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DIRECTORATE FOR FINANCIAL, FISCAL AND ENTERPRISE AFFAIRS
INVESTMENT COMMITTEE

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Workshop on International Investment Statistics

Direct Investment Technical Expert Group (DITEG):
Compilation of outcome papers (meeting of 15-17 June 2004)

Note by the joint IMF/OECD DITEG Secretariat

12-13 October 2004

The present document includes a summary of the discussions by the DITEG at its first meeting held on 15-17 June 2004. The document makes frequent reference to issues papers and background documents circulated in June 2004.

DITEG is an advisory group and its decisions are not binding (see terms of reference). The conclusions reached by the DITEG are referred to in the Workshop on International Investment Statistics (WIIS) of the OECD Investment Committee and the IMF Committee on Balance of Payments Statistics (BOPCOM) for their decisions in the context of the revision of the "OECD Benchmark Definition of Foreign Direct Investment" and the "IMF Balance of Payments Manual", respectively. The present note includes questions addressed to WIIS and to BOPCOM. The Secretariat note DAFFE/IME/STAT(2004)22 provides additional discussion points to complement these questions.

At their 12-13 October 2004 meeting, WIIS Delegates are invited: (i) to review the conclusions of the DITEG included in the present document; (ii) to discuss the recommendations taking also into account additional discussion points included in DAFFE/IME/STAT(2004)22; (iii) to make final recommendations on these issues in view of the revision of the OECD Benchmark Definition of Foreign Direct Investment, of which the revised draft

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SUMMARY OF OUTCOMES OF THE FIRST MEETING OF THE DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG)

for

IMF Committee on Balance of Payments Statistics

and

Workshop on International Investment Statistics

June 15-17 2004, OECD, Paris

The first meeting of the Direct Investment Technical Expert Group (DITEG) was held during June 15 - 17, 2004 at the OECD, in Paris. This report indicates issues/topics for which the DITEG prepared outcome papers and summarizes the discussions/decisions on issues/topics for which the DITEG did not prepare outcome papers at this stage. This report also summarizes decisions of DITEG on processes, future agenda, and other administrative matters.

I. Issues/topics of the first meeting

A. *Valuation of direct investment in equity and branches*

1A. Valuation of direct investment equity

See outcome paper # 1A

1B. Valuation of branches

See outcome paper #1B

B. *Identification of branches*

See outcome paper #10

C. *Reverse investment and directional principle*

- A new proposal was introduced during the discussion on which there was no issues paper. As a consequence, further discussion of this topic was deferred to the December 2004 meeting.
- United States to prepare an additional issues paper for the next meeting

D. 10 per cent threshold

See outcome paper #2 (to be prepared by the OECD)

E. Indirect investment: Fully consolidated system

See outcome paper #3

F. Special purpose entities

See outcome paper #9

G. Reinvested earnings

5A. National/sectoral saving

See outcome paper # 5A

5B. Reinvested earnings of indirectly owned direct investment enterprises

See outcome paper #5B

H. Mergers and acquisitions

Issue not discussed. To be taken up at December 2004 meeting.

I. Bringing together all direct investment-related issues (transactions in goods and services, income, financial flows, stocks between affiliates) as an appendix to the balance of payments manual

See outcome paper #6 and #19

II. Administrative matters

- The DITEG agreed on the updated list of issues for DITEG, the assignment of issues papers, and the process for establishing an agenda for the next meeting.

- The group agreed that it will continue its work through electronic communication (including EDG).

- The Secretariat will circulate the draft outcome papers and summary of the conclusions the members who will provide their comments within two weeks to the Secretariat. After the outcome papers and summary of conclusions are finalized, they will be posted on the IMF's, OECD's and BEA's external websites.

- The next meeting of the DITEG will be held during December 6 – 9, 2004 at IMF Headquarters in Washington D.C.

III. Participants: DITEG members (see terms of reference)

DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG): OUTCOME PAPER # 1(A)

12 August 2004

1. Topic: ***Valuation of direct investment equity***

2. Issues: *See DITEG Issue Papers # 1(A) by the US, ECB, and Australia*

3. Recommendations:

(i) The group agreed that market valuation is the preferred concept for the measurement of direct investment equity, and that this concept needs to be maintained and stressed in the updated standards.

(ii) The group agreed that the international organizations (IMF and OECD) should provide more guidance and information on options for measuring market values, particularly for measuring the market value of equity in unlisted companies.

(iii) Several background papers were presented to the group, and these papers described numerous different methodologies for estimating the market values of direct investment equity:[1]

(a) Actual prices at which recent transactions were conducted. These prices would almost always exist for listed companies (based on stock exchange quotations) and would sometimes exist for unlisted companies whose shares had recently traded.

(b) Methods based on stock market indexes (see background documents provided by the United States and by Australia).

(c) Methods that applied capitalization ratios (market value divided by book value) for listed companies to unlisted companies.

(d) Methods that revalued just tangible assets of direct investment enterprises, including land and other property, plant, and equipment, and inventories (see background document provided by the United States).

(e) Methods based on net asset values, including identified intangibles and goodwill, reflecting current period prices.[1]

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[1] A description of these methods, including details on topics such as how to identify and value goodwill (item (iii)e), may be clarified in compilation guides or annexes to the standards rather than in the body of the updated standards themselves.

(f) Methods based on net asset values, but excluding goodwill, reflecting current period prices.

(g) Methods based on the volume of own funds of the direct investment company, i.e. "Own Funds at Book Value" (see background documents provided by the ECB)[2]

(iv) Some practical issues were raised about the continued existence of asymmetries due to differences in valuation methods and differences in accounting rules followed by different countries. It was believed that the extension of fair value accounting principles to additional balance sheet items by the organizations that establish accounting standards may narrow these differences over time.

4. Rejected Alternatives:

(i) The group also identified some methods that it considered to be unacceptable.

(a) The group rejected the broad use of historic cost or acquisition price (same as in *BPM5*).

(b) The group rejected accumulating balance of payments flows to estimate direct investment equity on an annual basis.

5. Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop in International Investment Statistics (WIIS)

(i) Do the Committee and the WIIS agree that market valuation is the preferred concept for the measurement of direct investment equity, and that this concept needs to be maintained and stressed in the updated standards?

(ii) Do the Committee and the WIIS agree that the use of historic cost/acquisition price, and the accumulation of flows over a long period of time, should not be acceptable methods for valuing direct investment equity? (See 4(i) above.)

2 In addition to other components (paid-up capital, investment grants, shares premium accounts) the OFBV method incorporates cumulative reinvested earnings (including current-year results). It was reported that, in the future, in calculating OFBV, most assets of some companies will have to be written up or down at least once a year to reflect their fair or current values.

DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG): OUTCOME PAPER # 1(B)

6 August 2004

1. Topic: <u>Valuation of branches</u>

2. Issues: *See DITEG Issues Paper # 1(b)*

3. Recommendations:

(i) The group agreed that all assets, including intangible assets, should be included in the valuation of branches and supported the proposal in the *Annotated Outline* that the value of a branch be defined as being the 'sum of all assets, including intangible assets, as well as financial and nonfinancial assets, less debts and financial derivatives in a liability position".

(ii) The group agreed that the term "net worth of the branch" used in the IMF's present manuals and in the OECD's *Benchmark Definition of Direct Investment* was not favored and that an alternative term needed to be devised.

(iii) A number of group members had concerns about the use of the term "net equity" proposed in the *Annotated Outline* as a replacement for the term "net worth of the branch" and suggested "equity in branches" or "branch equity" as alternatives.

(iv) Some practical issues were raised about the difficulty of identifying ownership of certain intangible assets and the group agreed that guidance on this issue should be provided in the revisions of the *BPM5* and the *Benchmark Definition*.

4. Rejected Alternatives:

(i) The group rejected the option of retaining the present description in the *Benchmark Definition* of the items to be included in the valuation of branches.

(ii) The group rejected the option of adding selected non-current assets to the *Benchmark Definition* list of the items to be included in the valuation of branches.

5. Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop in International Investment Statistics (WIIS)

(i) Do the Committee and the WIIS agree with the recommended definition of the valuation of branches? (See 3(i) above.)

(ii) Do the Committee and the WIIS agree that the term "net worth of the branch" be replaced with an alternative term? (See 3(ii) above.)

(iii) Do the Committee and the WIIS prefer the replacement term "net equity" proposed in the Annotated Outline, or the terms "equity in branches" or "branch equity" as alternatives? (See 3(iii) above.)

DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG): OUTCOME PAPER # 2

24 September, 2004

1. Topic: ***Direct investment: 10 per cent threshold of voting power/equity ownership, employment***

2. Issues: *See DITEG Issues Paper # 2 by OECD and Luxembourg (and background paper by Luxembourg)*

3. Recommendations:

(i) The group endorsed the proposal to move to 20 per cent of voting power or ordinary shares as the threshold for the operational definition for a direct investment relationship, even though it was recognised that changing the current threshold of 10 per cent to 20 per cent would not have a significant impact on the data. The group found that there were no strong conceptual grounds for choosing 10 or 20 per cent, and so any choice below 50 per cent would be arbitrary. However, there are strong practical arguments for supporting the change to 20 per cent threshold, namely with regard to accounting standards. International Accounting Standards (IAS) as well as the accounting standard used by the United States utilize a 20 per cent threshold for financial statements. Nonetheless, some caution was also expressed about anchoring statistical standards explicitly to those of the accounting world. The group felt that if the change to the 20 per cent threshold were to be adopted, the rationale given by the accounting world for promoting that threshold should be cited, not just the explicit link.

(ii) The group re-affirmed the current definition that direct investment is evidenced when there is a significant degree of influence by the direct investor over the direct investment enterprise. On the basis of practical considerations, it was agreed by most experts to maintain the principle that a strict numerical threshold (proposed at 20 per cent) should be the sole operational criterion and, in line with current standards, deviations should not be recommended. The group recognized that, in some circumstances, the strict application of the threshold rule may be inappropriate as there will be exceptions below and above the threshold, i.e. the existence of a significant degree of influence below the threshold or a lack of significant influence above the threshold. There was a degree of unease expressed by some members for reconciling the concepts that are to be measured and the use, in practice, of a strict numerical threshold. It was also recalled that the IAS allows a more flexible approach.

(iii) The group agreed that the definitions in the *Balance of Payments Manual,* the *Benchmark Definition of Foreign Direct Investment,* and the *System of National Accounts (SNA)* need to be consistent. It was also agreed that there is a value in further clarification of "ordinary shares" and "voting rights". Special attention is needed to harmonise the definition of a "branch" with the SNA to ensure that there is a distinction made between a branch and an unincorporated business which is not a branch (at present, no such distinction is drawn in *BPM5* or the *Benchmark Definition*). As a result of the discussion on the needs to improve the definition of "subsidiary", "associate", and "branch", there was a debate on the usefulness of maintaining these categories of direct investment enterprises versus a different system which would recognise only two categories of direct investment enterprises: (a) majority-owned and (b) others (not majority-owned). However, there was no final decision reached on this proposal. Further work on definitions will be conducted electronically; IMF will circulate proposed definitions.

(iv) The group considered the proposal to add two criteria to the definition of direct investment: (a) number of employees; and (b) the size of capital. Some concerns were expressed about using employment as a variable for separating "real" direct investment from "flow through" direct investment, as there may be many instances where few, if any, employees may nevertheless represent "real" direct investment. Some of the experts questioned the introduction of this concept, mostly targeting Special Purpose Entities (SPEs), as a standard component, given that such entities concern relatively few countries. Others expressed concerns for the consistency of the proposal with the treatment of equity and debt with SPEs by counterparties. It was suggested by some that the objective of the proposal was rather to develop a new category for the analytical needs of foreign direct investment statistics but not to eliminate the investments by financial entities with no employment. It was also questioned whether, more generally, the definition of foreign direct investment should include a criterion relating to the significance of economic activity. The group did not reach a firm conclusion but agreed to continue to debate the issues in the context of the broader discussion on SPEs which raise concerns for the analytical requirements of detailed foreign direct investment statistics.

3. Rejected Alternatives:

(i) The group rejected the alternative to lift the current 10 per cent threshold to 50 per cent. It was agreed that direct investment should not be defined as comprising only "majority owned affiliates" as opposed to the current concept of "significant influence".

(ii) The group rejected the flexible treatment of the numerical threshold (see also comments above under 3 (ii).

4. Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop in International Investment Statistics (WIIS):

(i) Do the Committee and the WIIS agree that it is preferable to change the current threshold 10 per cent to 20 per cent, for better alignment with international accounting standards, even though the real impact on the data is likely to be small?

(ii) Do the Committee and the WIIS agree on the strict application of the agreed threshold as opposed to its flexible application? Do they agree that using a numerical guide as the sole criterion is justified even though there are some recognised exceptions and the strict application of these criteria may be difficult to reconcile with the underlying definition of FDI?

(iii) Do the Committee and the WIIS agree that there is a need to review fundamental definitions, such as those for "ordinary shares" and "voting rights", and to have the same definitions of "subsidiary", "associate", and "branch" as in the SNA? Do they see a need for including two sub-categories under unincorporated enterprises, i.e., branches defined more conventionally (as in the SNA) and other types of unincorporated enterprises?

DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG)

OUTCOME PAPER (DITEG) # 3

1. ***Topic:*** Indirect FDI relationships and alternatives to the Fully Consolidated System

2. ***Issues:*** See DITEG Issue Papers # 3 by the IMF, the ECB and Japan

3. ***Recommendations*****:**

(i) DITEG discussed the rationale behind the Fully Consolidated System (hereinafter, "the FCS") and concluded that it is based on a mixture of "influence" and "control". A layer based on "influence" arises where a direct investor has between 10 percent[3] and 50 percent of the voting power (directly and indirectly) in another enterprise. A layer of "control" arises where a direct investor can control the activities of another enterprise, as a result of its having more than 50 percent voting power (directly or indirectly). As a consequence, a layer based on "control" may include several direct investment enterprises, each more than 50 percent owned by the direct investment enterprise above it in the chain of ownership. DITEG determined that no chain could have two adjoining layers based on influence[4] and that any layer based on influence following the first layer would be considered the last layer in the chain. In the case where the first layer is one of control, the maximum number of layers is two – control followed by influence. In the case where the first layer is one of influence, there could be up to three layers – influence, followed by control, followed by influence.

Combinations of Influence and Control Possible under FCS

	Layer 1	**Layer 2**	**Layer 3**
1. Direct Investor	Control		
2. Direct Investor	Control	Influence	
3. Direct Investor	Influence		
4. Direct Investor	Influence	Control	
5. Direct Investor	Influence	Control	Influence

(ii) DITEG was of the opinion that, on conceptual grounds, the FCS is closest to the concept that FDI statistics attempt to measure. Therefore, DITEG recommends that the FCS be maintained as the conceptual reference in the updated version of the manuals. However, DITEG recognized the difficulty in applying the FCS and the difficulties encountered by

3 . References to the 10% threshold should be changed across the paper should a final decision to move towards a 20% cutoff be finally taken.

4 . That is, an associate of an associate would break the direct investment chain.

reporters to understand its rationale, all the more as it does not coincide with the rules governing the accounting consolidation process.

(iii) With the aim to simplify data collection while preserving the analytical value of FDI figures several alternatives to the FCS were discussed by DITEG, namely (1) a narrow definition limited to directly held direct investment enterprises; (2) the use of a cut-off of 10 percent or more ownership for both direct and indirect ownership ("10% method"); and (3) the use of the standard 10 percent threshold for direct relationships and more than 50% ownership for indirect relationships ("10/50 % method"). In addition, other countries proposed a complete adherence to consolidation rules applicable in business accounting standards within each country or full alignment to International Financial Reporting Standards (IFRS).

(iv) A majority of DITEG members was of the opinion that the "10/50 % method" was closest to the FCS, since it just skipped layers lower than the first layer based on influence, where they exist, while still covering the rest of the direct investment companies. Some DITEG members also pointed out that this method is also closest to the consolidation rules applicable under IFRS.

(v) DITEG also considered that, in most cases, the "10% method" provides similar results to both the FCS and the "10/50 % method" and was, thus, also regarded as an acceptable approximation to the FCS.

(vi) A concern that was mentioned was restrictions on foreign ownership applied by some countries, which implies that most FDI relationships to those destinations amount to a maximum of 49%. DITEG did not consider this circumstance to pose unique conceptual issues and therefore did not modify its recommendations on this subject.

(vii) Finally, DITEG was of the opinion that whatever the system applied in practice, indirectly owned companies which are, via a circular chain of ownership, in the same country as the direct investor should also be part of the foreign direct investment perimeter. [5]

4. *Rejected Alternatives*:

(i) DITEG considered that the first option (limited to direct ownership links) should be rejected on the grounds that it would significantly diminish the analytical value of FDI figures.

While recognising the practicality of a full adherence to accounting consolidation rules, the majority of DITEG was of the opinion that the existence of different accounting rules across countries would pave the way for an increasing level of global asymmetries. Additionally, it would make statistics fully dependent on changes in the accounting framework.

5. *Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop in International Investment Statistics (WIIS)*

(i) Do the Committee and the WIIS agree with DITEG's recommendation to maintain the FCS as the central conceptual reference for the delineation of the direct investment perimeter in the updated version of the manuals?

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5 . More specifically, reinvested earnings and equity stocks based on the volume of own funds of direct investment enterprises should include reinvested earnings generated by such resident (indirectly owned) direct investment companies.

(ii) Do the Committee and the WIIS agree that, from the above-mentioned options, the so-called "10/50 %" method is the closest practical approximation to the FCS?

(iii) Do the Committee and the WIIS agree that the so-called "10%" method is an acceptable proxy to the FCS?

(iv) Do the Committee and the WIIS agree with the rejection of a narrow definition limited to directly held direct investment enterprises?

(v) Do the Committee and the WIIS agree with the concerns expressed by DITEG as regards the possibility to make the statistical definition of the direct investment perimeter fully dependent on accounting rules?

DIRECT INVESTMENT TECHNICAL EXPERT GROUP: OUTCOME PAPER #5A

August 6, 2004

1. ***Topic: Reinvested Earnings***

2. ***Issues -*** *see DITEG Issues Paper #5A. See also BOPTEG outcome paper #18*

3. ***Recommendations:***

(i) DITEG considered the three broad alternative treatments of reinvested earnings proposed in Issue Paper #5A, as follows:

(a) Treat saving of direct investment enterprises on the same conceptual basis as the treatment of savings of other resident enterprises, and not impute reinvested earnings as direct investment income in the Current Account and as a transaction in the Financial Account;

(b) Extend the current treatment of reinvested earnings to all equity investment (i.e. non-resident-to-resident portfolio investment and all resident-to-resident investment relationships); or

(c) Retain the current treatment, with the possible extension of imputing reinvested earnings for non-resident-to-resident portfolio investment.

(ii) DITEG discussed the relative merits of the alternative treatments being proposed but were unable to reach consensus on the preferred conceptual treatment for reinvested earnings. About half of the experts supported the current treatment of reinvested earnings (i.e. restricted to non-resident-to-resident direct investment relationships). These experts were of the view that the current treatment of reinvested earnings is based on the concept that the direct investor has significant influence in the management of the direct investment enterprise and that the decision to retain some earnings within the enterprise represents a conscious, deliberate investment decision on the part of the direct investors. These experts did not agree to an extension of reinvested earnings to non-resident-to-resident portfolio investment. However, some of the group felt that the treatment of retained earnings of mutual funds in *ESA95* (they are deemed to be distributed and then reinvested — in the same manner as for direct investment) was appropriate.

(iii) A similar number of experts noted the current inconsistency between SNA93 and BPM5/BD3 standards and agreed that this inconsistency needed to be addressed. However, there was no agreement on the preferred alternative conceptual treatment.

(iv) Those in favour of not imputing reinvested earnings argued that this would bring BPM5/BD3 standards in line with the current SNA standards, in that the level of saving by an enterprise is an indicator of the extent to which an enterprise intends to fund accumulation from internal resources. The decision to save rather than to pay dividends is deliberate and similar to other

decisions made in the management of the enterprise, such as decisions to invest in fixed capital. The enterprise is considered a separate institutional unit from its owners partly because it can make such decisions, regardless of the level of influence of its shareholders.

(v) These experts noted that there are significant practical difficulties in collecting reinvested earnings data and that in most cases current period quarterly estimates are projections based on the previous year's annual data, and added that it would be even more difficult to develop estimates of reinvested earnings for portfolio investment. Concerns were also expressed about increasing the number of imputed transactions.

(vi) Those in favour of extending imputation of reinvested earnings to non-resident-to-resident portfolio investment and resident-to-resident investment relationships argued that earnings of an enterprise accrue to all investors as they are earned. Dividends are cash payments which may be less than, equal to or more than the earnings accrued. Earnings less dividends accrue to investors in the form of income. As the earnings are available to the enterprise for its use, they are deemed to be reinvested in the enterprise.

4. Rejected alternatives

None.

5. Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop in International Investment Statistics (WIIS)

(i) What are the Committee's and WIIS views regarding the appropriate conceptual treatment of reinvested earnings for entities in a:

(a) direct investment relationship? Is the present treatment acceptable? Or should reinvested earnings not be treated as a transaction, and be recorded instead as an entry in the other change in assets account?

(b) portfolio investment relationship? Is the present treatment acceptable? Or should reinvested earnings for portfolio investment be imputed? See 3 (vi) above.

(ii) In view of the position of the AEG and the range of views among direct investment statistics experts, does the Committee agree that a pragmatic outcome would be to retain the current treatment of reinvested earnings? See 3 (ii) above.

DIRECT INVESTMENT TECHNICAL EXPERT GROUP: OUTCOME PAPER # 5(B)

6 August 2004

1. Topic: <u>Reinvested earnings of indirectly owned direct investment enterprises</u>

***2. Issues** – See DITEG Issues Paper #5B*

3. Recommendations

(i) The group agreed that reinvested earnings should be grossed up, along the chain of indirectly owned enterprises.

(ii) The group agreed that, on a bilateral basis, reinvested earnings should only be allocated to the most immediate counterpart country, regardless of where the reinvested earnings may have originated.

(iii) The group agreed that the new manual and the new *Benchmark Definition* should clarify the treatment of reinvested earnings of indirectly owned enterprises. At present, countries that are applying the methods explained in Figure 1 (of the BD3) may be double counting the reinvested earnings of indirectly owned enterprises; these earnings could be both included in the operating profit of the recipient enterprise and added to the total reinvested earnings passed up the chain of enterprises.

4. Rejected alternatives

None

5. Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop in International Investment Statistics (WIIS)

(i) Do the Committee and the WIIS agree that reinvested earnings should be grossed up all the way along the chain of indirectly owned enterprises?

(ii) Do the Committee and the WIIS agree that the most immediate country in the chain should be allocated the reinvested earnings, regardless of where the earnings may have originated?

(iii) Do the Committee and the WIIS agree that the revision of BPM5 and the new edition of the Benchmark Definition should clarify the treatment of reinvested earnings of indirectly owned enterprises to eliminate the possibility of double-counting?

DIRECT INVESTMENT TECHNICAL EXPERT GROUP

OUTCOME PAPERS #6 AND #19

1. Topic: Bringing together all direct investment-related issues (transactions in goods and services, income, financial flows, stocks between affiliates) as an appendix to the balance of payments manual

***2. Issues** – See DITEG Issues papers #6 and #19*

3. Recommendations

(i) The group agreed that the new balance of payments manual should include an appendix setting out possible presentations on all transactions (including goods and services) and positions between affiliates.

(ii) DITEG recognized that transactions and positions between affiliated financial SPEs are excluded from direct investment under existing international standards. The treatment of SPEs raises similar conceptual and practical questions for the core accounts and supplemental presentations.

(iii) The group agreed that such presentations should be considered satellite accounts (and so, would not be part of the standard reporting requirements), and may vary from country to country, depending on the emphasis that individual countries may wish to place on particular aspects of these relationships.

4. Rejected alternatives

None

5. Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop in International Investment Statistics (WIIS)

(i) Do the Committee and the WIIS agree that the new manual should include an appendix, setting out possible alternative presentations of transactions between entities in direct investment relationships? See 3(i) above.

(ii) Do the Committee and the WIIS agree that any such presentation of data should be considered to represent a satellite account, and that it not be a standard reporting requirement? See 3(ii) above.

DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG): OUTCOME PAPER # 9

6 August 2004

1. Topic: Special Purpose Entities (SPEs) and Holding Companies

2. Issues – see two DITEG Issues Papers #9 (one prepared by the Australian Bureau of Statistics and one by the IMF)

3. Recommendations:

(i) The group agreed that, in balance of payments statistics, SPEs should be recognized as separate statistical units resident in the economies in which they are located in those instances where they are established in different economies from the enterprise that created them. However, the group also acknowledged that such a treatment, while being the best practical approach (especially to deal with asymmetries), may distort economic interpretation of direct investment transactions and positions, especially for economies with significant SPE activity. In noting that the balance of payments cannot be everything to everyone, the group indicated that even greater distortions may result from trying to capture all aspects of SPEs within the balance of payments framework. Accordingly, the group noted that there may be a need for a separate dataset for direct investment to address these problems. Nonetheless, the group recognized that SPEs represent a real economic phenomenon and need to be covered in economic statistics, accordingly.

(ii) The group agreed that physical presence is not necessary for an SPE to be considered a resident in the economy in which it is incorporated/registered, noting that SPEs should not be "looked through". The group agreed that employment, production, technology transfer, etc., are not required for a direct investment relationship to be established. Where there is no physical presence, production, etc., the group agreed that it would be appropriate to classify SPEs as non-bank financial institutions.

(iii) The group considered whether it was worth trying to develop an internationally agreed standard definition of SPEs, but agreed that it would be not be realistic in the time available. However, the group felt that, where material, it would be useful if the compilers in territories that are hosts to SPEs were to identify the SPEs separately on the basis of their own national definitions.

4. Rejected Alternatives:

The meeting rejected the classification of holding companies by institutional sector and industry according to the characteristics of the global group of affiliated enterprises.

5. Questions for the IMF Committee on Balance of Payments (the Committee) and the OECD Workshop in International Investment Statistics (WIIS)

(i) Do the Committee and the WIIS agree that SPEs should be treated as separate institutional units where they are located in different economies from the enterprise that created them? See 3(i) above.

(ii) Do the Committee and the WIIS agree that SPEs should be treated as resident in their territory of incorporation/registration, even in the absence of employment, production, etc.? See 3(ii) above.

(iii) Do the Committee and the WIIS agree with the approach to classify SPEs, where they have no physical presence, employment, or production, to nonbank financial institutions where they are located in different economies from the enterprise that created them? See 3(ii) above.

(iv) Do the Committee and the WIIS agree with the approach to identifying separately SPEs on the basis of national definitions as needed, but not having a standard definition or SPE subsector? See 3(iii) above.

(v) Do the Committee and the WIIS have a view on whether holding companies owning resident enterprises should be classified (a) on the basis of being a holding company or (b) on the basis of the functions of the enterprises it owns? See 3(ii) and 4 above

DIRECT INVESTMENT TECHNICAL EXPERT GROUP (DITEG): OUTCOME PAPER # 10

6 August 2004

1. Topic: Criteria for identifying branches

***2. Issues** – see DITEG Issues Papers #10*

3. Recommendations:

(i) The group agreed that all the criteria listed in the issues paper are to be considered indicative, and that none was felt to be essential (in many instances, it was felt that many on the list may not be present but the unit may still be recognized as a branch). The group felt that an absence of an income statement and a statement of assets and liabilities would make the collection of data for a branch very difficult.

(ii) The group recognized the need for clarification of criteria in the new manual.

(iii) The group agreed that physical presence is not required for financial institutions.

4. Rejected Alternatives:

None

5. Questions for the Committee and the WIIS:

(i) Do the Committee and the WIIS agree that all the criteria listed in issues paper #10 should be regarded as being indicative to determine whether a branch represents a separate institutional unit, or should an income statement and a statement of assets and liabilities be considered necessary? See 3(i) above.

(ii) Do the Committee and the WIIS agree that physical presence is not necessary for a branch operating in the financial sector? See 3(iii) above.