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Director

STATISTICS DEPARTMENT

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Mr. Ivo Havinga
Chief of the Economic Statistics Branch,
United Nations Statistics Division,
New York,
USA.

SUBJECT: Comments On EAG and Provisional Recommendations

Dear Mr. Havinga,

This is in reference to IMF letter of June 12, 2006, addressed to Governor, State Bank of Pakistan, seeking comments on EAG recommendations made in the Frankfurt meeting and full set of the provisional recommendations for updating of SNA 93. Our views on some of the issues are as under:

Issue: Contract Leases and licenses:

Financial & Operating leases need different treatment due to difference in concepts and nature of the two types of leases. Operating lease is a contract in which lessee have the rights to use an asset for a very short period of time where maintenance of the assets is the responsibility of the leaser. The depreciation and maintenance cost is charged to the profit and loss account. The ownership remains with the leaser and the leased amount received by the leaser is credited in the profit and loss account.

On the other hand, financial lease has a different concept and treatment. The asset is transferred to the lessee along with all its rights, rewards and risks. The lessee pays its rental to the leaser, which covers cost of the asset along with interest. The leaser credits its income account with the interest earned on the lease. The value of the asset and its depreciation charges are reflected in the books of the lessee and its maintenance is also the responsibility of the lessee. The value of the asset is transferred to the lessee account with the repayment proportion and at the end of the lease contract the ownership is transferred to the lessee

So, there is a strong reason to distinguish between financial and operating leases without depending on the production activity in which it was used. The break down between repayment of interest and principal should be made in case of financial lease only as interest paid on lease is charged to the financial account and the principal amount paid is to be recorded in the leased asset account. In case of operating lease, the breakdown of principal and interest amounts would not be meaningful.

Leases are for a specific period and for a limited economic life, so lease of an asset having unlimited life should be treated as resource lease rather than financial or operating Lease

Issue: Contract and Lease: Government Permits

When government issues licenses to undertake some specific activity by using its sovereign powers and are issued on some restricted bases, if the concerned asset is returned and non-utilized amount is received from the government, it should be treated as sale of an asset. If the asset is not returned to the government then receipt should be treated as tax.

Issue: Non-performing loans

The issue related to treatment of interest associated with non-performing loan when it is written off. The recording of loan along with interest on accrual basis is a consistent decision.

Issue: Classification and Terminology of assets

The following sub-categories are suggested under "Inventories" in the proposed revised classification of non-financial assets.

Inventories

- Stores and Spares (suggested category)
- Material & supplies
- Raw material (suggested category)
- Work in progress
 - WIP on cultivated assets
 - Other work in progress
- Finished Goods
- Military inventories
- Goods held for resale (for trading concern)

Issue: Equity

To value the shares of an unquoted corporation, it is suggested that the valuation should be based on net worth of the corporation and it should be raised by average percentage of dividend paid during the recent last 3 years.

General comments:

The recommendations made by Advisory Expert Group on balance of payment issues focus on strengthening the SNA to capture the key features of globalization and ensuring harmony with the updated Balance of Payment manual. A number of recommendations are made on issues concerning non-financial assets would harmonize SNA with the Handbook on National Accounting, Integrated Environmental, Economic Accounting and other developments in the economy and methodological advances. Recommendations

made on issues concerning financial instruments would cover the new developments in financial markets and instruments.

The proposal for the revision of SNA 1993 covers 44 issues, most of which would relate to countries which have or who are in process of complete implementation of SNA 1993. Since Pakistan is in the process of partial implementing the SNA 1993, the issues related to various components of SNA 93 cannot be anticipated at this stage. Further, comments on several issues/recommendations have already been communicated through our previous communications on the subject.

Yours sincerely,



(Dr. Azizullah Khattak)
Director