13 Primary Income

Introduction

13.1 Primary income represents the return that accrues to resident institutional units for their contribution to the production process or for the provision of financial assets and renting natural resources to nonresident institutional units. Primary income includes the following components:

(1) Income Associated with the Production Process
   (a) Compensation of employees
   (b) Taxes and subsidies on products and production.

(2) Property Income
   (a) Investment income:
      - Dividends and withdrawals from income of quasi-corporations
      - Reinvested earnings
      - Interest
   (b) Rent.

13.2 Further grouping of primary income is discussed in the subsequent sections.

Compensation of Employees

13.3 Compensation for employment may be earned by persons residing in economies that differ from the economies in which they are employed on a short-term basis (for less than one year) and also by persons residing in their own economies but employed by a nonresident company established in the economy of these persons or by foreign government enclaves located in this economy. The former would include earnings of border, seasonal, and other short-term workers resident in one economy paid by an employer resident in another economy that are in an employer-employee relationship. The latter would include compensation paid by foreign embassies, foreign military establishments, and international institutions to residents of the economies in which the embassies and so forth are located.

13.4 The existence of an employer-employee relationship is central in determining whether the remuneration received by short-term workers is treated in the balance of payments as compensation of employees or as fees for services. The identification of an employer-employee relationship requires good knowledge of the type of activity conducted by resident workers outside their economy (e.g., construction, housekeeping, agriculture work, etc.) and type of agreement between such workers and the institutional unit for which they work. The first characteristic that indicates that the employer-employee relationship exists is whether the employer has the right to control or to direct what shall be done and how it shall be done. However, certain control on the work also exists when the work is provided by a self-employed person. Other characteristics of the existence of employer-employee relationship are existence of an agreement (formal or informal) between the employer and employee into which they enter voluntarily and when the remuneration is based on either the time spent at work or some other objective criteria. Additional criteria that could help determine if an employer-employee relationship exists are: payment of social contributions by the employer as well as the entitlement of the employee to the benefits that usually are provided to employees by a company (e.g., certain types of allowances, holidays, and sick leave).

13.5 If an individual is contracted to produce a certain amount of work or a given result, this suggests that the individual is self-employed and is selling services. An individual is deemed to be self-employed if: he/she operates his/her own unincorporated company and therefore sells its output; he/she is responsible for the scale of operations and finances, owns or rents machinery for the work; pays social contributions by himself/herself; pays taxes on the provision of services; and so forth.

13.6 Several types of services, such as construction, agricultural services, and software development, can raise questions about the borderline between compensation transactions and sales of services. For instance, if a worker is hired by a nonresident employer to undertake long-term construction activity and the worker is paid regular remuneration measured by the time spent at the work, the remuneration should be treated as compensation of employees. However, in many cases an employer contracts a nonresident individual to conduct a certain amount of construction work with a certain result. The contracted individual, in turn, may conduct the work by subcontracting to other nonresident workers. The first contracted individual pays a lump sum to the second contracted individual for the agreed amount of work, and the second individual further pays to subcontracted nonresident workers the remuneration for the provided work. If the contracting parties are residents of the same economy, the transactions between them are beyond the balance of payments scope. When the contracted individual is deemed to be selling construction services to nonresidents, the remuneration received should be registered in balance of payments as construction services.

13.7 When an employer-employee relationship exists, it may also be important to identify which institutional unit is the employer of the worker, and if this employing unit is resident or nonresident of the compiling economy. This may be particularly challenging when an employment agency is involved in the transaction.

13.8 Compensation of employees includes compensation paid in kind, as well as that paid in cash. Transactions under this item should be recorded on a gross basis—that is, before any deductions for expenses (such as income taxes and acquisition, by the employee, of goods and services in the host economy). These expenses should be recorded under appropriate balance of payments items. Example 13.1 may help clarify the treatment of compensation of employees.

Example 13.1 Recording of Compensation of Employees in Balance of Payments

A resident of economy A works for three months in economy B and earns US$500 in cash before tax. In addition, the employer provides accommodation estimated to be worth US$100. The worker pays income tax of US$70 to the government of economy B. Additionally, the worker contributes with US$50 to a social security scheme in economy B and spends US$130 on clothing and food during his stay in economy B. The following entries would appear in the balance of payments of economy A:

Current account	Credit	Debit
Services		
Travel		
Business		230[1]
Acquisition of goods and services by border, seasonal, and other short-term workers		230
Primary income		
Compensation of employees	600[2]	
Secondary income		
Other current transfer		120
Current taxes on income, wealth, etc.		70
Social contribution		50
Financial account	**Net acquisition of financial assets**	**Net incurrence of liabilities**
Other investment		
Currency and deposits	+250[3]	

[1]Includes 130 for clothing and food and 100 for accommodation.
[2]500 paid in cash *plus* 100 for accommodation paid in kind.
[3]500 paid in cash *minus* 70 income tax *minus* 50 contribution to social security scheme *minus* 130 spent on clothing and food.

13.9 Credits for compensation of employees have two distinct components: (1) compensation earned by residents working for institutional units abroad and (2) compensation earned by local staff working for foreign embassies and similar institutions—including international organizations—and by local staff working for nonresident institutional units operating in the compiling economy. Likewise, debits for compensation of employees have two distinct elements: (1) compensation earned by nonresidents working for resident institutional units of the compiling economy and (2) compensation earned by local staff working for the compiling economy's foreign embassies and similar institutions located abroad and by local staff working for resident institutional units that have an activity

abroad. The balance of payments compiler should be aware of each of these components because a collection methodology well suited to measuring one component may not be appropriate for measuring another.

13.10 The compensation of employees net of taxes, social contributions, and other expenses made by the short-term workers in host economies is included, along with personal transfers and capital transfers between households, in the value of personal remittances (see *BPM6*, paragraph 12.27).

Data Sources

13.11 Compensation of employees is typically measured by using one or more of the following sources: an international transactions reporting system (ITRS), enterprise surveys of employers, surveys of travelers, official sources, surveys of embassies, and partner economy data. More about data sources that could be employed for collecting and/or estimating compensation of employees is presented in *International Transactions in Remittances: Guide for Compilers and Users* (IMF, 2009).

International transactions reporting system

13.12 An ITRS may provide satisfactory coverage of compensation of employees sent by residents working abroad or of nonresidents working in the compiling economy. However, the compiler should understand that amounts reported in ITRS for compensation of employees are on a net basis that does not include expenses in the host economy. The compiler should attempt to estimate gross amounts. Also, the data collected through an ITRS on compensation of employees could include misclassifications, because the ITRS reporters cannot accurately identify if workers are in an employer-employee relationship and also if they work in the host economy for more than or less than one year.

13.13 The compiler might use an alternative source, such as a survey of travelers, to make the estimate.[1] For example, in order to estimate the gross amount of compensation of employees, the compiler might establish percentages of compensation for employment that relate to income tax payable to the host economy's government, to contributions to social and pension schemes, to goods and services acquired in the host economy, and to the net amount retained by the employee. Net amounts reported in an ITRS could then be expanded by using relevant percentages, and appropriate offsetting entries for transfers and travel could also be calculated. For example, the balance of payments compiler might establish that, for residents working abroad, 10 percent of compensation is paid in taxes and social contributions, 15 percent is spent on goods and services, and the remaining 75 percent is remitted to the compiling economy and recorded in an ITRS. Credits for total compensation of employees would be equal to the ITRS figure multiplied by 1.33 (grossed up from 75 percent). Transfer and travel debits would be equal to 10 and 15 percent, respectively, of estimates of gross compensation of employees.[2]

13.14 In order to adjust the ITRS data for misclassifications already mentioned, the compiler might use variables collected through a survey of travelers, migration survey, or a specialized survey of remittances. Such variables are the existence of a cross border employer-employee relationship and the duration of stay in host economy, by pattern of surveyed workers.[3]

13.15 Use of an ITRS to measure compensation of employees will omit compensation paid in kind. Such compensation could be identified by using surveys of travelers, household surveys, or enterprise surveys (for debits only). However, the compiler should be aware of limitations of each type of survey related to data on remittances, including compensation of employees. To improve the coverage of information on remittances collected through surveys, the compiler should make efforts to include additional questions in surveys that would provide useful information for estimating remittances by components. For example, questions on the existence of an employer-employee relationship, on type of remittances received (in cash or in kind), or on channel of remittances (banks, money transfer operators, or informal channels such as bringing money in-pocket, hawala, etc.) could be added to a survey of travelers or to a migration survey. This would bring a great improvement to the estimates of compensation of employees and remittances-related balance of payments components.

[1] The survey of travelers is discussed in more detail in Chapter 3.

[2] For best results, separate percentages should be calculated for nonresidents working in the compiling economy and for residents working abroad.

[3] For more information on types of surveys employed in estimating remittances data, see Chapter 4 of the *International Transactions in Remittances: Guide for Compilers and Users* (IMF, 2009).

13.16 The compiler should ensure that compensation for employment paid to local workers by foreign embassies and similar institutions and by companies that are not residents of the economies in which they are located (e.g., construction companies engaged in short-term projects) is not "bundled" with other balance of payments transactions. For example, an ITRS may record amounts transferred to cover expenses of the compiling economy's foreign embassies. It is important that amounts used to pay local staff be recorded separately from other expenses. If this is not the case, supplementary sources (such as official sources in the case of embassies located abroad; surveys of embassies in the case of foreign embassies in the compiling economy; or enterprise surveys in the case of companies operating in economies in which they are not resident) could be used to provide necessary balance of payments information.

Surveys of employers

13.17 Surveys of employers could be useful sources of information on compensation payable by resident companies to nonresident employees and on compensation payable to local employees by nonresident companies located in the compiling economy.[4] The main advantages of using surveys of employers are that amounts are typically recorded on a gross basis, and compensation paid in kind can often be readily reported. The disadvantages of using surveys of employers are the amount of effort required to maintain coverage; the lack of information on credits for compensation of employees earned by residents working abroad and on compensation paid to local staff of embassies and so forth; difficulties in identifying nonresidents who are short-term workers residing temporarily in the economy from the company accounting system; and the expense of conducting a separate collection to measure what is, for some economies, a relatively trivial item in the balance of payments. Of course, collection expenses might be greatly reduced if the information were collected as part of a general approach that used enterprise surveys to compile balance of payments statistics.

Surveys of travelers

13.18 As well as collecting information on travel expenditure, surveys of travelers[5] could be used to collect information on compensation earned by travelers. The main advantage of using this source is that it collects data directly from workers on a timely basis, and therefore the mistakes due to memory recall would be avoided. The disadvantage to using a travelers' survey is that supplementary data sources would be needed to capture information on compensation payable to local staff of foreign embassies and so forth, and on compensation payable to local staff working for companies operating in economies other than those in which the companies are resident.

Official sources

13.19 Official sources may be able to provide useful information on compensation payable to the local staff of the compiling economy's embassies and so forth located abroad. Also, some economies have official agencies responsible for nonresidents working in the economy or for residents working abroad. These agencies could have information that would be useful for compiling the compensation of employees item in the balance of payments. In addition, administrative data on the number of work visas issued by the compiling economy's government could be used to estimate the number of cross border commuters, seasonal, and other short-term workers.

13.20 Also, the border authorities in some economies may conduct studies on the economic impact of border crossers and for this purpose collect information on number of daily commuter workers. This information could be useful for estimating the compensation of employees of border workers. The main disadvantage in using data from the border authorities is that such a survey is not conducted on a regular basis.

Surveys of embassies and so forth

13.21 Surveys of foreign embassies and similar institutions, including international organizations, located in the domestic economy could be a good source of information on compensation payable to

[4]Such surveys are discussed in Chapter 3, "Collections on Goods and Services Statistics."

[5]For information on this survey, see Chapter 3, "Collections from Persons and Households."

resident staff working for these institutions.[6] Even if only a subset of embassies responds to such surveys, there may be reasonable information on per capita salary and so forth, which could then be multiplied by the number of local staff working for foreign and international institutions in order to obtain an overall estimate. Information on staff employed by these institutions should be available from an economy's ministry for external affairs or from similar government organizations.

Partner economy data

13.22 In some economies, partner economy data may be the best source of information on compensation of employees (particularly credits). Alternatively, partner economy data could be used as a check on estimates derived from other sources. However, the compiler should assess the data collection and the estimation techniques employed by the partner economies in order to assure that those data are reliable.

Data Models and Extrapolations

13.23 In the absence of complete data, a data model or models could be used to estimate part or all of the compensation of employees. The use of most data models involves multiplying estimates of numbers of employees by estimates of per capita compensation. The numbers of residents in an employer-employee relationship abroad and of nonresidents in an employer-employee relationship in the domestic economy could be available from migration statistics or from an official source, such as a relevant government agency. Estimates of per capita compensation could be based on benchmark studies and adjusted for growth occurring in wages after the period of the study and for any other necessary factors. The estimates could also be based on other related indicators, such as the average earnings of employees in the compiling economy. This indicator could be used for deriving estimates of compensation paid to nonresidents in an employer-employee relationship in the compiling economy or compensation paid to local staff of foreign embassies and so forth. In addition, such estimates could be based on the average earnings of employees in partner economies. This indicator could be used for deriving estimates of compensation paid to residents in an employer-employee relationship abroad or compensation paid to local staff of the compiling economy's embassies and similar institutions abroad.

13.24 Extrapolations of compensation of employees generally involve similar techniques. When numbers of employees are extrapolated, provision should be made for any known or expected developments taking place in the compiling economy (or in partner economies) and having a potential impact on these numbers. Likewise, when per capita compensation estimates are extrapolated, account should be taken of known or expected developments in wages and, when relevant, exchange rates.

Investment Income

Introduction

13.25 Investment income is income derived from ownership of external financial assets and payable by residents of one economy to residents of another economy. The structure of the investment income account is consistent with that of the corresponding financial flows and positions, thus facilitating the analysis of rates of return. Most financial instruments give rise to investment income. Debt instruments such as SDRs, loans, most debt securities, and deposits (including unallocated gold accounts) give rise to interest. Equity and investment fund shares give rise to dividends or other distributions from corporate income. Gold bullion, currency, noninterest bearing deposits, financial derivatives, and employee stock options never give rise to investment income.

13.26 Investment income is broken down by the following components for purposes of compilation (not in *BPM6* standard component sequence):

- Pure interest (excluding financial intermediation services indirectly measured (FISIM))
- Distributed income of corporations:
  - Dividends on equity other than on investment fund shares
  - Withdrawals from income of quasi-corporations
  - Reinvested earnings on foreign direct investment other than on investment funds

[6] These surveys are described in Chapter 3, "Collections on Goods and Services Statistics."

- Other investment income:
  - Investment income attributable to insurance policyholders
  - Investment income payable on pension entitlements and standardized guarantees
  - Investment income attributable to investment fund shareholders
- Dividends
- Reinvested earnings.

13.27 Investment income should be classified by financial account functional categories: direct investment, portfolio investment, other investment, and reserve assets. Direct investment income should be classified by dividends and withdrawals from income of quasi-corporations, reinvested earnings (including investment income attributable to investment fund shareholders that are in a direct investment relationship), and interest. These components, except for reinvested earnings, are further subdivided by counterpart—that is, direct investors, direct investment enterprises (DIENTs), and fellow enterprises. In supplementary classifications for fellow enterprises, the ultimate controlling parent is identified as resident or nonresident in the compiling economy, or as unknown. A supplementary item provides direct investment income attributable to policyholders in insurance, pension, and standardized guarantee schemes, and to investment fund shareholders, with a separate classification of investment income attributable to investment fund shareholders.

13.28 Portfolio investment income should be classified by dividends on equity other than investment fund shares, investment income attributable to investment fund shareholders (subdivided into dividends and reinvested earnings), and interest on debt securities by maturity (i.e., short-term and long-term).

13.29 Other investment income is classified by income on equity and investment fund shares that are not classified in any other functional categories, interest, and income attributable to policyholders in insurance, pension, and standardized guarantee schemes.

13.30 Income on reserve assets is classified by income on equity and investment fund shares and interest.

13.31 Interest before FISIM should be disclosed as a memorandum item for direct investment, other investment, and reserve assets.

13.32 Close relationships often exist among investment income, transactions in external financial assets and liabilities (the financial account of the balance of payments), and positions of these assets and liabilities (the international investment position—IIP). Because of these relationships, investment income estimates are often compiled from sources similar to those used to compile the financial account and the IIP. Accordingly, it may be helpful to refer to Chapter 9 in conjunction with the Investment Income part of this chapter.

Data Sources

13.33 Surveys of companies (including financial corporations) with external assets and liabilities, an ITRS, or official sources can be used to measure balance of payments transactions in investment income. Whatever approach is used, collection and estimation methods should be well designed to ensure that investment income is measured accurately. Table 13.1 summarizes the possible compilation strategies available to the compiler.

13.34 Enterprise surveys may be selective (e.g., concentrating only on financial corporations or companies in direct investment relationships) or broadly based (e.g., covering nearly all companies with external assets and liabilities). Primary income should be recorded on a gross basis—that is, before the deduction of financial fees and withholding taxes. It is important that enterprise survey collection forms be well designed, that reporters have a good understanding of the collection requirements, and that close contact is maintained between the compiler and survey respondents. Enterprise surveys may include collections from financial intermediaries that report data on income from securities.

13.35 Data on investment income, such as income related to official debt and reserve assets, could also be obtained from official sources. The official debt office may also have information on interest payable by other sectors of the economy, particularly when interest payments are guaranteed by the government. Some economies require, either as part of foreign exchange controls or foreign investment approval procedures, that companies submit applications to remit profits. These applications could be used to estimate some components of investment income, but be aware that applications may not always materialize into actual remitted profits.

Table 13.1 Compilation of Investment Income and Other Primary Income Items

Description	Source and method of compilation
Direct investment income Income on equity and investment fund shares Dividends and withdrawals of income from quasi-corporations Direct investor in direct investment enterprise Direct investment enterprises in direct investor Between fellow enterprises *If ultimate controlling parent is resident* *If ultimate controlling parent is nonresident* *If ultimate controlling parent is unknown* Reinvested earnings *Investment income attributable to policyholders in insurance, pension, and standardized guarantee schemes, and to investment fund shareholders* Interest Direct investor in direct investment enterprise Direct investment enterprises in direct investor Between fellow enterprises *If ultimate controlling parent is resident* *If ultimate controlling parent is nonresident* *If ultimate controlling parent is unknown* Memorandum: Interest before FISIM	Data on dividends and withdrawals of income from quasi-corporations, together with interest, can be collected through enterprise surveys or an ITRS. In either case, care should be taken to ensure that noncash income is collected. However, the compiler should be aware of the limitations of ITRS in collecting such datafor example, reporters might have difficulties in identifying the counterpart (direct investor, direct investment enterprise, or fellow enterprise), as well as the location of the ultimate controlling parent. Data on reinvested earnings can be collected as a supplement, in enterprise surveys, in an ITRS, or sometimes as a by-product of a foreign exchange or foreign investment approval system. Data on investment income attributable to policyholders in insurance, pension, and standardized guarantee schemes, and to investment funds shareholders can be collected through a survey of companies involved in such activity—e.g., insurance companies.
Portfolio investment income Income on equity and investment fund shares Dividends on equity excluding investment fund shares Investment income attributable to investment fund shareholders Interest Short-term Long-term	Income credits and debits (income receivable on claims on nonresidents and income payable on liabilities to nonresidents) can be collected in surveys of companies, surveys of financial intermediaries and/or custodians, an ITRS, or from official records. Care should be taken to ensure that income accrued but not paid is measured and offset appropriately in the financial account. An alternative methodology may involve maintaining an inventory of securities held by residents and estimating the dividends and interest on those securities by using yield analysis.
Other investment income Withdrawals from income of quasi-corporations Interest Memorandum: Interest before FISIM Investment income attributable to policyholders in insurance, pension, and standardized guarantee schemes	Data can be collected through enterprise surveys, an ITRS, or official sector sources. Some economies estimate income flows on certain assets, such as other sectors deposits abroad, by using data obtained from international institutions. Alternatively, data models based on yield analysis may be used to estimate certain components. Interest includes also interest payable on SDR allocations.
Reserve assets Income on equity and investment fund shares Interest Memorandum: Interest before FISIM	Data can be collected from official sector sources. It includes, among others, interest receivable on SDR holdings.
Other primary income *Taxes on products and production* *Subsidies* *Rent*	Data can be collected through enterprise surveys, an ITRS, or official sector sources. Care should be taken to ensure that rent accrued but not paid is measured and offset appropriately in the financial account. Data on taxes on products and production should be available from official sources, such as tax records (in the case of withholding) and records of other relevant government agencies (in the case of fees, fines, etc.). Data on subsidies also should be available from relevant government agencies.

Source: IMF staff.

13.36 An ITRS can serve as a useful source of data for measuring investment income. However, some transactions require special attention if investment income is to be measured completely and accurately. Interest accrued and not yet paid will be missed unless the compiler monitors such transactions carefully. The issue of recording interest on an accrual basis is discussed further in paragraph 13.73 of this chapter. Furthermore, many investment income transactions are not made through the banking system or do not involve the payment of cash (e.g., reinvested earnings and investment income earned on technical reserves held by insurance corporations). Where these transactions are significant, the compiler should ensure that these transactions are reported and that offsetting entries in the balance of payments accounts are also recorded. For example, it is likely that the compiler will have to approach companies and insurance corporations directly to measure reinvested earnings attributable to direct investors and investment income attributable to policyholders.

13.37 Many survey respondents tend to record certain transactions after certain costs, such as after commissions, fees, or taxes have been deducted. Instructions to the surveys pertinent to these matters should be clear to ensure that data are reported according to balance of payments requirements, before deducting these costs. Also, discounts and premium income associated with nonequity securities may not be separated from other amounts paid at the redemption, so an ITRS should be designed to collect information on premiums and discounts that have to be included under investment income. If not, alternative sources for this information should be established.[7]

13.38 As persons completing ITRS forms may be unfamiliar with the level of detail, an ITRS must be well designed to ensure correct classification of transactions. The compilation of reinvested earnings is discussed in a subsequent section of this chapter.

[7]Related financial transactions reported in an ITRS also may have to be adjusted for premiums and discounts.

Estimation in the Absence of Data and Extrapolations

13.39 The most common approach to estimating investment income in the absence of direct information on investment income receipts or payments is to use a data model in which income yields are applied to levels of financial assets or liabilities.[8] This approach is quite commonly used to estimate interest and dividends on securities and is sometimes used to estimate income on other financial items, such as loans and deposits. However, this approach is rarely used to measure direct investment income. Like most other data models, the income yield model often works well when used at a detailed level of disaggregation. For example, better estimates of portfolio investment income debits would be derived if separate models were established for equities and for debt securities. In more sophisticated models, the income on each type of security held might be estimated separately. Data models are further discussed in Chapter 8.

13.40 One of the keys to developing estimates of good quality is choosing an appropriate income yield. For estimates of dividend debits, the average dividend yield in the compiling economy's stock markets could be a good indicator. For estimates of dividend credits, the weighted average yield in the stock markets of partner economies could be appropriate. For interest debits and credits, separate models could be developed for each significant type of instrument and by each currency in which financial assets and liabilities are denominated. For example, for loan liabilities denominated in U.S. dollars, an appropriate yield might be the United States lending rate, adjusted for risk (if any) associated with the compiling economy. *International Financial Statistics (IFS)*, which is published by the IMF, provides a number of interest rates that may be useful in determining appropriate yields.[9] If disaggregation of this nature is not possible, then a

[8]Levels of financial assets and liabilities may either be measured directly or derived by using the perpetual inventory method. Perpetual inventory models for portfolio securities typically involve use of appropriate financial market indices to determine the impact of nontransactions changes in levels. However, at a minimum, stock should be measured annually.

[9]These rates are included in world and regional tables provided at the beginning of issues of *IFS*.

weighted average yield, with weights determined on the basis of whatever information is available, could be applied. Regarding the currency composition of financial assets and liabilities, the *BPM6* recommends a set of tables to be compiled as memorandum item that cover currency composition of debt claims to nonresidents (Table A9-I-1a) and of debt liabilities to nonresidents (Table A9-I-2a).

13.41 When actual data are not available on a timely basis, estimates of investment income may have to be extrapolated from data for earlier periods. Most extrapolation techniques for portfolio and other investment income involve determination of historical income yields. These yields are then adjusted, in the case of interest, for changes in interest rates and credit risks and, in the case of dividends, for changes in profitability and policies with regard to the retention of earnings.[10] The adjusted yields are then applied to estimates of positions, which may be based on actual data or extrapolated. Alternatively, the compiler may use known interest payment schedules for certain components of debt and yield analysis for the remainder.

13.42 For the extrapolation of direct investment income, similar techniques could be used. For equity income on direct investment, the best results are usually achieved when total equity income—that is, dividends and withdrawals from income of quasi-corporations plus reinvested earnings—is extrapolated and then broken down into component parts on the basis of historical distribution patterns and known changes in these patterns. The compiler may also be able to obtain useful information on profitability and on dividend payments from discussions with a few significant direct investors (in the case of credits) and DIENTs (in the case of debits).

[10] Changes in interest rates will not fully impact other investment income in the periods in which the changes occur because many financial assets and liabilities will have fixed rates of interest. The compiler should analyze the composition of other investment assets and liabilities to determine the fixed-interest component. This information should be used to moderate the impact of changes in interest rates on income estimates. For dividends, information on changes in profitability could be available from profit surveys used to compile national accounts or from tax records. Information on changes in distribution policies could be obtained from stock exchanges. For example, changes in the ratio of average dividend yields to the inverse of the average price/earnings ratio could be used as an indicator of changes in distribution policies.

Calculation of Reinvested Earnings for Direct Investors and Investment Fund Shareholders

13.43 Reinvested earnings are calculated by using the accounts of DIENTs or investment funds. Reinvested earnings of a company are the owner's share of the company's retained earnings or net saving (before reinvested earnings payable are deemed distributed). Retained earnings or net saving (before attributing reinvested earnings) of a company may be formally stated as follows:

Retained earnings[11] =

+ Net operating surplus (operating revenue minus operating expenses)

+ Net dividend income receivable

  + Dividends receivable

  – Dividends payable

+ Net interest receivable

  + Interest receivable

  – Interest payable

+ Company's share of retained earnings of any direct investment enterprises

+ Net rent receivable

  + Rent receivable

  – Rent payable

+ Net current transfers

  + Current transfers receivable

  – Taxes and other current transfers payable

– Adjustment for the change in pension entitlements.

13.44 In the next step, to obtain reinvested earnings, each shareholder/owner's share of retained earnings is determined by multiplying total retained earnings by the percentage of the shareholder/owner's claims on these retained earnings:

Reinvested earnings =

Retained earnings

× Percentage of equity held by the shareholder/owner.

13.45 Thus, reinvested earnings do not include any realized or unrealized holding gains or losses (e.g., holding gains and losses due to price changes,

[11] See the *BPM6*, paragraph 11.34, and the *2008 SNA*, paragraph 26.63.

exchange rate changes, or other changes in volume of assets, such as write-offs); consequently they are excluded from this calculation. Because business accounting measures of profits often include holding gains or losses, adjustments to business accounting records may be necessary.

13.46 All of these data should be available from the accounts of companies concerned and, more particularly, from company income and expenditure and profit and loss statements. For direct investment, companies could be permitted to report on an individual basis or a group of related companies could report on a consolidated basis. When these companies are consolidated, they are referred to as a "local enterprise group." In the case of a resident direct investor, the local enterprise group includes the institutional unit that directly owns a foreign direct investment enterprise (DIENT), the resident companies that directly or indirectly control this company, and the resident companies that any of these companies directly or indirectly control in their own economy. In the case of a resident DIENT, the local enterprise group includes the resident company that is directly controlled or influenced by a foreign direct investor, plus the institutional units that it directly or indirectly controls in its own (local) economy. To be fully consistent with requirements of the balance of payments methodology, the balance of payments compiler may have to make some of the adjustments that are subsequently discussed.

13.47 One of the components of the retained earnings is the net operating surplus, which is the value added from the operations of the company—that is, the value of the outputs *less* the value of the intermediate inputs; *less* consumption of fixed capital (including any provision for this consumption); *less* taxes on production (less subsidies); and *less* compensation of employees.

13.48 Consumption of fixed capital should be calculated on the basis of current replacement cost (*BPM6*, paragraph 11.45). However, company accounts may reflect a variety of bases, including historic cost depreciation. When advising companies on how to report, the compiler could suggest that consumption of fixed capital be calculated by using current cost accounting methods and by excluding any special tax allowances for depreciation, such as accelerated depreciation allowances. Alternatively, the balance of payments compiler may, in conjunction with the national accounts compiler, make an aggregate adjustment, which is based upon knowledge of company accounting practices, to consumption of fixed capital estimates underlying reported reinvested earnings data. Another option is for the balance of payments compiler to ask companies on what basis consumption of fixed capital was recorded; when current replacement cost was not used, the compiler may consider making adjustments to data reported in individual collection forms.

13.49 Net operating surplus should be adjusted to determine retained earnings by taking into account other current earnings (such as dividends receivable), net interest receipts (interest receivable less interest payable), current transfers (such as subsidies received), and the reinvested earnings receivable from other companies (including companies located abroad).

13.50 Retained earnings are finally obtained after deducting taxes due for payment from net earnings and any dividends due for payment (or withdrawals from income of quasi-corporations). A shareholder/owner's share of retained earnings should be calculated according to the shareholder/owner's equity share in the company.

13.51 As previously noted, the calculation of retained earnings should exclude capital gains and losses, even if these are included in company profit and loss statements. For example, if a company paid a dividend because it sold a financial asset on which it made a windfall profit—that is, the sale price of the asset was much greater than the purchase price—the distribution to the investor should be shown in the financial account as a distribution of equity capital and excluded in the calculation of reinvested earnings.

13.52 Insurance companies may be DIENTs. Net operating surplus of insurances companies is equal to the following:

Net operating surplus (operating revenue minus operating expenses) =

Output from "production" (whereby calculated as actual premiums earned *plus* premium supplements *minus* adjusted claims incurred (or changes in actuarial reserves)

+ Dividends/interest receivable from the investment of own assets

– Operating costs (salaries, rent, etc.).

13.53 Deposit-taking corporations (banks) may also be DIENTs. Net operating surplus for deposit-taking corporations and other financial corporations should equal fee-based revenue (including imputed fees such as those from foreign exchange trading), *plus* property income receivable, *less* property income payable. Write-downs and write-offs of loans and other financial instruments are capital losses, and so they should be excluded from the calculation of operating surplus.

13.54 Reinvested earnings can also be derived from examination of a company balance sheet. One of the components of a balance sheet is shareholder funds. Shareholder funds may change in a period as a result of the following:

- Issues less redemptions of shares
- Extraordinary items, such as capital gains and losses
- Changes in revaluation reserves
- Retained earnings.

13.55 Thus, retained earnings can be measured directly or derived by deducting the first three components from the total change in shareholder funds. However, the compiler should be aware that a company balance sheet may be prepared according to accounting rules that differ from those required by the balance of payments methodology. (In particular, differences may arise with position valuations, recording and classification of capital gains and losses, and consumption of fixed capital.) The differences may have an impact on the derivation of reinvested earnings from balance sheets, and when the impact is significant an appropriate adjustment should be made. For this reason, many balance of payments compilers prefer to calculate reinvested earnings by analyzing profit and loss statements (in which appropriate adjustments are more easily identified) rather than calculating reinvested earnings from balance sheets.

13.56 When a chain of direct investment relationships exists, it is clarified that reinvested earnings should be recorded between the direct investor and its directly owned DIENTs only—that is to say when there is an immediate 10 percent or more equity ownership; this directly owned DIENT should include its share of the reinvested earnings of DIENTs in its ownership chain in the calculation of its own reinvested earnings.

13.57 Reinvested earnings can be negative or positive in sign for both the investor and the DIENT or investment funds. Negative reinvested earnings indicate that, for the reference period, the dividends paid out by the DIENT or investment funds are higher than net earnings in that period or that the company is operating at a loss.

13.58 Negative reinvested earnings incurred by a *resident direct investment enterprise* should be recorded as follows:

- *Negative debit* for investment income on direct investment—Income on equity—reinvested earnings
- *Offsetting negative* entry in the financial account—Direct investment—equity—reinvestment of earnings (net incurrence of liabilities).

13.59 Negative reinvested earnings obtained by a *resident direct investor* should be recorded as follows:

- *Negative credit* for investment income on direct investment—Income on equity—reinvested earnings
- *Offsetting negative* entry in the financial account—Direct investment—equity—reinvestment of earnings (net acquisition of financial assets).

13.60 Thus, if a DIENT incurs an operational loss of 100 units, the following balance of payments entries that should be recorded are presented ahead.

A. For the *direct investment enterprise*:

	Credit	**Debit**
Current account		
Primary income		
Investment income		
Direct investment		
Income on equity		
Reinvested earnings		–100
	Net acquisition of financial assets	**Net incurrence of liabilities**
Financial account		
Direct investment		
Equity		
Reinvestment of earnings		–100

B. For the direct investor:

	Credit	Debit
Current account		
Primary income		
Investment income		
Direct investment		
Income on equity		
Reinvested earnings	–100	
	Net acquisition of financial assets	**Net incurrence of liabilities**
Financial account		
Direct investment		
Equity		
Reinvestment of earnings	–100	

13.61 For investment fund shares owned by nonresidents and for direct investors' equity in their DIENTs, retained earnings are imputed as being payable to the owners/direct investors and reinvested as an increase in their equity. In other cases of equity owned by nonresidents, there is no imputation of income or financial account transactions to the owners on account of retained earnings. As the result, the increase in the value of the equity caused by the accumulation of retained earnings not attributed to owners is reflected in increased value in equities in IIP without transactions in balance of payments and is, therefore, shown as a revaluation.

Recording Interest Income on an Accrual Basis

13.62 The interest can be seen as including both an income element and a charge for a service (FISIM).[12] The identification of FISIM as the financial service implicitly included in interest requires corresponding adjustments to interest as recorded in the primary income account. Actual interest payable by borrowers is partitioned between a "pure interest" charge at the reference rate (in primary income) and FISIM (a service). Similarly, pure interest receivable by depositors is calculated by applying the reference rate to depositors, and depositors are shown as consuming a service equivalent to the difference between the actual interest and interest at the reference rate. The interest shown in the primary income accounts is shown after adjusting for FISIM—"pure interest"; also, there is a memorandum item for interest before adjusting for FISIM—"actual interest" (see *BPM6*, Box 10.5, for a numerical example).

13.63 Interest is recorded in the balance of payments on an accrual basis.[13] That is, interest on the amount of principal outstanding is recorded as accruing continuously to the creditor. Accrued interest is the amount ultimately receivable by the creditor and payable by the debtor. Accrued "actual interest" (disseminated as a memorandum item) also includes FISIM accrued. Accrued interest may differ from the amount due to be paid during a specified period, and this amount may, in turn, differ from the amount actually paid in the period. In the balance of payments, offset entries to accrued interest can take one of three forms.

13.64 First, if interest is accrued during a particular period but not due for payment in that period, the offset to the accrued interest should be recorded as a financial account transaction in the same type of instrument as the underlying principal. For example, if a resident (e.g., nonfinancial corporation) of the compiling economy holds a bond issued by a nonresident company, and interest of 10 is accrued but not due for payment during a particular period, the following balance of payments entries should be recorded:

	Credit	Debit
Current account		
Primary income		
Investment income		
Portfolio investment		
Interest		
Long-term	10	
	Net acquisition of financial assets	**Net incurrence of liabilities**
Financial account		
Portfolio investment		
Debt securities		
Other sectors		
Nonfinancial corporations		
Long-term	10	

[12] Detailed discussion on FISIM is presented in Appendix 3 of this *Guide*.

[13] For numerical examples on recording of accrued interest on loans see *External Debt Statistics: Guide for Compilers and Users*, Box 2.3.

13.65 When interest is actually paid—which, in the case of a security issued at a discount with no interest payments, will be when the security is redeemed—the offset to the payment that flows through the banking system should be recorded in the financial account as a reduction in investment in the instrument in which the offset to the accrued interest was recorded, rather than as investment income. Following the foregoing example, when the security matures and interest and principal are paid, the following balance of payments entries should be recorded:

	Net acquisition of financial assets	Net incurrence of liabilities
Financial account		
Portfolio investment		
Debt securities		
Other sectors		
Nonfinancial corporations		
Long-term	–10	
Other investment		
Currency and deposits		
Deposit-taking corporations		
Short-term	10	

13.66 Second, if interest accrued during a particular period is paid during that period, the offset to the accrued interest is simply a financial transaction through the banking system.

13.67 Third, if the interest accrued during a particular period is due for payment during that period but not actually paid (interest in arrears) the offset to the accrued interest should be recorded as a financial account transaction in the same type of instrument as the underlying principal. Balance of payments entries are similar to those presented earlier for the accrued interest.

13.68 Data on arrears are important in their own right, and thus should be presented as supplementary items, where significant, or memorandum items in the case of exceptional financing (see *BPM6*, Appendix 1).

13.69 For debt securities (portfolio investment) and other types of debt, accrued interest should be calculated in accordance with interest terms specified in the contract.[14] For example, if a bond is issued at par and the contract specifies a fixed-interest rate of 10 percent each year, the accrued interest for each year should be calculated as 10 percent of the amount outstanding. On the other hand, if variable interest rates are applicable to debt, the prevailing rate appropriate to the debt instrument should be used to calculate accrued interest.

13.70 If the debt security has coupon payments, in both cases described earlier the result may differ depending on coupon interest payments made during the period. If coupon interest payments are higher than calculated accrued interest (i.e., the instrument was issued at a premium), the difference should be recorded as a withdrawal of investment in the underlying security in the financial account. If coupon interest payments are lower than accrued interest (i.e., the instrument was issued at a discount), the difference should be recorded as further investment in the underlying security.

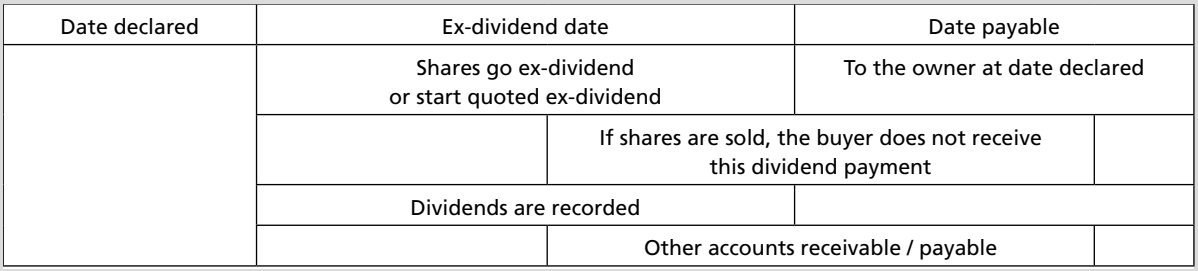
13.71 It should be noted that, for debt securities, the valuation in the balance sheets and recording of purchases and sales in the financial account and positions do not depend on the method used for the calculation and recording of interest accrual. Acquisitions and disposals of debt securities are recorded at transaction prices, and the positions are recorded at market prices or fair values.

13.72 To obtain the information necessary for properly recording accrued interest on securities, the balance of payments compiler could approach creditors and debtors through enterprise surveys or a supplement to an ITRS.

13.73 The nature of an ITRS makes it more difficult to measure interest on an accrual basis than on a payment basis. Nonetheless, an ITRS can be used as a source for measuring investment income in the balance of payments because interest, in many cases, is paid in the periods in which it is accrued. The compiler need be concerned largely about collecting supplementary information for significant cases in which interest is not paid in the same period in which it is accrued (e.g., interest in arrears and interest on zero cou-

[14] Debtor approach. Box 11.2 of the *BPM6* gives an example of a zero-coupon bond.

Figure 13.1 Dates Associated with Dividends



pon and deep discounted bonds). Conversely, the use of yield analysis to derive estimates of investment income accords closely with the requirements of accrual accounting but is an approximation of the method preferred in the *BPM6* for recording interest. The compiler should be aware of situations in which prevailing interest rates are not relevant for the calculation of accrued interest—that is, in the case of fixed interest, nontradable debt—and should ensure that these are considered in the calculation of interest yields.

Dividends and Ex-dividend Date

13.74 For corporations, the distributed income is in the form of dividends. For quasi-corporations, the investment income is withdrawals from income of quasi-corporations, such as distributed branch profits, which are recorded when they actually take place.

13.75 Dividends represent a part of income that has been generated over a substantial period; sometimes they may be related to the company's profits in the previous period, and in other cases, they are only loosely related or not at all.

13.76 There are three dates associated with dividends:

(1) The date they are declared

(2) The ex-dividend date: this is the date when the declared dividend is excluded from the market price of shares. The holder of the security at the moment shares go ex-dividend is entitled to receive the dividend on the date payable

(3) The date they are settled.

13.77 Dividends are recorded at the moment the shares go ex-dividend (date 2). Between the ex-dividend date and actual settlement (2 and 3), the amount payable is recorded as other accounts receivable/payable (see Figure 13.1).[15]

Superdividends

13.78 As mentioned, dividends may be or may not be related to the company's profits in the previous period. For practical reasons, no attempt is made to align dividend payments with earnings, except when the dividends are disproportionately large. Superdividends are extraordinarily large dividends that are out of line with recent experience on the amount of income available for distribution to the owners of the corporation or quasi-corporation. They arise when the corporation declares payments disproportionately large relative to the recent past level of dividends and earnings. The superdividends can be identified by the following characteristics:

(1) They are often paid out of the proceeds from sales of fixed assets, operating units, or liquidations.

(2) The level of dividends declared is greatly in exess of previous dividends and trends in earnings (considering around the last five years).

13.79 The excess payment should be excluded from dividends and treated as a financial transaction, specifically as withdrawal of shareholders' equity from the corporation. Equally, liquidating dividends paid to shareholders should be recorded as a withdrawal of equity (see Example 13.2).

[15] According to *GFSM 2014*, in the unusual case where there is no ex-dividend date (which may occur when there is only a single shareholder in certain public corporations), dividends should be recorded at the time they are declared. This methodology may be also used in the international accounts.

Example 13.2 Calculation of Dividends

On March 4, a DIENT of the compiling economy declares a payment of dividends of US$800. On June 26 its shares go ex-dividend, and on July 14 the company pays dividends. Knowing that the level of dividends paid in each of the last five years was US$200, the following balance of payments entries should be recorded in the balance of payments of the DIENT's economy, assuming that the US$800 is a material amount for that economy:

Balance of payments for quarter 1 (dividend declared payable to holders of record on June 26): No entries should be recorded.

Balance of payments for quarter 2 (shares go ex-dividend):

	Credit	Debit
Current account		
Primary income		
Investment income		
Direct investment		
Income on equity and investment fund shares		
Dividends		200

	Net acquisition of financial assets	Net incurrence of liabilities
Financial account		
Direct investment		
Equity and investment fund shares		
Equity other than reinvestment of earnings		
Direct investor in direct investment enterprises		–600
Other investment		
Other accounts payable—other[1]		
Other sectors		
Short-term		800

Balance of payments for quarter 3 (payments are made):

	Net acquisition of financial assets	Net incurrence of liabilities
Other investment		
Currency and deposits		
Other sectors		
Short term	–800	
Other accounts payable—other		
Other sectors		
Short-term		–800

[1]Between the ex-dividend date and the payable date dividends and superdividends are recorded as other accounts receivable/payable—other.

Investment Income Attributable to Investment Fund Shareholders

13.80 Investment funds are collective investment undertakings through which investors pool funds for investment in financial or nonfinancial assets. Those units acquiring shares in the funds thus spread their risk across all the instruments in the fund. Investment funds provide a convenient, accessible, and affordable vehicle for financial investment. Typically, investment funds sell shares or units to the public and invest in a diversified portfolio of securities, although they may also invest in other assets, including real estate, or they may be limited to a small number of investors. Investment fund shares have a particular role in financial intermediation as a collective investment in other assets, so they are identified separately.

13.81 Investment fund shares refer to the shares issued by mutual funds, rather than the shares the mutual fund may hold. Each share represents a proportional equity in the investment portfolio managed by investment funds.

13.82 Investment income attributed to holders of shares or units in investment funds includes the following:

(1) Dividends distributed to investment fund shareholders

(2) Reinvested earnings attributed to investment fund shareholders.

13.83 Dividends attributable to investment fund shareholders are recorded in exactly the same manner as dividends for individual corporations. Dividends are a form of investment income covering all distributions of profits by corporations to their shareholders or owners.

13.84 It is considered that the net earnings of investment funds after deducting the operating expenses belong to shareholders. When only a part of the net earnings is distributed as dividends, the part of retained earnings owned by nonresident shareholders should be treated as if they were distributed to them and then deemed reinvested.

13.85 Reinvested earnings are recorded using the same principles as those described earlier for foreign DIENTs; any undistributed earnings of an investment fund owned by nonresidents are shown as reinvested earnings in the primary income account and as reinvestment of earnings in the financial account. When nonresident shareholders own only part of the shares of the investment fund, the amount that is deemed to be remitted to, and reinvested by, the nonresident shareholders is proportional to the percent share of the equity owned.

13.86 Investment income attributable to nonresident owners of investment fund shares (both dividends and reinvested earnings) is usually recorded as portfolio income; nonresident shareholders' participation usually provides less than 10 percent of the voting power in the investment fund, but it may also arise in other functional categories—that is, direct investment, other investment, or reserve assets.

13.87 Investment funds could be DIENTs when a nonresident shareholder owns 10 percent or more of the voting power in the investment fund. In this case, dividends and reinvested earnings attributable to that shareholder should be recorded under direct investment income. As mentioned before, this heading refers to income attributed to the shares issued by mutual funds, rather than to income attributed to the shares the mutual fund may hold, except when investment funds invest in other investment funds. In this case, investment funds can be direct investors in other investment funds, and investment income should also be recorded under direct investment income attributable to investment fund shareholders.

13.88 Investment income attributable to investment funds shareholders is recorded in other investment income when it cannot be classified in any other functional category (see *BPM6*, paragraph 11.106). This could be the case when funds are limited to certain investors (who are not direct investors), such as unincorporated funds, instead of being available to the public generally.

13.89 There may be considerable holding gains and losses on investment fund shares; indeed, the most frequent reason for acquiring these instruments is to benefit from the holding gains that arise from holding them. Investment income attributable to owners of investment funds excludes holding gains and losses arising from investment by the funds. Holding gains and losses are recorded in the other changes in financial assets and liabilities account.

Fees for Securities Lending without Cash Collateral

13.90 Securities lending without cash collateral consists of the delivery of securities by their owner (the securities lender) for a given period of time to another party (the securities borrower). In this circumstance, legal ownership of the securities is transferred to the borrower (and the borrowers can subsequently on-sell the securities outright to other entities), but the economic risks and rewards of ownership remain with the original owner, who remains susceptible to gains and losses from changes in prices of the securities.

13.91 The lender receives a fee from the borrower under the securities lending agreement that represents a return to the security lender for putting the securities at the disposal of the securities borrower. This securities lending fee received by the securities lender is, by convention, to be recorded as interest, under other accounts receivable/payable in *other investment income,* rather than in the category associated with the instrument to which this payment relates (see *BPM6,* paragraphs 5.73 and 11.68).

13.92 The economic owner of securities (securities lender) continues to record investment income on the securities (see *BPM6,* paragraph 11.69). If coupons or dividends are paid to the securities borrower, who then pays the securities lender, a rerouting from the securities borrower to the securities lender of these payments is recorded. In this way the payments are

recorded as transactions between the issuer of the securities and the securities lender. This maintains consistency between stocks and flows.

13.93 If the total payment by the securities borrower to the securities lender includes both the securities lending fee and the rerouted payments, and these two elements cannot be disaggregated in the manner described above, for practical reasons, the compiler may wish to record the total payment as interest in *other investment income.*

Other Primary Income

13.94 Other primary income is a residual category that includes primary income other than compensation of employees and investment income. This category includes the following:

(1) Taxes on products and production

(2) Subsidies on products and production

(3) Rent.

13.95 Data sources available to collect other primary income are presented in Table 13.1.

Taxes and Subsidies on Products and Production

13.96 Taxes and subsidies on products and production are recorded separately in other primary income. This includes any payments of taxes on production payable by a resident to another government as well as any subsidy receivable by a resident from another government.

13.97 Taxes on products and production are included in the primary income account, while taxes on income and wealth are included in the secondary income account (e.g., taxes on capital gains and taxes on wages and salaries) (*BPM6*, paragraphs 11.92 and 12.28). A tax on products is a tax that is payable per unit of a good or service (e.g., value-added tax and import duties). These taxes may be added to the prices of the goods or services sold. Other taxes on production consist of all taxes except taxes on products that companies incur as a result of engaging in production (e.g., payroll taxes and business licenses).

13.98 For most economies, taxes and subsidies receivable from or payable to nonresident producers would be nonexistent or negligible. They arise if an international or regional organization levies its own taxes or pays subsidies. They may also arise when economic activity by nonresidents (such as short-term construction or installation projects) is insufficient to constitute a branch.

13.99 The f.o.b. valuation for international accounts purposes means that export taxes are treated as payable by the exporter and that import duties and other taxes of the importing economy are payable by the importer; therefore these are resident-to-resident transactions and are not recorded in the international accounts. In some cases, an exporter of a good contractually agrees to pay import duties. In such cases, the duties are outside the scope of the primary distribution of income in the international accounts. This treatment is adopted because the duties arise from the process of importation, and so they are an obligation of the importer. They are, therefore, treated as payable by the importer, and so are resident-to-resident transactions. The amount of import duties paid by the exporter, therefore, is not included in the f.o.b. value of the goods. Similarly, if an importer agrees to pay export taxes, the tax is still an obligation of the exporter. The amount of the export tax paid by the importer, therefore, is included in the f.o.b. value of the goods and rerouted through the exporter.

13.100 In some circumstances, a duty or other tax may be imposed by the customs authorities without ownership being acquired by a resident of that economy. Examples may include goods to be processed, repaired, or stored, or for use by visitors. In such cases, when customs duties are payable by nonresidents, the duties are recorded as taxes on products in other primary income.

Rent

13.101 The income payable for the use of a natural resource is called rent. Natural resources include land, mineral rights, forestry rights, water, fishing rights, air space, and electromagnetic spectrum.

13.102 Rent covers income associated with the ownership of natural resources. Natural resources give rise to property income other than investment income. Rent may arise in cross border situations, but rarely, because all land is deemed to be owned by residents, if necessary by creating a notional resident unit. An example where rent may be recorded in the international accounts may be short-term fishing rights in territorial waters provided to foreign fishing fleets. It is also possible that other natural resources adjoining a border could be extracted from a base on the other side of the border, thus giving rise to rent. Another example of rent in the balance of payments is given in

Box 10.1, describing the treatment of production sharing agreements.

13.103 Payments and receipts by government of rent on land areas without buildings (such as embassies, consulates, military bases, representative offices with diplomatic status) that are used by other governments that rent them for diplomatic, military, or other purposes should be shown as rent. For rent on land and buildings see the section ahead.

13.104 Another component that is classified under rent is related to agreements in professional sports involving the sale of rights to use players. Under so-called loan agreements, a player is allowed to temporarily play for a club other than the one with whom the player is currently under contract. The fees paid under loan agreements should be recorded in property income as rent. More details on transfer of rights to use the sport players are presented in "Contract, leases, and licenses" in Chapter 15.

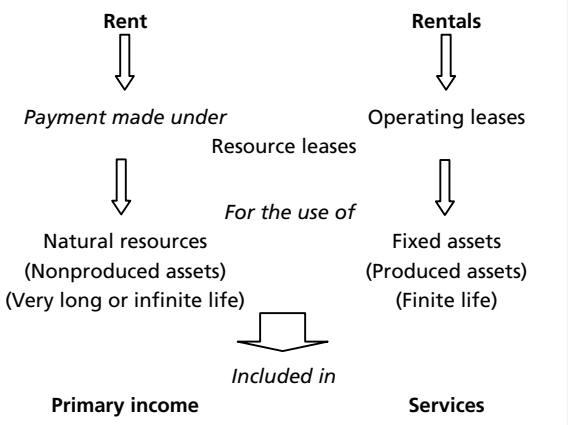
Rent and Rentals

13.105 The compiler should distinguish between rent and rentals. Rentals are payments made under an operating lease to use a fixed asset, such as buildings or equipment, belonging to a resident in another economy. Rent is a payment made under a resource lease for the use of a natural resource. Rent is considered property income and included in the primary income account while rentals are treated as sales or purchases of services.

13.106 An operating leasing is one in which the legal owner of a produced asset has the operating risks and rewards from ownership of the asset. It is the responsibility of the legal owner to provide any necessary repair and maintenance of the asset. Under an operating lease, the asset remains on the balance sheet of the lessor (owner) even though it is used by the lessee. The operating leasing gives rise to services and is recorded as technical, trade-related, and other business services (if leased by a commercial entity), and as government goods and services n.i.e. (if leased by international organizations, embassies, and so forth). A resource lease is an agreement whereby the legal owner of a natural resource that has a very long or infinite life makes it available to a lessee in return for a regular payment, which is recorded as rent. The resource continues to be recorded on the balance sheet of the lessor (owner) even though it is used by the lessee.

13.107 The differences between rent and rentals are illustrated in Figure 13.2.

Figure 13.2 Difference Between Rent and Rentals



13.108 In practice, however, a single payment may cover both rent and rentals when an institutional unit rents land that consists of land in its natural state and buildings situated on it in a single contract, or lease, in which the two kinds of payments are not differentiated from each other. The allocation of the payment between rent and rentals when there is no objective method of splitting it is done in the favor of component with the highest value. (See also "Operating Leasing" in Chapter 12.)