schemes
Non-life
Pensions
Pensions
Other
DB
DC

Tables

There are six tables in annex IV of the 1993 SNA. Together they are consistent with the main set of tables running through the volume. For chapter 17 I took these tables and converted them to eight tables that together are still consistent with the main set of tables. Table 17.9 gives some idea of the effort involved in incorporating the extra detail. The format of the tables is still that of those in the 1993 SNA; only transactions most relevant to understanding the means of recording each type of insurance are shown. (In fact these tables cover both insurance and pensions).

UNSD sent some very detailed comments (attached). Essentially they suggest reworking all the tables to include a full set of transactions and to show what an insurance company's accounts might look like also. This would be a considerable task. To my mind there is a very good case for having a much longer document prepared at some time in the future on insurance. This could be either an electronic annex to be appended at some time (not necessarily seen as part of the second deliverable) or could be a free-standing handbook. It could go into much greater detail on many of the issues and could include tables such as UNSD suggests.

Question: How would the ISWGNA like to approach the question of the tables in chapter 17?

The next three pages show the relevant UNSD comments. The remarks in para 12 are correct and helpful. It is the following suggestions that are for discussion.

12. The example in table 17.2 needs a production account if the guidelines of par 17.69 and 17.71 (1) is accepted. Employers' imputed contribution should then be more than 9.0 to include the service charge. Let us assume that output/cost is 1.0, then imputed contribution is 10 and **net** contribution is 9.0. 1.0 will be also treated as final consumption expenditure. However, this guideline may be too data-demanding to implement. The cost of operating unfunded schemes can be treated merely as intermediate consumption by the producers, which is similar to the treatment of social security.

13. Table 17.3: When the actual flows of receipts and expenses by the non-life insurance company is analyzed, the totals do not balance as shown below.

Actual receipts and expenses of the non-life insurance company (based on table 17.3)

USES		**RESOURCES**		
Claims	45	Total premiums	51	
		Premiums	45	
		Service charges (output)		6
		Property income		6
Cost + profit (=output of insurance)	6			
Increase in technical provision	3			
Total	**54**	Total		**57**

(a) The increase in technical provision should be 6 instead of 3.Claims must be recorded as paid by the insurance companies and not by households as shown in the table.
Too many values are the same (equal to 6). It is better use different values for different variables.

(b) It is suggested that a simplified business account on receipts and expenses of an insurance company, similar to the one presented above, be presented for all tables so that readers can understand what additional imputations are needed in order to record the flows according to the SNA.

(c) It is suggested that when an example is given, the recording of all related and essential transactions should be shown. The editor may choose to deliberately skip some transactions but it is confusing to the readers when it is done

14. Table 17.7 is understandable, although I suggest that the actual receipts and expenses of the pension funds be described before the recording is described so that readers can easily understand it. The figures in table 17.7 are shown in the example of business accountants below. In this case, actual receipts and expenses are balanced.

Actual receipts and expenses of a defined contribution scheme **(based on table 17.7)**

Expenses		Receipts	
Cost + profit (=output of insurance)	**1.4**		
		Property income	3
Benefits	26	Contribution	25.5
		Employers' actual contribution	14.0
		Employees' actual contribution	11.5
Change in pension entitlement	1.1		

Total	**28.5**	Total	**28.5**

Given the information, the recording in table 17.7 can be improved as follows:: (a) Compensation of employees' actual contribution, (11.5), are produced somewhere in the economy and must be shown in the table; (b) The saving of the pension fund **must zero (output is equal to cost of operating the fund (assume all it is COE)**

Below is the SNA recording in table 17.7 may be as follows, the financial accounts shows the treatment of net contribution and benefits:

Table 17.7

		Business		Pension funds		Households	
		U	R	U	R	U	R
Output					1.4		
Value added	Compensation of employee	14+10.1		1.4			
	Employers' contributions	14					
Primary							
D1	Compensation of employees						25.5
D122	*Employers' contributions*						*14*
D41, D42	Property income	3			3		
D44	*Property income attributable to insurance policy holders*			3			3
Secondary							
D61	*HH net contributions*				27.1	27.1	
D6112	*Employers' contributions*				14	14	
D6121	*Employees' net contribution*				11.5+3-1.4	11.5+3-1.4	
D62	Pension benefits			26			26
D8	*Pension entitlements*			1.1			1.1
	Final consumption					1.4	
B8g	**Saving**	**-27.1**		**0.0**		**27.1**	
Financial accounts							
Currency				+27.1 - 26		-27.1 +26	
Pension entitlement					**+27.1 -26**	**+27.1 -26**	

15. Table 17.8 is very difficult to understand and the paras from 17.161-17.166 are not very helpful. Besides, from my own verification, table 17.8 also needs review. Below, I put the numbers into the actual flow of receipts and expenses for the pension fund first in order to have the equality of the total of expenses and the total of receipts. The actual change in pension entitlement (shown by the editor to be -4.5) should be -2.9. See below.

Actual receipts and expenses of a defined contribution scheme (based on table 17.8) WITHOUT IMPUTATION

Expenses		Receipts	
Cost + profit (=output of insurance)	**0.6**		
		Property income	2.2
Benefits	16	Contribution	11.5
		Employers' actual contri.	10.0
		Employees' actual contri.	1.5
Change in pension entitlement	-2.9		
Total	**13.7**	Total	**13.7**
		Actual should be -2.9, not -4.5 as in table 17.8 as this can be calculated by deducting benefits and output from the total on the right hand side	

Given this basic data, imputations can then be added (similar to the way Francois Lequiller did in his AEG paper on non-life and pension funds), but in a way that there is a balance between receipts and expenses. If additional imputed contribution must be made then imputed change in pension entitlement must be introduced (which is in addition to the actual pension entitlement kept by the insurance company). Given imputed pension supplement is 4 as done by the editor, the imputed change in pension entitlement can be calculated as shown in the table below.

Actual receipts and expenses of a defined contribution scheme (based on table 17.8) WITH IMPUTATION

Expenses		Receipts	
Cost + profit (=output of insurance)	**0.6**		
		Property income	2.2
Benefits	16	Contribution	19.6
		Employers' actual contri.	10.0
		Employers' imputed contri.	4.1
		Employees' actual contri.	1.5
		Imputed pension supplement	4
Change in pension entitlement	5.2		
Actual	-2.9		
Imputed	8.1		
Total	**21.8**	Total	**21.8**

As currently presented, it is not possible to figure out the sequence of assumptions.

Annuities

I had originally intended to include an example on annuities and then for a number of reasons, including pressure of time, did not. Several commentators said an example would be helpful and in particular Viet suggested this would be helpful. I entered into discussion with Viet (attached) which is incomplete because, as you will note from the date, at that time I was concentrating more on moving than on annuities. However, you will see that the subject is not altogether easy.

I would suggest there are a number of choices open to us.

1. We could simply abandon the section on annuities and leave to it to any later longer document as suggested above.

2. We could amend the text in the light of comments but not try to include an example

3. Someone could volunteer to take forward the work Viet and I began and this could be included in the fixed up text.

Question: What is the ISWGNA view?

From:	Viet Vu
To:	HARRISON Anne, STD/NAFS;
CC:	havinga@un.org;
Subject:	RE: Comment on annuities
Date:	Friday, August 17, 2007 7:44:48 PM
Attachments:	Viet.xls

Dear Anne,
Thanks for your example. Your example do help me understand the problem and also enable me to suggest a solution. I have played around with your example which I attach below to come up with the solution.

1. You assume that the financial company wants to charge 90 for its output. The company may have to do the analysis the way you present in the first 5 columns. Given that, it comes up with the base-line actuarial reserve shown in column E.
2. I take that actuarial reserve as given,
Output can be calculated from the first 5 columns:
  Output = Premiums + premium supplement - claims - change in the acturarial reserves.
Premiums in the case of annuities is always zero. Premium supplement is actual interest. Change in the acturarial reserves is change in the base-line acturarial reserve.
2. If I use the same information in the your example, I must be able to derive the output of 90.
3. But in reality, actual interest may be different. Let us say that interest rate in period 2 is 7%, then the same formula in (2) still applies. Output in period 2 is now 286, not 90. The higher output is explained by a higher interest received.
4. The last thing is the output of the last period. 1545 can only be understood as bonus paid back to the annuitant.
This proposal would provide different output for different period and output is based solely on the data provided by the company. Here I assume that the company must have an actuarial reserve.
Please react.
Viet
(See attached file: Viet.xls)

<Anne.HARRISON@oe
cd.org>
To
17/08/2007 02:09 <vuv@un.org>
AM cc
<havinga@un.org>
Subject
RE: Comment on annuities

Dear Viet,
Thank you for your comment. It is perhaps useful to discuss this before your comments are posted. If you would like to take this futher and develop a numerical example, this could indeed be helpful.
Part of the problem with your example is that five years is too short to show realistic figures. Typically in UK at present, for example, a paymen tof 10,000 buys you 600 a year for life, or, let us us say, 25 years. The NPV of 600 a year at 5% assuming 25 years payments is 8693. 10000 represents the npv of a value of about 690 a year (10000/8693*600) which means the insurance company expects a premium of 90 a year for 25 years.
The attached spread sheet shows in the first column the NPV of 600. Next four columns show how 10000 declines over 25 years assuming 5 % interest and withdrawals of 690. Next four columns show how th enpv of 8693 declines with 5% interest and withdrawals of 600 per year. Last four columns show the differnce between the previous sets of four columns. This shows us the premium of 90 plus the premium supplement, the differnce between the opportunity cost on the differnce between the 10000 and the 8693. This is what it costs the annuitant. If the insurance company makes more or less, then their disposable income will be affected.
The whole is dramatically affected by how long the annuitant actually lives. If he only lives for 20 years, the implied premium is much higher; if he actually lives for 30, it is correspondingly lower.
I agree a numerical example would be useful. Is my explanation and this (hasty) example helpful to your understanding?
Bwst wishes,
Anne

-----Original Message-----
From: Viet Vu [mailto:vuv@un.org]
Sent: Mon 8/13/2007 4:27 PM
To: HARRISON Anne, STD/NAFS
Subject: Comment on annuities

Dear Anne,

Para. 17.74 on annuities of the previous draft of Chapter 17 has a promise as follows:

"An example of these flows is shown in table??
Table ??? here"

The new draft does not include the example.

I have tried to read the part on annuities in the new draft but see problem. I would like to consult with you before I put it as UNSD comments. I don't yet have an answer on the treatment, but I believe that there is a standard in business accounting for recording that we can follow. Unfortunately I do not have any book which is devoted excluvisely on accounting for the insurance industry. I think that you or someone else may need to look further in this area.

Below is my draft comment.

Viet

I will use the example to show a serious problem with the treatment of annuities proposed in chapter 17.

The section in chapter 17 is currently written from an analytical point of view and from the point of view of the insurance company (the debtor point of view). But the analysis can be done from either the creditor (the annuitant) or the debtor's point of view, because we have two sectors that are in transactions.

Let us say that the insurance company has to pay out to the annuitant \$1000 in each of the five periods and the discount rate that it uses 5%. The present value of these payments is \$4329.48

(Embedded image moved to file: pic57204.jpg)

In this case, the insurance company will engage in business only if the annuitant is willing to pay in premium of at least \$4329.48. Its liability in present value to the annuitant is \$4329.48. The size of his output will be dependent on:

§ how much the annuitant is willing to pay in premiums

§ the ability to obtain an interest rate that will exceed the discount rate used to calculate the present value of his liability.

As in any analytical model, where information is perfectly symmetric in the sense that the annuitant also knows exactly the same information as the insurance company, such that the annuitant is willing to pay only a premium of $4329.48, and therefore in such as case no output can be calculated or assumed. In this case, premium is equal to the present value of all claims over the contract period and at the first period, for the insurance company, assets (money received from the annuitant as premiums) must be equal to its liability to the annuitant (equal to the present value of the future stream of payments).

However, a correct treatment of annuity should be based on actual book keeping of the insurance corporations, not on hyphothesis. Let us assume that the payment of premium at period 1 is $4329.48. The company then invested this amount and received in the first period an actual interest of $216 (=4328x0.05) - this must be the actual interest received, if the company received a higher value then that must be used instead. The recording is as follows:

§ $4329.48 is recorded as both asset (money received) and liability of the insurance company.

§ The formula of output: premiums earned + premium supplement - claims,

§ So for the first period

Output of the first period = ?? + 216 - 1000

Premium earned for each period is an issue that is not discussed in the text, but let us assume that it is calculated by spreading it evenly over 5 periods, then premium earned for each period=$4329.48/5=865.9

Output of the first period = 865.9 + 216 - 1000 =81.9

If one continues with this calculation, assuming that interest rate does not change over time, then total output over 5 periods is negative, which means that the simple assumption of spreading premiums over 5 periods is not correct, as one would expect the total output to be zero. Thus there are problems we need to look at, but it can be said that the SNA should record actual transactions, not hypothetical transactions as done in the current text.

	Start year	interest	withdrawa	End of yr	Start year	Interest	Withdrawa	End of year				
600	10000	500	690	9810	8693	435	600	8528	1307	65	90	1282
571	9810	491	690	9611	8528	426	600	8354	1282	64	90	1256
544	9611	481	690	9401	8354	418	600	8172	1256	63	90	1229
518	9401	470	690	9181	8172	409	600	7980	1229	61	90	1201
494	9181	459	690	8950	7980	399	600	7780	1201	60	90	1171
470	8950	448	690	8708	7780	389	600	7568	1171	59	90	1139
448	8708	435	690	8453	7568	378	600	7347	1139	57	90	1106
426	8453	423	690	8186	7347	367	600	7114	1106	55	90	1071
406	8186	409	690	7905	7114	356	600	6870	1071	54	90	1035
387	7905	395	690	7610	6870	343	600	6613	1035	52	90	997
368	7610	381	690	7301	6613	331	600	6344	997	50	90	957
351	7301	365	690	6976	6344	317	600	6061	957	48	90	914
334	6976	349	690	6635	6061	303	600	5764	914	46	90	870
318	6635	332	690	6276	5764	288	600	5453	870	44	90	824
303	6276	314	690	5900	5453	273	600	5125	824	41	90	775
289	5900	295	690	5505	5125	256	600	4782	775	39	90	724
275	5505	275	690	5090	4782	239	600	4421	724	36	90	670
262	5090	255	690	4655	4421	221	600	4042	670	33	90	613
249	4655	233	690	4198	4042	202	600	3644	613	31	90	554
237	4198	210	690	3717	3644	182	600	3226	554	28	90	492
226	3717	186	690	3213	3226	161	600	2787	492	25	90	426
215	3213	161	690	2684	2787	139	600	2327	426	21	90	357
205	2684	134	690	2128	2327	116	600	1843	357	18	90	285
195	2128	106	690	1545	1843	92	600	1335	285	14	90	210
8693												

Anne’s example

First column simply calculates NPV of 600 a year for 25 years at %% discount.

Next four show interest earned at 5% and deduction of 690 a year. Next two sets of four columns show the calculations for the pension of 600 and premium of 90 separately.

Viet's example

Output	Interest	withdrawal	Change in actuarial reserve	Actuarial reserve
				10000
90	500	600	-190	9810
286	687	600	-200	9611
90	481	600	-209	9401
90	470	600	-220	9181
90	459	600	-231	8950
90	448	600	-242	8708
90	435	600	-255	8453
90	423	600	-267	8186
90	409	600	-281	7905
90	395	600	-295	7610
90	381	600	-309	7301
90	365	600	-325	6976
90	349	600	-341	6635
90	332	600	-358	6276
90	314	600	-376	5900
90	295	600	-395	5505
90	275	600	-415	5090
90	255	600	-435	4655
90	233	600	-457	4198
90	210	600	-480	3717
90	186	600	-504	3213
90	161	600	-529	2684
90	134	600	-556	2128
90	106	600	-584	1545

Chapter 17.2: Standardised guarantees

1 issue: Expected calls

Expected calls

The ECB asks if, given the parallels with non-life insurance, there should be a concept of "adjusted (expected) calls" used for standardized guarantees similar to adjusted claims in insurance. My response would be that perhaps, technically this might be appropriate but that standardised guarantees are by their nature such that exceptional levels of calls are totally unlikely, this is an unnecessary refinement.

Question : What is the ISWGNA's view?

Chapter 17.3 Pensions

5 Issues: Tables

Consistency with chapter 7

Defined contribution payouts

ABO/PBO

Segregated (largely) unfunded schemes

Pensions is a difficult area in that the joint ECB/Eurostat task force is still working and will not come to a conclusion until early 2008. It is clear, though , that if there are significant differences between their conclusions and the text in chapter 17, these are likely to be raised at the SC. I think we need to think about how to deal with any differences that emerge even though they are beyond the 60 day comment period.

Tables

There is a mistake in table 10 that will be sorted out.

Table 11 is based on the task force recommendation for the compromise supplementary table. I suggest we leave this as it is but plan already to have a cover note saying this is due to timing and will be brought into line with their final recommendation.

Consistency with chapter 7

They certainly should be consistent and I will check they are.

Defined contribution payouts

This is a difficult conceptual issue. One point of social insurance is to give participants income in retirement not just run-down of savings. For individual life insurance policies the benefits are payable as run-down of savings in the financial account. The payout on a defined contribution pension scheme is usually in the form of an annuity. This comes back to the way in which annuities are recorded in the system and the section on annuities. However, supposing we are agreed on the fundamental principle, an annuity is a capital sum held by the insurance company on behalf of the individual. Each year they receive property income on the outstanding balance and a further sum that is recorded as a run down of capital in the financial account.

If we do the same for payouts under a defined contribution pension scheme, two consequences follow. The first is that at the moment of retirement, the individual receives a large capital sum. Although this is immediately re-invested, household saving will increase by this amount. Is this acceptable or do we want to avoid the receipt and payment and simply assume the capital built up in a pension scheme is transferred to an annuity balance? On the whole I think we probably do and some minor editing will be required.

The second problem is the following. As contributions to a defined benefit pension scheme build up, the whole increase in value is recorded as income. The increase in value due to the unwinding of the discount factor is recorded in full even though some of it may be paid for by holding gains. For a defined contribution pension scheme, that part of the increase in value due to holding gains and losses is NOT recorded as income. The income part of a defined benefit pension scheme is thus higher than for a defined contribution pension scheme during the contribution phase. The payment from a defined benefit pension scheme is recorded entirely as income. However, if we record the payment from a defined contribution pension scheme according to the annuity principle, some part is income and some part is a run down of capital. This is therefore symmetric with the difference in build-up of income but is it acceptable? If not what alternative is there?

ABO/PBO

This is an are exercising the task force. There is pressure from some members to show the impact of promotions as a transaction not a change in volume. I do not think this is consistent with either SNA accrual principles or IASB guidance. We need to keep in touch on this, though, and again be prepared to cover any difference in the cover note to the SC.

I gather the task force is still not convinced of the cohort argument in chapter 17 and has the impression that there are sudden surges in liabilities when promotions occur. (This is behind some of the pressure to record promotions as transactions.)

There has also been some discussion about whether there needs to be price inflation allowances built into the liabilities. I have sent an initial reply that if price inflation is built in, discounting is done at nominal rates and if no inflation is built in discounting is at real rates so the results are much the same. I am not sure of the reaction to this but Reimund is in town this week for BOPCOM and I expect to talk with him about this and other matters arising and will update the group verbally.

There is a further meeting of the task force in December leading up to the report due to go to CMFB in January. Obviously I will not be able to go, though invited, but I think it important that the "SNA" position be well represented and I wonder whether some combination of Charlie, Gallo and Christian could take over the role of liaison with the task force and alert us to any remaining differences?

Segregated (largely) unfunded schemes

This is a difficult conceptual issue also. As written, the text assumes two likely scenarios for funding defined benefit pension schemes. One is that the employer retains full responsibility for the scheme (is the sponsor of the scheme). This covers the case where the scheme is actually unfunded. For these schemes, whether there is any actual funding or not, the employer is always responsible for any shortfall in provision. He must make implicit contributions sufficient to cover both the current service element (in compensation of employees) and the increase in the past service element (in property income).

The second alternative is that the employer passes responsibility for the scheme to another unit who becomes the scheme's sponsor. Such schemes are funded. The current service element is paid by the employer to the employee who then passes it on to the fund. The fund is responsible for the property income element. It pays the full amount and hopes to cover costs by making holding gains . Any shortfall of the fund may be payable from the employer to the fund or any surplus payable from the fund to the employer. (Whether such payments are due depends on the nature of the agreement between the employer and the fund.) The text says any such payment is recorded is a financial account transaction.

What is not covered is a variant whereby there is a sponsor other than the employer but the scheme is significantly under-funded. Why would a fund agree to such a situation? In the case where it is a government fund. An example is where the employees' contributions are paid to the fund who invests them to help meet benefits but the government pay for any shortfall on a pay as you go basis. Under the proposal to record liabilities in full, should we show the government as liable to cover not only the current service element but also the part of the past service element arising from their contributions as property income due to the fund?

An earlier proposal had an imputed property income flow from the employer to the fund for all the property income due to the beneficiaries except the property income earned by the fund excluding holding gains and losses. The part that was not then due because of holding gains and losses was to be shown as "reimbursed" in the financial account. Where the fund is able to cover all the property income due to the beneficiaries from property income and holding gains and losses, this procedure has a current account payable by employer that is cancelled in the financial account, either mostly or to excess. I think this is not consistent with the way in which we record normal insurance and is particularly unfortunate if the employer is government but the scheme is funded since the outgoing property income shown as payable will affect government saving unnecessarily.

I have thought about including a property income payment from the employer to the fund based on the outstanding liability of the employer to the fund. In the normal course of events, though, even a well run fully funded scheme will show relatively small surpluses or deficits due to or from the employer most years. There is little reason to impute a property income flow on these and a reverse flow, from the fund to the employer is implausible.

I think a better solution might be to suggest partitioning the fund and to treat the part that does receive actual contributions as segregated with a separate sponsor and the part that does not as not segregated and the responsibility of the employer. What does the ISWGNA recommend?

Chapter 17.4: Financial services

1 issue: Location in the book

There are many comments of an editorial nature. In particular there are very many comments from the ECB and from the financial institutions section of the IMF. I suggest I should talk to the people involved in both institutions on a bilateral basis.

Both however, question why this material appears in chapter 17 and not in chapter 11. I feel rather strongly that it is important to show the reader how transactions relating to financial instruments appear in chapters 6, 7 and 11, other flows in 12 and stocks in 13 in one place. To force all of this into chapter 11 would (i) misplace information belonging elsewhere, (ii) not be helpful to someone looking or further information on interest flows, for instance, in the distribution of primary income account. Does the ISWGNA agree?

Chapter 17.5: Contracts, leases and licences

1 Issue: Mobile phone licences

The News and Notes article on the appropriate treatment of mobile phone licences was negotiated long and hard by the ISWGNA with considerable word-smithing to get agreed wording. I have therefore taken the view that it has the status of 1993 SNA “text”. There have also been calls to include the agreed treatment in the update and in a couple of cases the recommendation on other assets is to follow the mobile phone guidance. . I therefore included the text pretty much as is. However, some comments suggest this should be significantly reduced. Is this the view of the ISWGNA?

1. Output of the central bank

6.1 Before discussing financial services more generally, it is helpful to discuss the output of the central bank. There are three broad groups of central banks services. These are monetary policy services, financial intermediation and borderline cases. Monetary policy services are collective in nature, serving the community as a whole, and thus represent non-market output. Financial intermediation services are individual in nature and in the absence of policy intervention in the interest rates charged by the central banks, would be treated as market production. The borderline cases, such as supervisory services may be classified as market or non-market services depending on whether explicit fees are charged that are sufficient to cover the costs of providing the services.

6.2 In principle, a distinction should be made between market and non-market output but in practice the possible resource intensiveness of the exercise and the relative importance of making the distinction should be considered before implementing the conceptual recommendations.

Borderline cases such as supervisory services

6.3 Central banks frequently provide supervisory services overseeing the financial corporations. One could argue that this is for the benefit of society in general and the national accounts should record them as government final consumption. In support of this view, one could draw a parallel with government performing market regulation policies, which it also may entrust to a specialized agency, or to government providing for roads, dams and bridges. From this view, surveillance services are collective services and should be recorded as government consumption expenditure.

6.4 However, one could also argue that government's regulatory services are to the benefit of the financial intermediaries, because these services contribute to the functioning and financial performance of these institutions. From this perspective, they are comparable to regulatory services of government such as quality control on food and drugs, which the national accounts record as intermediate consumption of producers. The fact that financial intermediaries pay a fee for these services in some countries (for example in a number of countries in Latin America) supports this view. Following this reasoning, surveillance services are not collective services but should be recorded as intermediate consumption of financial intermediaries. However, even if the view is taken that supervisory services are market output because a fee is charged, if the fees are not sufficient to cover the supervisory costs incurred by the bank, then the services should be treated as non-market output and part of government consumption expenditure.

Provision of non-market output

6.5 As long as it can be identified as a separate institutional unit, the central bank is always included in the financial institutions sector and never in general government. The collective consumption represented by monetary policy services is recorded as expenditure by general government but government does not incur the costs incurred by the central bank. Therefore a current transfer of the value of the non-market output should be recorded as payable by the central bank and receivable by the general government to cover the purchase of the non-market output of the central bank by government.

Provision of market output

6.6 If the financial intermediation services provided by the central bank are significant, and if it is possible and worthwhile to compile data for a separate establishment providing them, these services should be shown as payable by the units to whom they are delivered. Supervisory services treated as market output are recorded similarly.

Further addendum to chapter 7

The following paragraph appears at present in chapter 6 9as para 6.147).

6.7 If the interest rates charged by the central bank are artificially high or low because of policy intervention , the excess over the reference rate should be treated as a tax or a subsidy as appropriate collected (paid) by the central bank on behalf of government and thus shown directly in the accounts for general government under the heading of other taxes (subsidies) on production.

Comments requested further elaboration. Drawing on the IMF discussion paper, and discussion with two of the authors, suggests removing that short para from chapter 6 and adding a rather longer section to the addendum to chapter 7 since the question is not one of the measurement of output but of the way in which interest flows are partitioned and re-routed.

1. Interest rates set by the central bank

6.8 The central bank's main responsibility is to formulate and carry out part of economic policy. It therefore often acts differently than other financial corporations and generally has received the authority from government to enforce its views. It is therefore appropriate that, in cases where the central bank uses its special powers to oblige market participants to pay transfers without direct *quid pro quo*, to record the proceeds as implicit taxes. Conversely, in cases when the central bank makes payments that are clearly for policy rather than commercial purposes, it may be argued that implicit subsidies are paid. Three cases are considered:

(i) the central bank is able to dictate below market rates for reserve deposits;

(ii) the central bank pays above market rates in a situation where the external value of the currency is under pressure;

(iii) the central bank acts as a development bank offering loans at below market rates to priority industries.

6.9 If the interest rates are determined for policy reasons and not by commercial forces, then the difference between flows calculated using the reference rate and the actual rate set by the central bank should be recorded not as market output, specifically FISIM, but as implicit taxes and subsidies as described immediately below. This procedure is analogous to and consistent with the practice of treating the difference between the market exchange rate and an alternative exchange rate imposed by the central bank as an implicit tax or subsidy. (cross-ref)

Below market rates on reserve deposits

6.10 Suppose the central bank pays only three per cent to a commercial bank on reserve deposits when the market rate is five percent. The following recording is made in the System:

i. Although the commercial bank actually receives only three percent as "interest", it is recorded as receiving five per cent as interest and paying two per cent to government as a tax on production;

ii. Government is recorded as receiving two per cent from the commercial bank as a tax on production and as making a payment of a current transfer of two percent to the central bank (both these flows are notional);

iii. The central bank actually pays three per cent from the commercial bank but is recorded as paying five per cent to the commercial bank and receiving two per cent from government in the form of a current transfer.

No financial account transactions are involved with this re-routing.

Above market rates for currency support

6.11 Suppose the central bank pays seven per cent to a commercial bank for a limited period when the currency is under pressure at a time when the market rate is five percent. The following recording is made in the System:

i. Although the commercial bank actually receives seven percent as “interest”, it is recorded as receiving five per cent as interest and receiving another two per cent from government as a subsidy on production;

ii. Government is recorded as paying two per cent to the commercial bank as a subsidy on production and as receiving of a current transfer of two percent from the central bank (both these flows are notional);

iii. The central bank actually pays seven per cent to the commercial bank but is recorded as paying five per cent to the commercial bank and paying two per cent to government in the form of a current transfer.

No financial account transactions are involved with this re-routing.

Below market rates to priority industries

6.12 Suppose the central bank charges only three per cent to a priority industry when the market rate is five percent. The following recording is made in the System:

i. Although the priority industry actually pays only three percent as “interest”, it is recorded as paying five per cent as interest but receiving two per cent from government as a subsidy on production;

ii. Government is recorded as paying two per cent to the priority industry as a subsidy on production and as receiving of a current transfer of two percent from the central bank (both these flows are notional);

iii. The central bank actually receives three per cent to the priority industry but is recorded as receiving five per cent from the priority industry and paying two per cent to government in the form of a current transfer.

No financial account transactions are involved with this re-routing.