

Expert Group Meeting on Harmonization
of Economic Classifications

DRAFT CLASSIFICATION OF INTERNATIONAL
TRANSACTIONS IN SERVICES

Bureau of Statistics
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I. Introduction

The draft classification of international transactions in services shown in this paper has been prepared in connection with the proposed revision of the fourth edition of the Fund's Balance of Payments Manual, to be undertaken over the next few years. It will be circulated for comment to national balance of payments compilers and will be subject to refinement and modification. In developing this draft, account has been taken of: (a) the recommendations of the Expert Group on External Sector Transactions for the Revision of the SNA; (b) the recommendations of the Group of Balance of Payments Compilers which met in Paris in November 1987; and (c) the work undertaken by the EEC and the OECD in formulating proposals for a classification of international trade in services.

No attempt has been made to provide a general definition of services, as it is felt that this issue is being addressed in other fora, such as the Voorburg Group on Services, that are concerned with the differentiation between commodity flows and service flows in a consistent fashion, both for domestic and international transactions. The draft classification, therefore, is fashioned predominantly on the March 11, 1988 draft of the Central Product Classification (CPC) ESA/STAT/AC.32/5, the distinction between commodities and services broadly paralleling that of the CPC, although some important deviations are noted below.

II. Relationship between the Draft Classification and the CPC

The Expert Group on External Sector Transactions recommended that a standard list of service items should be used as the basis for the harmonization of the classification of services in the Balance of Payments Manual and A System of National Accounts. Those items would include the traditional items shown under services--transport, travel, etc.--and also those items that are becoming increasingly important as international transactions, such as financial services and communications. The details to be shown should agree with the CPC, preferably at a high level of that hierarchy. The Group, furthermore, recommended that those concerned with the CPC classification pay particular attention to the needs of the balance of payments and external sector accounts, so that harmonization between these accounts and other accounts, including input-output, be attainable.

The Group of Balance of Payments Compilers agreed with the need for harmonization and continuity. Although this Group realized that this would cause serious problems of linkage with the CPC, it emphasized the need for the retention of separate items for travel and government transactions. In addition, this Group made a number of suggestions regarding the separate identification and coverage of certain items. Among these were suggestions for the separate identification of processing activities, telecommunications, data-bank services, business and management services, education and health services, motion picture rentals, and radio and television services.

As work on the finalization of the CPC is drawing to a close, this Group suggested that balance of payments compilers should make known their special concerns relating to the classification of international transactions in services. Furthermore, the Group of Compilers emphasized that the Fund and other interested agencies, i.e., the United Nations, the OECD, and the European Communities, coordinate efforts in order to achieve a harmonized

classification of international transactions in services. A revised classification should, as much as possible, take into account the present structure of the main international exchanges of services and their likely future direction. Among the services transactions that received special attention of the Group were the so-called financial leases and service arrangements similar to financial leases, transportation, insurance, and other distributive services on merchandise, and goods for processing and repair.

The categories of service transactions in the draft classification closely parallel the CPC and are based on the nature of services rendered or acquired, i.e., the classification is based on the type of service produced or supplied. The two exceptions to this approach are the groups for travel and government transactions n.i.e., which are based on the consumer of the services and for that reason have no analogues in the CPC.

Travel is treated in this fashion because it is a significant item in the balance of payments statement of many countries and many countries are actually engaged in promoting international tourism. Furthermore, although the Fund's Compensatory Financing Facility initially covered only shortfalls in merchandise export earnings, it was extended in August 1979 to include any shortfalls from travel and workers' remittances. For these reasons, and because of the statistical feasibility of collecting the data, a separate category for the travel item, covering, in addition to services, commodity purchases by travelers for their own consumption or to give away, is provided for in the draft classification. Further dissection of the travel item, which would permit a link to the CPC, could be handled by supplementary tables or satellite accounts.

Government transactions n.i.e. covers outlays of embassies, consulates, and military and other establishments of a foreign government, of diplomatic and consular staff and their dependents in the country where they are stationed, and of international and regional organizations. In addition, government transactions n.i.e. includes public administration and other services provided by governments and extraterritorial organizations.

With respect to financial leases and service arrangements similar to financial leases, both groups agreed that these transactions should be recorded as if a change of ownership of the relevant asset had taken place, rather than as a service transaction. In this context, the groups expressed the view that an international standard for distinguishing between financial and operational leases is needed. In addition, it was generally felt that, until further guidance is forthcoming, the 75 percent cut-off referred to in the Manual should continue to apply in distinguishing between financial and operational leases for international transactions.

Regarding transportation, insurance, and other distributive services on merchandise, the Expert Group agreed that the totals of both imported and exported goods would be recorded in the external accounts on an f.o.b. basis. The coverage of the items for transportation, insurance, and other distributive services on merchandise in the CPC would, therefore, differ from

the corresponding items in the balance of payments and the national accounts for any services on merchandise rendered by residents of the exporting country between the point of delivery of the goods in the exporting country and the border of that country.

As to goods for processing, the Expert Group agreed that both in the balance of payments and in the national accounts, goods exported/imported for processing and re-import/re-export should be recorded gross by the processing economy as well as by the economy that sent the goods for processing. This procedure should be followed if there is a substantial physical change in the goods reflecting a change in their characteristics. The Group also agreed, however, that there is a need for a clear definition in the revised SNA as to what constitutes processing activity. In that context, reference should be made to existing international guidelines on external trade statistics.

Regarding goods for repair, the Expert Group accepted that a distinction should be made between repairs performed on investment goods and repairs performed on other goods. The value of repairs on investment goods should be shown as part of the merchandise item; other repairs should be classified as a service item in both the balance of payments and the national accounts. With respect to the recording of these goods, the Group expressed the need for a review of existing international guidelines for the compilation of external trade statistics.

Finally, regarding the coverage of services in the balance of payments, the Group of Compilers expressed the view that transactions between foreign-owned resident enterprises and domestically-owned resident enterprises should continue to remain outside the scope of the balance of payment of the country where these enterprises are located.

The use of standard components for services and their subdivisions as provided in the draft classification does not preclude countries from developing and reporting details on service transactions along the lines of the subclasses of the CPC. Indeed, the fact that the draft classification is closely aligned with the CPC should facilitate the organization and collection of statistics on service transactions at the national level.

III. Draft Classification of International
Transactions in Services

<u>Proposed Standard Components</u>	<u>GPC</u>
1. Transport and storage services	861, 862, 863, 864, 865, 866, and 867
1.1 Passenger transportation	part of 8611, 8621, 8622, 8641, 8651, and 8661
1.2 Freight transportation and auxiliary transport services	8612, 8613, 8623, 8624, 863, 8642, 8643, 8644, 8652, 8653, 8654, 8662, 8663, 8664, and 867
1.2.1 Freight transportation	8612, 8623, 863, 8642, 8652, and 8662
1.2.2 Rental of transport equipment with crew	8624, 8643, 8653, and 8664
1.2.3 Other transport and storage services	8613, 8644, 8654 8663, and 867
2. Travel	
2.1 Tourism	
2.1.1 Business travelers	
2.1.2 Students and trainees	
2.1.3 Other tourists	
2.2 Other travel	
3. Government transactions n.i.e.	
4. Postal and telecommunication services	868 and 869
4.1 Postal and courier services	868
4.2 Telecommunication services	869
5. Construction services	71

6.	Services incidental to manufacturing	part of 81 and 82, and 843
6.1	Processing (manufacture on a fee or contract basis)	part of 814 and 816
6.2	Repair services	part of 815, 821, and 822 and 843
7.	Trade-related services	83
7.1	Commission agents' services	831
7.2	Merchandising (wholesale trade services)	832
8.	Financial services	871 and 873
8.1	Services of financial intermediation	871
8.2	Services auxiliary to financial intermediation	873
9.	Insurance services	872 and 874
9.1	Life insurance, pension, and annuity services other than compulsory social security	87201 and 87202
9.2	Casualty insurance	87203, 87204, 87205, 87206, 87207, 87208, and 87209
9.3	Services auxiliary to insurance and pension funding	874
10.	Business services	88
10.1	Leasing or rental services without operators	882
10.2	Computer services	883
10.3	Research, development, architectural, engineering, and other technical services	884 and 886

10.4 Legal, accounting, auditing and bookkeeping services; taxation services; market research and public opinion polling services	8851, 8852, 8853, 8854, and 8855
10.5 Management consulting services	8856 and 8857
10.6 Advertising services	887
10.7 Information services	888 and 962
10.8 Other business services	881 and 889
11. Miscellaneous services	811, 812, 813, 817, part of 821 and 822, 823, 841, 842, part of 85, 92, 93, 94, 95, 961, 963, 964, 969, 97, and 98
11.1 Education services	93
11.2 Health and social services	94
11.3 Motion picture, radio and television and other entertainment services	961
11.4 Other miscellaneous services	811, 812, 813, 817, part of 821 and 822, 823, 841, 842, part of 85, 92, 95, 963, 964, 969, 97, and 98

IV. Notes to the Draft Classification of International Transactions in Services

1. Item 1.1, passenger transportation, has the same coverage as the component for passenger services in the fourth edition of the Balance of Payments Manual, i.e., in addition to the services covered by fares, passenger transportation includes any other services for which passengers make expenditures on board carriers or for which they pay charges to carriers, such as those for excess baggage and for personal effects that accompany them, e.g., automobiles.

Passenger services is defined to cover all services performed in transporting passenger between economies, together with those performed within any given economy by a carrier operated by a nonresident enterprise. Services performed within an economy by resident operators are included in item 2, travel.

2. The scope of item 1.2, freight transportation and auxiliary transportation services, is defined in a manner consistent with the valuation of merchandise exports and imports at the customs border of the exporting country. Consequently, certain service transactions are included amongst commodity flows.

As to services not included in merchandise, item 1.2 covers the freight services (a) performed by residents of the compiling country on merchandise and most other movable goods acquired or owned by nonresidents and (b) performed by nonresidents on merchandise and most other movable goods acquired or owned by residents. Such services on passengers' effects accompanying the passengers are included in item 1.1, passenger transportation.

However, as a compiling country would often find it difficult, if not impossible, to ascertain whether its own merchandise exports and imports are actually owned by a resident or by a nonresident at the time the services are being performed, the Manual recommends a convention for constructing the entries that refer to the transportation of the compiling country's merchandise beyond the customs frontier of the exporting country. Under that convention certain offsetting transactions between residents and foreigners may in effect be netted against each other, while certain transactions between residents or between foreigners may be included in the statistics.

3. Item 1.2.2, rental of transport equipment with crew, refers to the service provided by owners in hiring or leasing their carriers to the enterprises that operate them and includes single voyage charters.

4. Item 2, travel, covers the services, other than the international carriage of travelers included in item 1.1, acquired from an economy by travelers during their stay in that economy to use themselves or give away.

In addition to the services covered by division 85, hotel and restaurant services, of the CPC, this item may also include services covered by other divisions of the CPC. However, this item does not include passenger transportation, which is covered in item 1.1.

5. Item 3, government transactions n.i.e., covers outlays of embassies, consulates, and military and other establishments of a foreign government, of diplomatic and consular staff and their dependents in the country where they are stationed, and of international and regional organizations. In addition, government transactions n.i.e. includes public administration and other services provided by governments and extraterritorial organizations.

6. Item 6.1, processing, refers to processing services that do not bring about a substantial physical change in the goods reflecting a change in their characteristics.

7. Item 6.2, repairs, refers to repair services on goods other than investment goods.

8. Item 7.2, merchanting, covers the difference between the value of goods acquired from one economy and the value of the same goods relinquished to that or some other economy without the goods ever crossing the frontier of the economy in which the temporary owner is a resident.

9. Item 9, insurance services, covers the services rendered under insurance or pension schemes. The Expert Group on External Sector Transactions has agreed, however, that it would be inappropriate to suggest recommendations regarding the measurement of those services until a full evaluation of the treatment of the complex of insurance transactions, including those related to life insurance and pension funds, is in place.

10. Item 9.2, casualty insurance, is defined in a manner consistent with the valuation of merchandise exports and imports at the customs border of the exporting country. Consequently, the cost of insurance up to the border of the exporting country is included in merchandise exports and imports.

As to services not included in merchandise, item 9.2 includes the insurance services (a) performed by residents of the compiling country on merchandise and most other movable goods acquired or owned by nonresidents and (b) performed by nonresidents on merchandise and most other movable goods acquired or owned by residents.

However, as a compiling country would often find it difficult, if not impossible, to ascertain whether its own merchandise exports and imports are actually owned by a resident or by a nonresident at the time the services are being performed, the Manual recommends a convention for constructing the entries that refer to the insurance of the compiling country's merchandise beyond the customs frontier of the exporting country. Under that convention certain offsetting transactions between residents and foreigners may in effect

be netted against each other, while certain transactions between residents or between foreigners may be included in the statistics.

11. Item 10.1, leasing or rental services without operators, covers leasing other than financial leasing. Financial leasing is defined as a leasing arrangement expected to cover at least three fourths of the cost of the goods, together with the carrying charges. Thus, financial leasing refers to a transaction in which the effect of a legal change of ownership is achieved without such a change taking place.

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