SNA 2008 changes

December 2013

Content

- Background to the update
- Financial services and financial accounts
- Capital issues
- Public administration
- Others

1. Background to the update to ESA 2010

- In 2003 the **UN Statistical Commission** (UNSC) called for an update of the SNA 1993 to « *bring the accounts in line with the new economic environment, advances in methodological research, and needs for users* »
- The Inter Secretariat Working Group on National Accounts (**ISWGNA**) comprising Eurostat, IMF, OECD, UN and World Bank was mandated to co-ordinate and manage the update project

A global revision process

- "Advisory Expert Group" (**AEG**, 20 experts worldwide and 5 from the groups) was created in 2003 to make recommendations on update proposals from all groups;
- Issues first deliberated by **topical** expert groups (such as Canberra II, TFHPSA, Pensions and other TF);
- **Consistency** with revision of other systems (BOP, Classifications, Business accounting) & statistics;
- **44 updating issues** and 39 clarification items.

MAJOR SNA ISSUES

Different types of issues:

- The 4 **most problematic SNA issues**:
  - Pension schemes
  - Research and Development
  - Military expenditure
  - Goods for processing
- **Some other issues :**
  - **Units** – Ancillary units, holding companies and SPEs, securitization vehicles, etc.
  - **Government transactions** with the public corporations it controls
  - New Chapter on **Public Sector**

2. FINANCIAL SERVICES AND FINANCIAL ACCOUNTS

Financial issues

- Definition of financial services and FISIM
- Clarification of holding companies, head offices, SPEs
- New approach for non-life insurance services
- Output of the NCB.
- More detailed sectors and clarification of instruments
- Employee stock options

7

Financial services (inc. FISIM)

- Definition of financial services expanded beyond intermediation to include dealing in risk management and liquidity transformation (incl. margins on forex and securities trading).
- FISIM should be calculated on loans and deposits, by $(r_L - rr) \cdot y_L + (rr - r_D) \cdot y_D$

Where r_L is interest on loans, r_D interest on deposits, y is the value of loans / deposits, and rr is the reference rate. Loans can be made on own funds

- [FISIM already adopted in EU after ESA95 amendment]

Issue 6a. Financial services

- There has been an expansion in financial services provided by "banks" beyond simple borrowing and lending
- The definition of what is a financial corporation was expanded to include units undertaking risk management and liquidity transformation
- Expansion of sub-sectors in financial corporation sector
- FISIM definition refined to include use of own funds

FISIM

- Not covered in detail here as previously discussed.
- Also already implemented in ESA, so no change with introduction of ESA2010.
- Although, BPM6 now requires FISIM to be implemented in BoP.

10

Subsectoring of the Financial corporations sector

- More detailed to provide more consistency with requirements of ECB etc.
- 9 subsectors compared with 5 in ESA95.
  - Central bank (exc NCB).
  - Deposit taking corps
  - MMF
  - Non-MMF
  - Other financial intermediaries (exc insurance and pension funds)

11

Subsectoring of the Financial corporations sector

- More detailed to provide more consistency with requirements of ECB etc.
- 9 subsectors compared with 5 in ESA95.
  - Financial auxiliaries
  - Captive Financial institutions
  - Insurance corps
  - Pension funds

12

ESA 95 Financial corporations sub-sectors				ESA 2010 Financial corporations sub-sectors
Central Bank	S.121		S.121	Central Bank
Other Monetary and Financial Institutions	S.122		S.122	Other Monetary and Financial Institutions
			S.123	Money market funds
Other financial intermediaries	S.123		S.124	Non-Money-Market Investment Funds
			S.125	Other financial intermediaries
Financial auxiliaries	S.124		S.126	Financial auxiliaries
			S.127	Captive financial institutions
Insurance corporations and pension funds	S.125		S.128	Insurance corporations
			S.129	Pension Funds
Non-financial corporations	S.11		S.11	Non-financial corporations

S127 - Captives

- S.127 consists of all fin corps and quasi-corps which are neither engaged in financial intermediation nor providing financial auxiliary services and where most of either their assets or their liabilities are not transacted on open markets.

S127 - Captives

- In practice, many units assigned to S.127 will be only recognised as institutional units because their residence is different from that of the parent.

S127 - Captives

- A range of units previously classified under S.123, S.124 and S.11 (holding companies for non-financial corporations) can be classified to S.127 because of their relationship to the parent rather than the nature of their activity.

Holding companies, Head offices

- Head offices / holding companies mix-up
- ESA 95 holding company = ESA 2010 Head office
- Holding companies holds company assets, but does not manage = FinCorp (captive).
- Head office manages all units of an enterprise.
- Produces financial or non-financial services depending on the output of its subsidiaries

SPEs guidance

- Little physical presence, related to another corp usually as a subsidiary.
- Special Purpose Entities(SPEs) - Resident SPEs not separate units from the parent. Non-resident SPEs are always separate institutional units.

Issue 25b. Holding companies, Special Purpose Entities, and trusts

- In the 1993 SNA, a *holding company* was taken to be “a corporation [without significant production of its own]. . . whose principal function was to control and direct a group of subsidiaries”
- These companies are classified to the pre-dominant activity of its subsidiaries
- *1993 SNA holding companies* would have been better called head offices

Issue 25b. Holding companies, Special Purpose Entities, and trusts (cont’d)

- In SNA 1993, there is no mention of companies who do not control, but simply manage assets on behalf of the enterprise group.
- It is likely that such companies, known confusingly in business as “holding companies”, would be classified under the SNA 1993 to the pre-dominant activity of the group

Issue 25b. Holding companies, Special Purpose Entities, and trusts (cont’d)

- IN SNA 2008, the labelling is changed, and the *1993 SNA holding companies* are re-labelled Head offices. They are classified in the same way, to the pre-dominant activity of the group
- Now in the SNA 2008, holding companies are recognised as owners of assets rather than controllers, and so classified as financial corporations
- Result – 2008 “corrects” the classification of holding companies, but the result is a huge switch of financial assets and liabilities from the non-financial sector to the financial sector!

Non-resident government SPEs

- Some are securitisation vehicles – units that securitise assets, and classified as “other financial institutions.”
- Securitisation based on a future flow of revenue is not the sale of an asset, but borrowing.
- If a non-resident government unit borrows, borrowing is imputed by the government controlling the SPE

The output of Central Banks clarified

- Is measured by sum of costs (not fees, commissions + FISIM).
- If market activities, show separately from non-market in a different unit
- Artificial low or high interest rates so that an implicit tax or subsidy exists, should be recorded accordingly

Issue 6b. Allocation of the output of central banks

- Central Bank activities should be split into market and non-market activities
- In theory, the market activities should be valued at prevailing market rates (e.g. FISIM consistent with calculations for the rest of the banking sector)
- ESA has chosen to measure all Central Bank activity as the sum of costs (anything else too uncertain and difficult)

Non-life insurance

- Premium – payment to insurance company
- Claim – amount payable to insured in the event of an event covered by the policy
- The excess of premium over claims is invested and this provides an extra source of income to meet claims
- Output of insurance is premiums plus property income less claims

Non-life insurance

- The SNA output is measured according to the same principles as the company
- Property income is earned on reserves (excess of premiums over claims)
- This property income is assigned to policy holders, and recorded in the secondary distribution of income account

Non-life insurance

- Claims may be volatile – the model should use a trend estimate rather than actual claims observed in any period
- This trend estimate should reflect actual and expected claims
- So, in national accounts:
- Output = premiums plus premiums supplement (property income on reserves) less adjusted claims
- For catastrophes, part of claims may be recorded as capital transfers rather than current transfers

Issue 5. Non-life insurance services

- Output = premiums + premium supplements – claims incurred
- Premiums are money paid by policy-holders
- Premium supplements are investment income earned on cash held by insurance company to pay future claims
- Claims are money paid out by insurance company

Issue 5. Non-life insurance services

- When a catastrophe strikes, excessive claims result in negative output, leading to negative value added
- So smooth the claims, replacing claims by "adjusted claims" in the calculation
- This takes account of how the company meets the claims in practice (e.g. raiding reserves)

Accounts exercise

- Handout

Reinsurance

- Treat same way as direct insurance.
- But separate out transactions from direct insurance (previously consolidated).
- Separate premiums and claims (no netting)

Retained earning of mutual funds, insurance companies and pension funds

- Investment funds are recognised in SNA 2008, which cover mutual funds and money market funds, but not pension funds
- Is this an ESA change to reflect ECB requirement? Can't find it in ESA list of changes nor SNA list?

Financial assets classification

- To reflect financial market innovations… the financial asset classification is updated + better guidance.
  - Monetary gold and SDRs
  - Currency and deposits
  - Debt securities
  - Loans (Short and Long term)
  - Equity and investment shares
  - Investment fund shares

Financial assets classification (cont)

- Insurance, pension and standardised guarantee schemes
- Financial derivatives and Employee stock options.
- Other accounts receivable/payable

Repos (clarification)

- Clarification only.
- Continue to treat as collateralised loan
- On-selling recorded as a negative asset to avoid double counting (previously on-selling was not recognised)

Issue 1. Repurchase agreements

- A securities repurchase agreement (a repo) is when securities are provided for cash, with a promise to buy them back later at a higher fixed price
- The provider retains the benefits and risks of owning the securities
- This is the same as borrowing money with the securities as collateral – a collateralised loan
- No change! (Some unresolved issues)

Employee stock options

- These will be scored as compensation of employees in kind.
- Grant date is when the option is offered
- Vesting date is first opportunity for the employee to take up the option
- Exercise date is when the option is take up (or it lapses)

Employee stock options

- IASB accounting recommendation is that the enterprise calculates a "fair value" for the options at grant date
- The recording of income should be spread over the period between grant and vesting
- Between vesting and exercise date, increase in value is recorded as a holding gain for the employee and a holding loss of the employer
- Before the option is exercised, the arrangement is a financial derivative and scored as such in the financial accounts

Employee Stock Options

- NA treatment in line with IASB standards
- Data should therefore be available in company accounts.
- Will result in higher levels of compensation of employees.

39

Issue 3. Employee Stock options

- ESOs are granted to employees (grant date)
- Employees must serve a vesting period (until vesting date)
- They can then exercise their options (at exercise date)
- Business accounting standards, accepted by tax authorities, say that
- ESOs should be valued at a best estimate of market price at vesting date, and scored as compensation of employees at grant date

Treatment of non-performing loans

- SNA provides definition of non-performing loan – payments >3 months overdue.
- Continue to record at nominal value with interest accruing (until loan written off)
- SNA recommends nominal value and market value of such loans to be recorded. (!?)
- Challenge is identifying such loans.

41

Issue 4a. Non-performing loans

- Non-performing loans are loans held on the lenders books as financial assets, which are unlikely ever to be repaid (but not yet written off!)
- In theory, a market value should be used to revalue the loans
- In practice, such estimations are uncertain
- No change (but memorandum items recorded)

Issue 4b. Valuation of impaired loans and deposits

- Impaired loans are loans which are partly written off
- When is write-off recognised, and how should interest on them be recorded?
- Technical measurement issues not resolved

Clarification of guarantees

- 3 types of guarantee
- Guarantees provided by a **derivative** eg credit default swap. No change.
- **Standardised guarantees** – issued in large number for small amounts. For example “export credit guarantees”. If the guarantor (the government) sets the fees below the expected level of defaults, a subsidy should be imputed.

Granting and activation of loan guarantees

- **One-off** guarantees are usually a contingent liability, and so not recorded as a financial asset or liability.
- However, if the unit backed by the guarantee is in obvious danger of bankruptcy, then the guarantee can be recorded as a loan from the start.

SDR liability recognised

- Monetary gold and SDRs are both recognised as financial assets in the SNA 2008.
- Monetary gold is taken by convention to have no corresponding liability,
- …but SDRs are now considered to represent a liability of contributing member countries, and assets for the IMF.
- So need to be treated as separate items.

Clarification of financial instruments

- Index linked debt - guidance on estimating interest flows and any holding gains/losses.
- Debt indexed to foreign currency – guidance.
- More flexibility on valuation of unlisted equity.
- Treat unallocated gold accounts as financial assets and liabilities if held with non-residents.
- Clarifies definition of monetary gold and bullion.

47

Clarification of financial instruments (cont)

- Continues to distinguish between loans and deposits, but introduces new item “inter-bank positions” when both parties are banks.
- Fees payable on securities lending and gold loans – record as interest (+ FISIM).
- Clarifies distinction between financial and operating lease based on economic ownership.

48

CAPITAL STOCK

Capital issues

Extension of assets boundary to include:

- R&D, capital services, units etc.
- Weapons systems
- Modify computer software to include databases
- Updated classification + more guidance.

Issue 9. Research and development

- Should R&D be recognised as capital formation?
- Yes
- Valued at sum of costs
- Increases GDP and GNI significantly
- The amount varies between Member States
- Great concern on measurement issues in Europe (e.g. revaluation of initial estimate)

Issue 9. R&D - challenges

- Should payments for use of R&D products be scored as rentals to the country of registration?
- Should GDP measures reflect tax avoidance schemes of multinationals?
- E.g. Royalty payments for brand names diverts profits to country of registration

Issue 10. Patented entities

- Patented entities were invented in SNA to reflect value in ideas protected by patents, although no production was observed in their creation.
- The concept has been dropped, replaced by R&D capital formation leading to intellectual property products

Issue 11. Originals and copies

- When a copy of an original is produced – for example, when a copy of Microsoft Windows 7 is sold – should new capital formation be recognised, beyond that recognised in the value of the original?
- No when licence payments are annual or more frequent, otherwise yes. These licence payments to be treated as rentals, not acquisition of an assets

Issue 12. Databases

- Should only “large” databases be capitalised?
- Drop the word large, and apply the usual tests to see if the creation of a database qualifies for recognition as capital formation
- Create an asset category “software and databases”, to be split if possible

Issue 13. Other intangible fixed assets

- Replace “Other intangible fixed assets” by “Other intellectual property products”
- This residual category still needed despite the recognition of R&D as capital formation

Issue 14. Cost of ownership transfers

- The issue discussed was how to treat decommissioning costs of large capital projects such as nuclear power stations
- In theory, recognise the decommissioning requirement in the acquisition price of the capital asset, then depreciate this to zero over its life.
- Recognise decommissioning as ownership transfer cost i.e. as capital formation when it occurs and written off in year it occurs

Issue 15. Cost of capital services

- Should we show capital services (the use of capital) explicitly in the production account as a component of value added? This will help productivity analysis.
- No – keep it as an extra

Issue 16. Government owned assets

- Should a return on capital be imputed when measuring government output as the sum of costs.
- This is an extra to the normal measure of capital consumption used.
- No – too much guesswork involved

Issue 17. Mineral exploration

- Expanded description of what is to be included as capital formation
- No change

Issue 18. Rights over non-produced assets for non-residents

- All non-produced assets should be treated like land – i.e. a nominal resident unit should be recognised when a non-resident owns the asset

Issue 19. Military expenditures

- Should weapon systems be recognised as assets, and should the criterion remain, that only military items with an equivalent civilian use could be recognised as assets.
- Yes – significant change for some Member States, with associated security issues on data collection

Issue 20. Land

- Land split into two main categories
  - Natural land
  - Improved land
- This allows land improvements to be recognised as capital formation leading to an increase in the asset holdings of improved land

Issue 20. Land

- The need for adjustments in the *other change in volume* account remains, due to lumping of natural land and improved land under one or other label, according to which makes up the majority of the combined asset

Issue 21. Contracts, leases and licences

- Under certain conditions, contracts can be recorded as non-produced, non-financial assets
- The contracts must be transferable, and value is only recognised on transfer
- Contracts are unusual in that although they are non-financial assets, they can take negative values

Issue 22. Goodwill and other non-produced assets

- Goodwill and marketing assets – value is calculated on purchase (take-over) of a company as the excess of the purchase value over the value of the other assets and liabilities identified in the company

Issue 23. Obsolescence and depreciation

- More text on the concepts and practical application

Research and development

- Research and development should now be recorded as gross fixed capital formation (not intermediate consumption)
- Identify a separate establishment if possible as R&D is not an ancillary activity.
- R & D is recorded as sum of costs
- Patented entities (recognised in the 1993 SNA) are included in these intellectual property products

R&D - Originals and copies

- Creation of an intellectual property original is capital formation, as the resulting asset is a source of economic benefits over time
- The benefits are earned by allowing users to use the content of the original through a licensing system
- If annual payments are made for a licence to use the original, payments are service payments as under an operating lease

Cost of capital services

- A new chapter is in the SNA 2008, explaining the role and appearance of capital services in the system
- It is desirable to estimate capital services and capital consumption in an integrated model
- There will be no changes to the SNA standard, but extra tables can be derived.

Databases

- Databases should be recorded as capital assets
- Any software associated with the database should be recorded separately
- Own account databases should be valued at cost
- Databases sold on the market should be valued at the market price

Weapons systems

- The 1993 SNA excludes “offensive weapons and their means of delivery” from capital assets, irrespective of their length of life
- The SNA 2008 records such items as capital assets

72

Government and non-market producers – cost of capital of own assets

- A return on fixed capital owned and used by non-market producers, was proposed. The rate of return was to be "expected real rate on government bonds, supplemented by other indicators of the cost of borrowing for government."
- This change was rejected, under pressure from European countries, due to the uncertainty associated with the chosen rate of return

Land improvements

- Improved land will be shown as a distinct item from natural land
- When it is not possible to partition the value between natural land and improved land, the whole value should be assigned to the dominant part

Goodwill and marketing assets (clarification)

- From purchased goodwill to purchased goodwill and marketing assets.
- Marketing assets include logos, customer lists etc
- Valued as excess of value paid over total assets less liabilities of an enterprise.

75

Water resources

- Covers surface and groundwater used for extraction where water is scarce and ownership can be exercised.

76

Consumption of fixed capital (clarification)

- Clarification that CFC should be measured using average prices of the specific asset, rather than a general price index.

77

Cultivated biological resources

- Previously cultivated assets.
- Only include as assets where under the direct control of institutional units.

78

Concept of resource lease introduced

- Resource lease introduced in cases where the **natural** resource continues to be shown in the balance sheet of the legal owner, even though a lessee is using the resource in production and paying rent.

79

Other changes

- Increased detail in the breakdown of other changes in volume of assets account.

80

Cost of ownership transfer

- Still treat as capital formation, but over the period the asset is expected to be held (not the life of the asset).
- Costs of transfer on the disposal of an asset should be recorded as GFCF, but written off in the year they are incurred.
- Terminal costs (dismantling) should be written off over lifetime of the asset.

81

Classification of assets

- Distinguishes between produced and non-produced assets.
- Classification expanded to reflect new categories of assets
  - Intellectual property products
  - Weapons systems
  - Cultivated biological resources

82

PUBLIC ADMINISTRATION

83

Issue 2. Employment retirement pension schemes

- Should the implicit liabilities of unfunded (government) pension schemes be recognised in the SNA ?
- No – not in the core accounts. Too much uncertainty in the estimation process, and difficult to untangle from general schemes in some countries
- Supplementary table specified, showing liabilities for both unfunded employee schemes, and general social security schemes

Public Administration issues

- Public/govt/private boundary issues.
- Permits, leases and licenses versus taxes.
- Pension entitlements

85

Public / private / government sector boundaries

- Control determines the boundary between public and private – a set of control indicators is listed in the SNA 2008
- General guidelines are given on the meaning of "economically significant prices" as a guide to market / non-market boundary decisions

Issue 24. Public-private partnerships

- Description of these schemes included, and guidance given on the issues to consider in deciding who is the economic owner of assets
- Room is left for developments in international financial reporting standards to guide the international statistical standards
- The current position in the international accounting standards is that ownership of the underlying assets at the end of the partnership is a key indicator in deciding who is the economic owner during the partnership

NPI's

- NPI subsectors can now be assigned to different institutional sectors eg govt
- Allows compilation of supplementary NPI tables summarising all NPI activity.

88

Treatment of restructuring agencies

- Clarifies classification of units engaged in privatisation and impaired assets (from banking crisis).

89

Treatment of govt issued permits

- See next slide

90

Contracts (permits?), leases and licences

- Most contracts do not represent assets, except for two cases:
  - A price difference appears between the contract price and the market price, and one party is able to transfer their contract role to another
  - When a contract permits a party to engage in an activity for which legal permission is necessary, and monopoly profits can be earned – this is an exception to the general rule that payments to government for permits and licences, no matter how the fee is fixed, should be classified as taxes.

Contracts, leases and licences

- The rest of this recommendation is very unclear, but the suggestion is made that in certain circumstances, payment of the tax can result in the acquisition of an asset.
- This breaks the fundamental rule of non-exchange payments to government, that a tax is unrequited. Watch this space!

Non-resident government SPEs

- Some are securitisation vehicles – units that securitise assets, and classified as "other financial institutions."
- Securitisation based on a future flow of revenue is not the sale of an asset, but borrowing.
- If a non-resident government unit borrows, borrowing is imputed by the government controlling the SPE

Ownership of fixed assets created through PPPs

- New guidance to determine whether the private or public partner is the economic owner of the asset.

94

Exceptional payments

- From PCs – record as withdrawals from equity, not dividends
- From Govt to quasi-corporations – if payment is to cover losses, treat as capital transfers. If they expect to receive a return on the payment, treat as an addition to equity.

95

Taxes

- Unsatisfactory – "taxes can be recorded as paying for the acquisition of a (non-financial) asset"
- Tax credits. The whole of the payable tax credit should be scored as a benefit in government expenditure. The amount recovered in tax paid should be noted.

Taxes on holding gains

- Treat as current tax on income.

97

Issue 7. Taxes on holding gains

- Can a tax on holding gains be placed in the category of income tax, and treated accordingly in the accounts?
- Yes

Recording pension entitlements

- Full presentation in Workshop 1, so won't cover here.
- Supplementary table now required.

99

OTHERS

100

Other issues (incl.consistency with BoP)

- Change of economic ownership introduced.
- Residence
- Units – Ancillaries, artificial subsidiaries, branches
- Goods sent abroad for processing
- Merchanting

STATEC Feb 2013 101

Change of economic ownership

- Determines timing of transactions
- New guidance to distinguish between legal and **economic** ownership.
- Economic owner is who assumes risks or receives benefits from an asset
- [Previous manuals implied legal ownership]
- No exceptions in BoP (re Goods for processing and merchanting)

STATEC Feb 2013 102

Residence

- Move to "centre of predominant economic interest" (from centre of economic interest)
- Useful for households, but not for corporations. Corporations which have a centre of economic interest in another country will almost certainly have a separate unit recognised in that country.

Individuals changing residence (migrants)

- No change in ownership of assets and liabilities.
- Simply reclassify to the new country of residence of the economic owner
- Record in the other changes in volume account, not capital transfers.

Ancillary units

- A productive activity is ancillary to the main production when the resulting product is a common type and used as intermediate consumption within the same enterprise
- However, if an ancillary unit is in a different location from the establishments it serves, it can be useful to recognise the unit separately and classify it according to its main activity.
- Output = sum of costs.
- Main impact on regional accounts

Issue 25a. Ancillary units

- The SNA 93 said that ancillary units should not be recognised as separate units from their parent.
- When the ancillary unit activity is different from the parent and in a different location, regional measures of activity when summed will differ from national ones
- To "solve" this issue, ancillary units where there is sufficient information for activity output to be measured as the sum of costs, are recognised as separate production units in SNA 2008

Artificial subsidiaries

- One form of SPE (along with captives and SPEs of government)
- Previously called ancillaries.
- Wholly owned by parent and created to provide services to parent.
- Often set up to avoid taxes.
- No independence, so only treat as a unit if it is resident in a different economy to its parent.

Non-resident unincorporated businesses (branches)

- 1993 SNA states that an unincorporated enterprise owned by a non-resident institutional unit should be treated as a notional resident unit in the country where it is sited.
- The 2008 SNA is more specific – a physical presence is not necessary, neither are a full set of accounts.
- If a unit **engages in production**, then it should be treated as a notional resident unit
- Being subject to income tax in the host country is a preferred criterion (even if exempt)
- The list of criteria is indicative, and a unit may be treated as a notional resident unit even if not all of the criteria are met.

Residence of multi-territory enterprises

- Guidance on treatment
- Eg airlines, shipping companies, piplelines
- If not possible to identify separate branches or a parent, prorate the operations.

109

Head office

- Clarification of head office from holding company.
- “manages other units of an enterprise, undertakes strategic planning and decision making”.
- Allocate to non-financial sector if subsidiaries are non-financial.
- If subsidiaries are financial, treat as a financial auxiliary

110

Valuation of output for own final use by households and corporations

- Include a return on capital as part of the sum of costs approach (in the absence of market prices).
- SNA93 did not include a return on capital.

111

Goods for processing

- Possibly the biggest change – from gross recording of the flow of goods for processing to a net basis.
- Previously goods sent abroad and returned after processing = trade in goods, even if no change of ownership.
- Now, follow strict change of ownership principle.
- Only record processing fee – manufacturing services on physical inputs owned by others.
- Goods flows = supplementary items.
- If the change is also applied internally in the domestic economy, there will be reclassification of flow of goods to the delivery of a service only, with no associated movement of goods
- Separate session in Workshop 1.

Merchanting

- Change of ownership, so goods (previously services).
- New category “goods under merchanting”.
- Purchases by merchant = negative exports, sales = positive exports
- Net recorded as goods under merchanting in compiling country (exports and imports in other countries)
- Do not enter economy so not in IMTS.