

Draft Classification of International
Transactions in Services

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I. Introduction

The Draft Classification of International Transactions in Services, hereinafter referred to as the Draft Classification, was initially prepared by the Fund's Bureau of Statistics in 1988 in connection with the work on the revision of the fourth edition of the Fund's Balance of Payments Manual (BPM). It is intended primarily to fill a widely felt gap in the existing classification of international trade in services in the framework of the balance of payments. Although the share of services in total international trade has increased in the 1980s, all international trade classifications have dealt exclusively with the classification of goods. The classification systems that include services such as the International Classification of Goods and Services (ICGS) and the Central Product Classification (CPC) are primarily oriented towards domestic transactions rather than international transactions.

The Draft Classification has had the benefit of comments from the Expert Group Meeting on Harmonization of Economic Classifications (April 1988), the Group of Balance of Payments Compilers (November 1987), as well as the statistical offices of the European Communities (EC), the Organization for Economic Cooperation and Development (OECD), and the United Nations Statistical Office (UNSO). The revised version of the Draft Classification (Appendix I) takes account of the above-mentioned comments and the recommendations of the Expert Group on External Sector Transactions for the revision of the SNA as well as the work undertaken so far by regional and international agencies such as the EC, the OECD, the UNSO and the IMF. The draft classification represents a tentative proposal for the classification of services as an integral part of the balance of payments and serves as the basis for further work in the revision process of the BPM. Consequently, comments are still being received from national statistical offices. The final version of the Draft Classification will take into account these views as well as those of the participants in the present meeting of the Voorburg Group. Following decisions taken in the Expert Group on External Transactions as to the borderline between goods and services, Appendix I provides details on the coverage of these flows in the balance of payments.

The plan of the remainder of this paper is as follows:

Section II will outline the objectives and the scope of the Draft Classification; section III will deal briefly with issues surrounding a workable definition of services; section IV will try to provide a rationale for the analytical categories chosen for the Draft Classification, particularly in relation to its conformity with the CPC and other classifications; and section V will give a short summary of the paper. Appendix I shows the Draft Classification and Appendix II provides an explanatory note on the items in the Draft Classification.

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II. Objectives, Nature, and Scope

1. Objectives

A general objective of any data classification system is to provide a coherent framework for the compilation of data with due regard to both the analytical needs of users and data collection requirements of compilers. In addition, the Draft Classification aims at facilitating international comparisons of traded and tradeable services. Finally, the classification seeks to serve as an international standard that would have the flexibility to accommodate the diverse statistical needs and capacities of countries at different stages of statistical development. In this connection, it needs to be stressed that the development of a classification of international transactions in services for purposes of international reporting of balance of payments data does not preclude countries from developing more elaborate and detailed breakdowns of component items; indeed, for statistically advanced countries, the Fund would request and store data in the degree of detail that such data are available and published by these countries.

2. Nature and scope

The classification makes provision for all traded and tradeable services although, it is not as detailed as the CPC mainly because CPC includes non-traded services. Meaningful analytical categories are formed by combining appropriate items that may be comparatively insignificant in international trade although they may be important in domestic transactions. The needs of multilateral trade negotiations are also taken into account.

The scope of the Draft Classification is restricted to nonfactor services, excluding such flows as airport taxes (treated as transfer payments in the SNA) as well as any factor income flows. The classification is hierarchical and can be expanded or contracted according to the needs and circumstances of the compiling country.

III. Difference Between Goods and Services

Although a precise distinction between goods and services is largely of theoretical interest, it is necessary to have at least a workable definition of services in the case of a classification system that deals only with services, because it would be confusing to place items that are generally regarded as goods in that classification. Also, differences in international trade between goods and services may have different implications for economic analysis and policy making, an issue highlighted by current multilateral trade negotiations. Moreover, because of the

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growing importance of international trade in services, it is necessary to distinguish between exports and imports of goods and services.

From available writings and discussions on this subject, ^{1/} it appears that a number of criteria have been suggested to distinguish between goods and services in different circumstances. For example, direct and immediate contact between the producer and the user has been emphasized as a hallmark of service as distinct from goods which could be produced and sold to an intermediary or stored without knowing who would use them. Similarly, tangible versus intangible, storable versus non-storable, or transportable versus non-transportable have been used as distinguishing features between goods and services. Although most of these criteria may be applicable in the majority of cases, there are numerous borderline cases that require judgmental decisions as to the classification. Borderline cases are exemplified by items such as photographs, computer tapes, and meals or drinks in restaurants. Other examples are goods in which some services become embodied when the goods are insured and transported, or are subject to repairs.

IV. A Rationale for the Draft Classification

1. Principles used in constructing the Draft Classification

The principles underpinning this classification system are derived from the recommendations of the Expert Group on External Transactions (March/April 1987) to the effect that a standard list of service items be used as the basis for the harmonization of the classification of services in the BPM and the SNA. Such a list should include the traditional items shown under services such as transport, travel, etc. as well as items that are becoming increasingly important in international trade (e.g., financial services and communications). The classification should be compatible with the CPC, preferably at a high level of that hierarchy. The Group further recommended that the CPC provide for the needs of both the balance of payments and external sector accounts of the SNA, so that harmonization between these accounts and other accounts, including input-output, be attainable.

The Group of Balance of Payments Compilers (November 1987) agreed with these guidelines and went further in emphasizing the need for the retention of separate items for travel and government transactions. In addition, this Group suggested separate identification and coverage of processing

^{1/} See "Final Expenditures and Uses" a chapter of revised SNA, May 1989 (mimeo) and UN Secretariat, Final Draft of the Central Product Classification (CPC), September 1988.

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activities, telecommunications, data bank services, business and management services, education and health services, motion picture rentals, and radio and television services.

As can be seen in Appendix I, the Draft Classification has embodied the basic principles underlying the above recommendations. In classifying different services, particular attention is given to their nature and production process. It has attained harmonization with the SNA (under revision) and close correspondence to the CPC (the exceptions will be noted shortly). It is also broadly compatible with the proposed Joint OECD-EUROSTAT Trade-in-Services Classification (see OECD TD/TC/WP (90) 43, Paris, 11th July 1990). However, the Draft Classification is more aggregated than the CPC and the OECD/EUROSTAT proposal in light of comments received from a large number of compilers who emphasized the need for a compromise between details and the statistical needs and capacities of a majority of users and compilers respectively. In addition to meeting present needs, the classification also provides for needs that can be realistically expected to emerge in the foreseeable future. Thus, in aggregating detailed categories, the Draft Classification has tried to ensure that analytically meaningful categories are retained.

2. STRUCTURE AND CODING SYSTEM OF THE DRAFT CLASSIFICATION

The structure of the Draft Classification is hierarchical and its coding system decimal, as in the CPC. Its categories have been built up from the sub-classes (five-digit codes), classes (four-digit codes), groups (three-digit codes), and divisions (two-digit codes) of the CPC, although the Draft Classification seeks correspondence with CPC at the three-digit level.

The Draft Classification is flexible insofar as each three-digit category can be expanded into as many as nine sub-categories. This could be done by appending one decimal place to the three-digit code which represents the most detailed category in this classification. Similarly, if some countries do not want as much detail, the three-digit categories could be compressed into two-digit categories.

3. Deviations from the CPC

As mentioned earlier, the Draft Classification closely follows the CPC and is based on the nature of services rendered or acquired. The two exceptions to this approach are the categories for travel and government transactions n.i.e., which are based on the consumer of the services and therefore have no corresponding categories in the CPC.

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Travel is treated in this manner because data are collected from the consumers of these services and most countries present the data in this form in their balance of payments statements. This treatment is also helpful to the national authorities that are engaged in promoting international tourism. Thus, keeping in mind the feasibility of collecting data, a separate category for travel covering, in addition to services, purchases of goods by travelers for their own consumption or for donating to others is provided for in the Draft Classification. However, if a direct link to the CPC for this item is considered necessary, this could be done through further disaggregation of "Travel" in a supplementary table or a satellite account.

Government n.i.e. represents consumption of goods and services by 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. This category also includes public administration and other services provided by governments and extraterritorial organizations.

Another departure from CPC is that, while CPC treats all processing and repairs as service items, the Draft Classification classifies only minor processing and repairs on non-investment goods as service categories. Major processing and repairs on investment goods are considered as being embodied in the goods processed and repaired respectively. This treatment reflects the recommendation of the Expert Group on External Sector Transactions. The Draft Classification defines major processing as the transformation of goods to such an extent that after processing it would be classified in a different group of the CPC. In other words, when goods are returned after minor processing, e.g., packaging, sorting, or grading, they should be classified in the same group of the CPC as before they were sent abroad and the amount of value added would be considered as a service transaction.

4. Proposal for a Joint OECD-EUROSTAT Trade-in-Services Classification

This proposal (referred to as the Joint Proposal hereinafter) is scheduled for discussion at the joint OECD-EUROSTAT Meeting of Balance of Payments Experts to be held ~~during~~ November 8-9, 1990 in Paris (see OECD TD/TC/WP (90) 43, 11th July 1990). It is fully compatible with the Fund's Draft Classification at the one-digit level. It is also linked to the CPC, but the linkage has been kept tentative and flexible mainly because the CPC is geared more to domestic than to international transactions and it is still in the process of elaboration with some of the explanatory notes remaining incomplete or unavailable.

The Joint Proposal is more elaborate than the Draft Classification in some respects. In the transportation category, the Joint Proposal has a

number of additional items, such as "Land Transport" with a further breakdown of "Rail Transport," and "Space Transport," and "Supporting and Other Services." Similarly, it has inter alia a breakdown of communications into postal, courier, and telecommunication services (see Appendix II of the Joint Proposal).

Other major differences between the Joint Proposal and the Draft Classification include a larger list of repair and processing items in the merchandise part of the former, while the latter includes most of these items in services (e.g., all repairs except those on investment goods). While the Joint Proposal includes all processing in merchandise with the exception of on-site processing and processing giving rise to an export followed by an import (or vice versa), the Draft Classification treats processing as part of merchandise only if the character of the good is changed enough to warrant its classification in another group of the CPC. Furthermore, merchandising transactions are included in the merchandise item in the Joint Proposal, while they are included as part of other business services in the Draft Classification.

V. Summary

The Draft Classification is compatible with the CPC at the three-digit level and with the Joint OECD/EC proposal broadly at the one-digit level and in some cases at the three- or four-digit level. It can be expanded or contracted according to the needs and the circumstances of national compilers.

In preparing the Draft Classification, the IMF Bureau of Statistics has sought and received active cooperation from other international and regional organizations as well as national compilers. The present version reflects comments already received and the final version will give due consideration to the views expressed at this meeting and those of other international fora and national authorities that might be available later.

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APPENDIX I

Balance of Payments: Classification of International
Transactions in Goods and Services

Current account

| | <u>Section</u> | <u>CPC 1/ Division</u> | <u>Group</u> | <u>Class</u> |
|--|----------------|----------------------------|--------------|---|
| Goods and services | | | | |
| a. Goods | | | | |
| 1. Merchandise | | | | |
| 2. Goods for processing (involving substantial physical change of goods) | | | | |
| 3. Repairs of investment goods | | | | |
| 4. Procurement of goods in ports by carriers | | | | |
| b. Services | | | | |
| 1. Transportation | 7 | | | |
| 1.1 Sea transport | | | | 721+Part of 745 |
| 1.1.1 Passenger | | | | 7211 |
| 1.1.2 Freight | | | | 7212 |
| 1.1.3 Other | | | | 7213+7214+ Part of sea-going vessels in 745 |
| 1.2 Air transport | 73 | | | |
| 1.2.1 Passenger | | | | 731 |
| 1.2.2 Freight | | | | 732 |
| 1.2.3 Other | | | | 733+734+746 |
| 1.3 Other transport 2/ | | | | |
| 1.3.1 Passenger | | | | |
| 1.3.2 Freight | | | | |
| 1.3.3 Other | | | | |
| 2. Travel | ... | | | |
| 2.1 Business and professional | ... | | | |
| 2.2 Pleasure | ... | | | |

1/ Section = One-digit; Division = Two-digit; Group = Three-digit;
Class = Four-digit.

... No correspondence.

2/ Comprises the following groups of the CPC, viz., 711, 712, 713, 722,
741-744, part of 745, and 747-749.

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APPENDIX ICurrent account

| | | <u>CPC 1/</u> | | |
|---|----------------|-----------------|-----------------------|----------------------|
| | <u>Section</u> | <u>Division</u> | <u>Group</u> | <u>Class</u> |
| 2.3 Students and trainees | ... | | | |
| 2.4 Other | ... | | | |
| 3. Communications | | 75 | | |
| 4. Construction services | | 51 | 511-518 | |
| 5. Insurance services | | | 812+814 | |
| 5.1 Life insurance 2/ | | | | |
| 5.2 Other insurance | | | | 8129+Part of 8121 |
| 5.3 Auxiliary services | | | 814 | |
| 6. Financial services (other than insurance) | | | | |
| 6.1 Financial intermediation | | | 811 | |
| 6.2 Auxiliary to financial intermediation | | | 813 | |
| 7. Computer and related services | | 84 | | |
| 8. Other business services 3/ | | | | |
| 8.1 Trade-related | | 62 | | |
| 8.2 Leasing or rental without operators | | 83 | | |
| 8.3 Research and development | | 85 | | |
| 8.4 Legal | | | 861 | |
| 8.5 Accounting, auditing, and taxation | | | 862-863 | |
| 8.6 Management consulting | | | 865 | |
| 8.7 Architectural, engineering, and other technical | | | 867 | |
| 8.8 Advertising, market research, and public relations | | | 864+871 | |
| 8.9 Other | | | 866, 872-879, 881-887 | |
| 9. Other personal services | 9 | | | |
| 9.1 Educational | | 92 | | |
| 9.2 Health | | 93 | | |
| 9.3 Recreational, cultural, and sporting | | 96 | | |
| 9.4 Other | | 97 | | |
| 10. Government, n.i.e. | ... | | | |

1/ Section = One-digit; Division = Two-digit; Group = Three-digit;
Class = Four-digit.

... No correspondence.

2/ Life insurance has correspondence to CPC at the 5-digit level
(subclass) only.

3/ Comprises the following divisions of the CPC, viz., 62, 83, and 85-88.

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Notes to the Draft Classification of
International Transactions in Services

1. Passenger transportation has the same coverage as the component for passenger services in the fourth edition of the Balance of Payments Manual (BPM), 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 transportation services are 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 freight transportation and the "other" category which covers auxiliary transportation services such as storage and handling 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, freight 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 passenger transportation.

3. Travel covers the services, other than the international carriage of travelers included in passenger transportation, acquired from an economy by travelers during their stay in that economy to use themselves or give away. It includes expenditures of students other than on educational and health services as well as expenditures in the domestic economy by nonresident workers.

In addition to the services covered by division 64, 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 items 1.1.1, 1.2.1, and 1.3.1.

4. 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.

5. Insurance services cover the services rendered under insurance or pension schemes and the whole complex of insurance transactions, including those related to life insurance, casualty insurance, and pension funds.

Item 5.2, Other insurance, represents pension and annuity services, accident and health insurance services, as well as non-life insurance services.

6. Item 8.2, leasing or rental services without operators, covers leasing other than financial leasing. The revised SNA (Draft) imputes a change of ownership from lessor to lessee in the case of a financial lease although legally change of ownership takes place only at the termination of the lease. This treatment is justified by the fact that the lessee assumes all the rights, risks, and responsibilities of ownership in practice at the commencement of the lease. The revised BPM will adopt this definition of financial lease.