IV. Goods

166. As defined in the *BPM*, the ***goods*** component of the balance of payments covers *general merchandise, goods for processing, repairs on goods, goods procured in ports by carriers,* and *nonmonetary gold. General merchandise* (sometimes referred to as *merchandise*) is defined for BOP purposes as covering (with a few specific exceptions) all movable goods for which actual or imputed changes of ownership occur between residents and nonresidents.

167. Certain commodities, although constituting real assets that undergo international changes in ownership, are nonetheless excluded from the ***goods*** component and included in other standard components of the balance of payments. Primary examples of goods excluded from the ***goods*** component and included in other portions of the **current account** are:

monetary gold, which is classified under *reserve assets* in the ***financial account;***

goods acquired by travelers and nonresident workers for their own use and recorded under *travel* (part of ***services***);

goods that are acquired from host countries by embassies, consulates, military missions and agencies, and related nonresident personnel and classified under *government services n.i.e.* (part of ***services***);

newspapers and periodicals (not in bulk) sent under direct subscription and included under *computer and information services* (part of ***services***);

goods that are acquired and relinquished within the same recording period, do not cross the frontier, and are recorded—on a net basis—under the *merchanting and other trade-related services* portion of *other business services* (part of ***services***).

168. Assets regarded as evidence of financial claims (even when such assets possess material form and are movable) are included in a BOP financial account component appropriate to the type of claim. Examples of such assets are paper money and coin in current circulation and securities that have been issued. Furthermore, if a change in the ownership of a real asset results from the acquisition of an existing enterprise by a resident of an economy other than the one in which the enterprise is located, the change of ownership is treated as a financial transaction and not included in ***goods***. (Exceptions are changes of ownership actually involving physical movement of goods across the frontier.) The change of ownership is treated thus because the enterprise is considered a resident of the economy in which the enterprise operates (see paragraph 92), and ownership of the enterprise is considered a financial investment.

169. As the previous paragraph indicates, the ***goods*** component does not cover all changes, between residents and nonresidents, in the ownership of commodities. Criteria for items to be included or excluded from ***goods*** are not always as clear as those for the exclusion of goods regarded as evidence of financial claims.

170. An explanation for the existence of exceptions to coverage, by the ***goods*** component of the balance of payments, of all exchanges in real assets may be found in the considerations (discussed in paragraph 143) for determination of BOP standard components. Two of these considerations are particularly important:

The item should exhibit distinctive behavior that demonstrates a unique response to a particular economic factor or combination of factors.

It should be possible to obtain statistics for the item without undue difficulty.

171. Therefore, transactions depicting similar behavioral characteristics are grouped together if separate data can be obtained for the group of transactions selected. For example, forces influencing the purchase of commodities by a nonresident traveler differ sufficiently from those affecting the host country's other exports to warrant the exclusion of such purchases from the ***goods*** component. In addition, it would be difficult to obtain statistics on individual purchases made by nonresident travelers.

Similar reasoning applies to the other exceptions cited in paragraph 167. For instance, goods that are acquired and relinquished within the same reporting period and do not cross the frontier are classified under *merchanting and other trade-related services* (rather than ***goods***) provided by an economy to the rest of the world because the provision of merchanting services is generally unrelated to a country's consumption of imports and production of exports.

172. While certain specific transactions are excluded from the ***goods*** component, other transactions are included—even though such transactions may be more akin to services. For example, an element of transportation is often included in the value of goods because of the BOP accounting convention requiring goods to be uniformly valued at the customs frontier of the exporting country. This basis of valuation differs from the pure concept of commodity transactions, which are usually used in constructing input-output tables for valuing goods at the establishment of the producer. The rationale for selection of the customs frontier as the point of valuation is discussed in paragraphs 220–227.

173. Within the ***goods*** component, four special types of transactions are separately distinguished from *general merchandise.* These are:

(1) goods sent abroad for processing and subsequently returned to the country of the original exporter (These goods are part of the *goods for processing* item.)

(2) goods (and services) used in the repair of other goods owned by nonresidents (These goods are part of the *repairs on goods* item.)

(3) fuels, provisions, stores, and supplies for carriers (Commodities purchased for commercial use in ships, aircraft, and other carriers are assigned to the *goods procured in port by carriers* item.)

(4) *nonmonetary gold*, which is subdivided into gold held as a store of value and other gold.

174. Although the commodities involved are clearly goods, the transactions are often undertaken for reasons other than the general level of economic activity within an economy. Also, the inclusion of such transactions in *general merchandise* could create a misleading impression about the volume of a country's merchandise transactions. For example, fuel purchased by carriers for use in operations is not recorded in the *general merchandise* category because purchases of fuel for carriers are more closely linked to transportation operations than to an economy's demand for oil. Classification of such fuel purchases as *general merchandise* transactions might be economically meaningful for the country selling the fuel but much less so for the country purchasing it. For similar reasons of symmetry, ships' supplies are grouped under *goods procured in port by carriers*. Transactions in *nonmonetary gold* are often motivated by considerations other than the use of gold as part of the processes of production and consumption. Including these transactions in *general merchandise* could create a misleading impression about an economy's production (in the case of exports) or consumption (in the case of imports). Accordingly, under the ***goods*** component, transactions in *nonmonetary gold* are shown separately from those in *general merchandise.* Transactions in *goods for processing* are often very large in a gross sense, but the net impact of these transactions on an economy is much smaller. Including these transactions in *general merchandise* could create a misleading impression about the overall size of a country's external trade.

175. In summary, the concept of transactions in goods excludes certain commodity exchanges between economies but includes certain distributive services. Furthermore, while most transactions in goods are classified under *general merchandise*, some transactions are separately identified. These classifications are the result of analytical considerations and statistical convenience.

Convention for Recording Change of Ownership

176. Aside from the exceptions noted previously, the content of the ***goods*** component is defined with reference to changes in the ownership of all movable goods subject to exchanges between residents and nonresidents. The change of ownership rule adopted for defining goods ensures, in principle, that the ***goods*** component is consistent—with regard to coverage and timing—with other items (especially financial items) in the balance of payments. According to the *BPM*, goods for export are generally considered to change ownership when the exporter ceases to carry the goods on his books as real assets and makes a corresponding change in his financial items. In this way, consistency is ensured between the ***goods*** component and the BOP ***financial account*** of the compiling county. Consistent compilation of the ***goods*** component by exporting and importing countries is thus ensured as well. The following example illustrates the simultaneity, both internal and inter-country, of the pairs of entries.

	Exporting Country	**Importing Country**
Goods	credit	debit
Financial account	debit	credit

177. International standards for trade statistics, which are often used as a source for compiling the ***goods*** component of the balance of payments, are based—not on change of ownership—but on physical movements of goods across national (or customs) frontiers. Although goods that change ownership internationally are, for the most part, the same goods that move across frontiers, the change of ownership and the movement of the goods do not necessarily occur at the same time. International transactions reporting systems (such as those based on foreign exchange and similar bank records) are another possible source of information for the ***goods*** component. In these systems, transactions in goods are not generally recorded on a change of ownership basis. The nature of these differences should become clearer in the context of information presented, in subsequent sections of this chapter, on timing adjustments required to convert source data for use in the balance of payments.

Exceptions to the Change of Ownership Rule

178. While the scope of the ***goods*** component is restricted to commodities that have undergone a change—between a resident and a nonresident—of ownership, the *BPM* nevertheless introduces a few exceptions to the change of ownership principle. Each exception and underlying rationale is discussed in a subsequent paragraph.

Enterprises Operating in More Than One Economy

179. As noted in chapter 2, when a multinational enterprise has significant operations in more than one economy, a separate resident enterprise is assumed to exist in each of the economies where the multinational concern is operating. Goods exchanged between the constituent units of the multinational enterprise do not, in fact, change ownership as would have been the case for goods exchanged by units of separate legal entities. Transactions between a parent company and a branch cannot, in the literal sense, bring about a legal change of ownership because both parties are part of the same legal entity. However, it is recommended in the *BPM* that any international shipment of commodities exchanged between units that are part of a multinational enterprise and constitute a single legal entity be construed as a change in the ownership of the goods. The transaction is therefore included in the balance of payments.

180. In the situation described in the preceding paragraph, a change of ownership is ascribed on the basis of international shipment. The circumstances differ very little from those in which a commodity is exchanged between a parent company and its subsidiary (an incorporated enterprise). As the parent company and its subsidiary constitute separate legal entities, the change of ownership rule may be strictly applied. In this case, the ***goods*** component of the balance of payments would be comprised of commodities that had actually undergone a change, between a resident (e.g., the parent company) and a nonresident (e.g., its subsidiary), of ownership. In the *BPM*, however, international transactions between affiliated enterprises that are not legally distinct from one another are treated the same as international transactions between enterprises that are legally distinct. Thus, the *BPM* recommendation is that all transactions between direct investment enterprises and parent or other related enterprises be recorded as if changes of ownership have occurred. This general instruction does not apply, however, to the kinds of transactions in goods specified in paragraph 201.

Financial Leases

181. The possession of goods may also, in effect, change between a resident and a nonresident who are not affiliated and do not record a change of ownership in their accounts. A common means of transferring the control of goods without a legal change of ownership is through financial leasing. Such lease arrangements provide for the recovery of all, or substantially all, of the cost of the goods and for carrying charges. Furthermore, under a financial lease, most (if not all) of the risks and benefits of ownership are transferred from the lessor to the lessee. In consideration of the essential nature—rather than the legal form—of the transactions, the *BPM* recommendation is that goods covered by such leasing arrangements be recorded in the balance of payments as exports and imports when the goods pass from a lessor resident in one economy to a lessee resident in another.

182. To distinguish financial leases from other forms of leasing, a suggested rule of thumb is that a lease arrangement expected to cover carrying charges and at least three-fourths of the cost of the goods is sufficient evidence of financial leasing and has the same effect as a change of ownership.[7] At the inception of the financial lease, the equivalent of the market value of the goods (not the cumulative total of expected lease payments) should be recorded under ***goods***, and an offsetting entry should be made in the ***financial account*** to record the credit extended to the lessee. (Refer to paragraphs 109–111 for more details on the methodology underlying the recording of transactions relating to financial leases.)

Goods for Processing

183. When there is no change of ownership, the treatment of goods sent abroad for processing and re-export depends upon whether the goods are returned to the economy of origin or exported to a third country. The *BPM* recommendation is that, when goods are shipped from one economy to another for processing and then returned to the first economy, transactions in these goods should be recorded under the ***goods*** component—but separately from *general merchandise* transactions—as if a change of ownership has occurred. However, when the processed goods are exported to a third country, no change of ownership is imputed; in this case, only legal changes of ownership are recorded in the balance of payments.

184. The rationale for the treatment of goods sent abroad for processing and returned to the original exporting economy is based upon requirements of the national accounts and can best be explained by an example. Cromania produces $100 of crude oil and sends the oil to a refinery in Dromesia for processing. A fee of $10 is paid for the processing. The oil is then returned to Cromania in the form of refined oil, which is valued at $110. In the "sources and uses of resources" approach employed in the national accounts, an imputed change of ownership is required to link the produced good (crude oil) with the consumed good (refined oil) in Cromania's national accounts. Were these imputations not made, Cromania's national accounts would show the "disappearance" of crude oil. That is, the crude oil would not be shown as being exported or used for intermediate consumption, and the refined oil would inexplicably appear without ever having been produced or imported.

185. As no legal change of ownership takes place when the crude oil is exported or when the refined oil is imported, imputed financial account entries are required in the balance of payments to preserve the balance between debit and credit entries. Cromanian BOP entries would be:

	Credit	**Debit**
Goods for processing	100	110
Other investment		
Assets		
Trade credits	100**	100*
Reserve assets (or other appropriate financial account item)	10**	

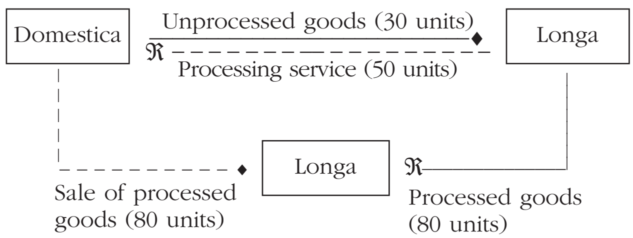
*Reflects the claim that Cromania has on Dromesia because of the oil that the first economy has sent to the second for processing

**Reflects (1) the extinguishment of this claim when the processed oil is returned to Cromania and (2) the payment for the processing

186. In the case of goods that are sent, without a legal change of ownership, from one economy to another for processing and then exported to a third country or ultimately acquired by the processing economy, there is no need to show the same link in the national accounts as production and consumption take place in different economies. In these instances, the *BPM* recommendation is that the change of ownership rule be applied and no transactions in goods are recorded in the balance of payments until legal changes of ownership actually take place. Accordingly, the value added to such goods by processing should be regarded as a service performed by a resident of one economy for a resident of another. For example, goods worth 30 units are shipped (without a transfer of ownership to the processing country) from Domestica to Longa for processing. After processing, the goods are sold by Domestica (the legal owner) to a third country (Pokolbin) for 80 units. In the balance of payments, there would be no transaction in goods between Domestica and Longa or between Longa and Pokolbin, although the external trade statistics of these countries would include those movements. There would, however, be a transaction in goods between Domestica and Pokolbin as well as a service transaction between Domestica and Longa.

[7]Certain leases not satisfying this rule of thumb can be considered financial leases if the leases are accounted for as financial leases in the accounting records of the transactors or if, in the compiler's opinion, most of the benefits and risks of ownership have passed from the lessor to the lessee.

187. The transactions of the three countries are illustrated in the following diagram. Solid lines show the movement of unprocessed goods (valued at 30 units) from Domestica to Longa and the movement of processed goods from Longa to Pokolbin. The processed goods are valued at 80 units (that is, 30 units for the unprocessed goods plus 50 units for the cost of processing). However, transactions to be recorded in the balance of payments consist of (1) the processing service for which Domestica pays a fee of 50 units to Longa and (2) the sale, by Domestica to Pokolbin, of the processed goods for 80 units. These two transactions are indicated by broken lines.



188. BOP entries for the three countries would be:

	Domestica		Longa		Pokolbin	
	Credit	Debit	Credit	Debit	Credit	Debit
General merchandise	80					80
Services		50	50			
Reserve assets (or other appropriate financia laccount item)		30		50	80	

Merchanting

189. Another exception to the change of ownership rule is made when goods are acquired from one economy and relinquished again to that or some other economy without ever crossing the frontier of the economy in which the temporary owner of the goods is a resident. Unlike the three previously discussed exceptions for which changes of ownership (although there were none in a legal sense) were ascribed, this exception negates the fact that the commodity has changed ownership. According to the *BPM*, the net amounts of the transactions are recorded and classified as transactions in ***services*** rather than transactions in ***goods***. The relevant services, which are merchanting (or commodities arbitrage), are classified under *merchanting and other trade-related services*.

190. The BOP treatment of merchanting transactions is in accordance with what may be termed the “real flows principle.” In accordance with this principle, the balance of payments includes, on a gross basis, transactions that are regarded as gross flows of real resources into and out of the domestic economy. However, the balance of payments includes only the value added in the domestic economy by other transactions in goods and services that do not play an important role in relation to economic activity in the reporting economy. With such transactions, the net balance is usually small in relation to the gross turnover. This treatment is consistent with that in the national accounts.

191. If a merchanting transaction is completed within one accounting period, the value added is the difference between the purchase price and the sale price of the goods. For example, a merchant in Clintonstan buys a commodity for 100 units from a resident of Bushland and sells the commodity within the same reference period to an importer in Algornia for 110 units. The production attributable to lintonstan is 10 units, which represent services produced by an entity engaged as a middleman in this form of international trade. In the example, ownership of the goods changes from Bushland to Algornia. BOP entries for the three economies would be:

	Clintonstan		Bushland		Algornia	
	Credit	Debit	Credit	Debit	Credit	Debit
Goods			100			110
Merchanting and other trade-related services	10					
Reserve assets (or other appropriate financial account item)		10		100	110	

192. Entries made for the three economies under ***goods*** and *merchanting and other trade-related services* are asymmetrical. This asymmetry stems from the pragmatic assumption that the importer in Algornia would seldom, if ever, have information on the merchanting profit or loss realized by the intermediary in Clintonstan. Furthermore, asymmetries arising from the treatment of merchanting transactions are unlikely to have a significant impact on the comparability of international BOP statistics.

193. The treatment is more complicated if a commodity is purchased abroad in one accounting period and sold abroad in another period. The *BPM* states that merchanted goods acquired in one recording period and relinquished in a subsequent period are recorded in the balance of payments of the temporary owner's economy as imports for the period in which the merchanted goods are acquired and that the same amount is deducted from imports in the period in which the merchanted goods are relinquished. In these cases, changes—from one recording period to another—in stocks of goods located abroad and valued at acquisition cost will constitute part of the ***goods*** component for the economy of the owner. Any difference between the value of the goods when acquired and when relinquished is to be entered under *merchanting and other trade-related services*. Had the merchanting transaction in the example in paragraph 191 taken place during two accounting periods (that is, if Clintonstan had purchased the goods in period 1 and sold them in period 2), the transaction would be recorded as:

Clintonstan's Balance of Payments

	Period 1		Period 2	
	Credit	**Debit**	**Credit**	**Debit**
Goods		100		–100
Merchanting and other trade-related services			10	
Reserve assets (or other appropriate financial account item)	100			110

194. The negative debit entry for imports in the second period is construed as a withdrawal from stocks held abroad. This transaction could have been recorded as a credit entry (exports) because a negative debit is mathematically equivalent to a positive credit. However, the treatment shown in paragraph 193 is preferred as this treatment ensures that, over time, an economy's transactions in goods are not "grossed up" unnecessarily.

Physical Movement of Goods and the Goods Component

195. What is the relationship between the physical movement of goods across customs or national frontiers and coverage of the ***goods*** component in the balance of payments? While there is significant correlation between goods that change ownership internationally and goods that move across the frontier, the changes and the movements do not usually occur at exactly the same times. Furthermore, certain goods that do not cross the customs border may undergo changes of ownership, whereas other goods may cross the border without changing ownership. These two situations and implications for BOP compilation are discussed in subsequent paragraphs.

Goods Not Crossing the Frontier

196. With the exception of merchanting transactions, international changes in the ownership of goods that do not cross the frontier are treated, in the balance of payments, as transactions in ***goods***. The following list contains examples of goods that might not cross the frontier but are nonetheless treated as ***goods*** because ownership has changed:

ships, aircraft, gas and oil drilling rigs, and production platforms;

goods consumed on offshore installations such as gas and oil drilling rigs and production platforms;

fish and other marine products caught and sold abroad directly from the compiling economy's ships;

goods lost or destroyed after the importer has acquired ownership but before the goods have crossed a frontier.

197. Ships and aircraft acquired by a reporting economy and put into international operation may never cross the customs frontier of the reporting economy but, on delivery, the ships and aircraft pass into the ownership of a resident enterprise and thus become part of domestic fixed-capital formation. The ships and aircraft, which are additions to the economy's capital assets, do not result from domestic production and therefore originate in imports of goods. The same is true of gas and oil drilling rigs and production platforms acquired from abroad by a resident enterprise and used in offshore operations. Such equipment may be acquired under a financial lease or be the property of a direct investment affiliate that is designated a resident enterprise. In both cases, transactions in ***goods*** should be recorded. (Refer to paragraphs 103–106 for a discussion of the treatment of mobil equipment.)

198. Once the residence of enterprises operating offshore installations (such as gas and oil drilling rigs and production platforms) is identified, any goods acquired from abroad and consumed by such installations are recorded as imports of goods by the economy operating the enterprise—even if the goods do not cross the actual frontier of that economy.

199. Fish and other marine products caught on the high seas and sold abroad directly from the compiling economy's ships are part of the compiling economy's production sold abroad and, economically, are akin to exported goods that actually cross the border of the compiling economy.

200. As change of ownership is the criterion for establishing whether a transaction in commodities has occurred, the ***goods*** component includes goods lost or destroyed after the importer acquired ownership but before the goods crossed the exporting or importing country's frontier. For example, an importer in Coonawarra takes delivery, at the establishment of the seller in Nostaw, of goods worth 1,000 units. The goods are subsequently lost before leaving Nostaw. Because the goods are lost, their value is not recorded in the trade statistics of either the exporting or the importing economy. Nevertheless, from the standpoint of both economies, a change in the ownership of real assets, which are probably exchanged for financial assets, occurs. The BOP statements (shown subsequently) of the two countries show these transactions as exports and imports of goods, even though physical movement of the goods across national frontiers does not occur. Were entries of 1,000 units (credit for Nostaw and debit for Coonawarra) not made in the ***goods*** component, each country's statement would be out of balance for this transaction. The financial movements (assumed, in this case, to be in *reserve assets*) reflecting payment for the goods are recorded whether or not the goods are successfully delivered.

	Nostaw		**Coonawarra**	
	Credit	**Debit**	**Credit**	**Debit**
Goods	1,000			1,000
Reserve assets (or other appropriate financial account item)		1,000	1,000	

Goods Crossing the Frontier Without Changing Ownership

201. With some exceptions, goods that cross the frontier without changing ownership are not covered under ***goods***. Exception are goods exchanged between a parent and a branch (or between two branches of the same parent enterprise), goods obtained under financial lease arrangements, and goods exported for processing and returned to the original exporting country. The following list enumerates categories of goods that are always excluded from the ***goods*** component—even if the goods cross the frontier. Therefore, the recommendation that all transactions between direct investment affiliates be recorded as if changes of ownership have occurred is modified to exclude these categories of goods:

(a) goods sent abroad for processing and subsequently sold to a third country

(b) goods sent abroad for repair

(c) goods sent abroad for servicing and re-export by the servicing economy and goods to which some value is added without the occurrence of a physical transformation of the goods (e.g., storage, sorting, or inspection)

(d) returned exports and imports

(e) goods shipped under operational (i.e., nonfinancial) lease arrangements

(f) transportation equipment, fishing vessels, gas and oil drilling rigs, and other mobile equipment owned by nonresident enterprises

(g) direct transit trade

(h) shipments by a specific economy to that economy's military and diplomatic establishments located outside the territory of that economy

(i) goods lost or destroyed after having crossed the frontier but before having been delivered by the exporter

(j) goods that are temporarily exported and imported but are not for sale (e.g., display equipment for trade fairs and exhibitions; art exhibits; animals for breeding, show, or racing; and stage and circus equipment)

(k) samples of no commercial value.

Reasons for the exclusion of goods in these categories are presented, with corresponding letters, in the following paragraphs.

202. *(a) goods sent abroad for processing*

The treatment of goods that are exported for processing and not returned to the economy of the original exporter is explained in detail in paragraphs 186–188. These goods are recorded under the ***goods*** component only when actual changes of ownership occur and not when such goods cross customs frontiers.

203. *(b) repairs on goods*

The recommendation of the *BPM* is that *repairs on goods* be recorded under goods but in an item seperate from *general merchandise*. However, only the value of the repairs—not the value of the goods before and after repairs—is recorded in the balance of payments. For example, the Australian Navy sends one of its ships to Singapore for a major refit. The cost of the refit is US$ 1,000,000. The following entries would be shown (in US$) in Australia's balance of payments:

	Credit	**Debit**
Goods		
Repairs on goods		1,000,000
Reserve assets (or other appropriate financial account item)	1,000,000	

The rationale for the BOP treatment of repairs on goods as transactions in goods (instead of transactions in services) is that the value added from such transactions primarily results from the provision of materials rather than from other inputs.

204. *(c) goods sent abroad for servicing and re-export*

The BOP treatment of goods sent abroad for servicing (without physical transformation of the goods) and re-export excludes these goods from the ***goods*** component. Instead, the services provided in connection with the goods are recorded under an appropriate item in the ***services*** component. For example, the servicing of aircraft is recorded under *air transport-other*, and the servicing of computer equipment is recorded under *computer and information services*. Storage, packing, and similar services are generally recorded under the *other transport-other* item of the ***services*** component. In some cases, however, it may be difficult to distinguish these goods from goods sent abroad for processing that involves physical transformation and re-export to the country of original export.

205. *(d) returned goods*

When a contract for the sale of goods is canceled after the goods have been shipped out of the exporting economy and the goods are consequently returned to the original owner, no change of ownership has taken place. In such cases, anticipation, at the time the goods originally cross the frontier, of the future return of the goods is highly unlikely. The *BPM* suggestion is that, for the sake of statistical convenience, compilers should make any adjustment necessary to eliminate such transactions from the ***goods*** component in the period when the goods are returned rather than revising entries for the period when the goods were originally (and incorrectly) recorded as exports or imports.

206. For example, during a particular period, the reporting economy's trade statistics show 100 units in returned goods (imports). These goods were exported in a prior period, and the nonresident buyer (presumably under the terms of the purchase contract) decided to return the goods to the seller in the reporting economy. The seller refunds the financial assets that he acquired at the time of the sale, so the foreign exchange holdings of the reporting economy are reduced by 100 units. How should the contra entry be made under the ***goods*** component? In the simplest terms, the return of the goods is a reversal of the change in ownership because the original seller of the commodity has repurchased it from the buyer. The return of the goods could be recorded as an import of goods, which would be denoted by a debit entry and appear thus in the balance of payments:

	Credit	**Debit**
Goods		100
Reserve assets (or other appropriate financial account item)	100	

207. However, it is suggested in the *BPM* that the contra entry to the decrease in reserve assets should be a negative entry in exports. BOP entries would be:

	Credit	**Debit**
Goods	–100	
Reserve assets (or other appropriate financial account item)	100	

The negative adjustment to the reporting economy's flows of goods in the current period is designed to reverse the change of ownership and to eliminate it from the balance of payments as if a change of ownership had never occurred.

208. If trade statistics are the source from which exports and imports are derived, the value of goods purchased and returned in the same period should be eliminated from total exports and total imports for that period.

209. *(e) operational lease arrangements*

Although goods shipped under operational (rather than financial) leases may physically move across national frontiers, these goods are excluded from coverage under the ***goods*** component. The lease payments due on these goods are recorded as *other business services-operational leasing* in the ***services*** component.

210. *(f) transportation equipment*

Excluded from the ***goods*** component—even though physical movement across national frontiers occurs—are transportation equipment, fishing vessels, gas and oil drilling rigs, and other items of mobile equipment that are operated in a host country's domestic territory or territorial waters but owned by nonresident enterprises. (Refer to chapter 2 of this *Textbook* and chapter 4 of the *BPM* for discussions on the residence of owners.) However, for BOP purposes, a change of ownership is said to occurr if (1) a resident enterprise operates mobile equipment under a financial lease arrangement or (2) a nonresident owner of mobile equipment separately accounts for the long-term operations of the equipment in the host country and the equipment is recognized by host country authorities as part of capital stock. In the first case, ownership is assumed to pass from the lessor to the lessee; in the second case, ownership is assumed to pass from the parent enterprise to a branch that is resident in the host economy.

211. *(g) direct transit trade*

Direct transit trade refers to goods that pass through a reporting country lying on a route between origin and destination. For instance, goods exported by the United States to Switzerland may be shipped to Rotterdam in the Netherlands and then sent by barge on the Rhine to Switzerland. Such goods are regarded as direct transit trade by the Netherlands and are omitted from the external trade statistics and balance of payments of that country. In such cases, there are no transactions in goods between nonresidents and residents of the country of transit. However, any transactions in transportation or any other services rendered by Netherlands residents in connection with goods in transit are recorded in the ***services*** component of the balance of payments of the Netherlands.

212. *(h) shipments to diplomatic and military establishments*

Although the goods move across national boundaries, shipments from an economy to extraterritorial military and diplomatic establishments of that economy are considered transactions between residents and are therefore excluded from the balance of payments.

213. *(i) goods lost or destroyed before change of ownership occurs*

Goods lost or destroyed inside the customs frontier of the importing economy will be recorded in the international trade statistics (ITS) of both the exporting and importing economies. Adjustments should be made to the statistics of both economies if the loss or destruction of goods took place before change of ownership occurred. Goods lost or destroyed between the customs frontiers of exporting and importing economies will be recorded in the exporting economy's ITS but not in those of the importing economy. An adjustment should be made to the statistics of the exporting economy if the loss or destruction of goods took place prior to a change of ownership. Goods lost or destroyed inside the customs frontier of the exporting economy will not be recorded in the ITS of either the exporting or importing economy. No adjustment to the statistics is required if no change of ownership occurs.

214. *(j) goods temporarily exported and imported*

Goods temporarily exported and imported and not intended for sale (for example, display equipment for trade fairs and exhibitions, art exhibits, and animals for breeding) are also excluded from the ***goods*** component on the grounds that no change of ownership occurs between residents of different economies. Although these goods cross national frontiers, there is an expectation that goods shipped for such purposes will be returned.

Time of Recording

215. The provision and acquisition of goods by an economy should be recorded in the balance of payments of that economy in the period in which the change of ownership takes place. The time assigned to a change in the ownership of goods is the time at which the two parties to the transaction record it in their books. The change of ownership criterion employed for the ***goods*** component is designed to promote and preserve consistency between the recording of goods and other items (particularly financial items) in the balance of payments.

216. Neither the physical movement of goods, on which customs statistics and similar returns are largely based, nor payment for goods, which is reflected in foreign exchange or banking system records, will necessarily coincide with the time that ownership of the goods changes. Timing adjustments necessary for statistics derived from these two sources are detailed in paragraphs 257–280. Except in the case of large, discrete transactions (such as deliveries of ships or aircraft), the appropriate adjustments are often difficult to make. Information on the actual time that ownership changes is seldom available in a form that can be related to times of physical movement or payment for goods. However, if the total value of trade, the regional pattern of trade, and/or the terms of payment for trade at the beginning of the recording period change substantially by the end of the period, failure to make adjustments for timing is likely to be a major source of error in BOP statements. Timing differences in the recording of goods by different countries produce asymmetry between totals for world exports and imports.

217. Consignment goods that are intended for sale but are not actually sold at the time the goods cross the frontier of the compiling economy should (in principle) be included in ***goods*** only at the time when ownership changes. As a matter of convenience and in the expectation that a change of ownership will occur shortly thereafter, such goods are sometimes recorded at the time that they cross the frontier. If that treatment is used and the expected change of ownership does not materialize, the goods are returned to the exporting country. Then the goods must be recorded, by means of the procedure suggested in paragraphs 205–208, as a deduction from exports and imports. If such an adjustment is made in a period following the period in which the goods were originally consigned, timing errors will be introduced into the balance of payments. Furthermore, for goods that are actually sold after having been consigned, there will be timing errors to the extent that sales take place in periods that differ from the periods in which the goods were consigned.[8]

Valuation

218. The value at which goods are recorded in the balance of payments is the market value of the goods at the place of uniform valuation, which is the customs frontier of the economy from which the goods are exported. At least two aspects of this general statement require elaboration.

Market Valuation

219. The concept of market value and the specific application of the concept to internationally traded goods are discussed in chapters 5 and 10 of the *BPM*. The United Nations, in connection with its standards for related statistics, has dealt at length with the issue of valuing exports and imports. The Customs Cooperation Council has also provided an extensive analysis of the standards to be applied for customs valuation of imports. Paragraphs 282–286 also pertain to application of the market value concept to goods and to reconciliation of the standards of the United Nations and the Customs Cooperation Council with those recommended in the *BPM*.

Point of Valuation

220. Goods are provided or acquired when ownership passes from a resident of one economy to a resident of another; transfer of ownership is synonymous with delivery by an exporter or exporter's agent to an importer or importer's agent. The delivery of goods may take place at any time and any place agreed upon by the exporter and importer. "Time and place" may vary between the point at which the exporter originally produces or acquires the commodity and the point at which the importer consumes the commodity or provides it to a third party.

221. The value assigned to a transaction in goods depends on when and where the transaction is valued. The simplest point for valuing goods is at time and place of delivery. At any other point, valuation may (1) fail to cover the total value of the goods and services being provided by residents of one economy to residents of another economy or (2) fail to exclude from that value additional goods and services transferred between residents of the same economy.

222. For example, an exporter in Domestica contracts to deliver goods to an importer in Cromania. The contract requires the exporter to deliver the goods at the establishment of the

[8]Timing errors will occur because, in the period in which the goods are consigned, entries for the initial consignment will not be offset by entries in the financial account. Instead, the offsetting entries will be recorded in a subsequent period when the goods are actually sold (or returned to the exporter).

importer. The cost of the commodity and associated distributive costs are:

Value of commodity at place of production in Domestica	2,000
Cost of transportation to the border of Domestica	50
Cost of transportation from the border of Domestica to the border of Cromania	200
Transportation cost from border of Cromania to the establishment of the importer	25

Road transportation in Domestica is provided by a resident carrier of Domestica. Ocean transportation is provided by a resident carrier of Daniherland. The inland freight in Cromania is purchased by the exporter from a railroad enterprise in Cromania. The value of the commodity at the place of delivery in Cromania is the sum of all the separate cost elements (2,275 units). If any other point of valuation (such as the establishment of the exporter, the frontier of the exporting economy, or the frontier of the importing economy) were selected, the value placed on the goods would not include all of the services acquired by Domestica and provided, during the delivery of the goods to the Cromanian importer, to Cromania. Valuing the transactions at the point of delivery results in the following BOP entries:

	Domestica		**Cromania**	
	Credit	**Debit**	**Credit**	**Debit**
Goods	2,275			2,275
Freight		225	25	
Reserve assets (or other appropriate financial account item)		2,050	2,250	

223. Under a different scenario, contract terms could call for the importer to take delivery of the goods at the establishment of the exporter. All costs of transportation and other related distributive costs are direct purchases by the importer. The value of the goods at the time and place of delivery is 2,000 units. Failure to select this valuation point could result in the inclusion, in the value of the goods, of services that are not actually provided by Domestica to Cromania. In this case, the distributive services acquired by the importer are provided in part by Domestica, in part by Daniherland, and in part by other residents in Cromania. Valuing the transaction in goods at the point of delivery would result in the following BOP entries:

	Domestica		**Cromania**	
	Credit	**Debit**	**Credit**	**Debit**
Goods	2,000			2,000
Freight	50			250
Reserve assets (or other appropriate financial account item)		2,050	2,250	

224. While a convention of valuing goods at the point of delivery may have merit from the standpoint of registering flows (between residents and nonresidents) of goods and services, such a convention imposes severe problems with regard to the interpretation, and possibly the availability, of data. If goods were valued in accordance with the varying terms of individual contracts, the goods might be recorded *free on board* (f.o.b.) at some inland point in the exporting country; or f.o.b. at the customs frontier of the exporting country; or *cost, insurance, and freight* (c.i.f.) at the frontier of the importing country; or c.i.f. at some inland point of the importing country. Statistical trends reflecting economic developments could be masked by data changes that were merely the result of changes in the time or place at which deliveries of most goods were recorded. The distortion of other statistics (such as data on freight transactions) associated with transactions in goods would be proportionately much greater. From a practical and analytical standpoint, it is desirable to distinguish, on the basis of a uniform principle, between (1) goods and (2) related distributive transactions.

225. A possible approach would be to adopt the uniform physical valuation point utilized for construction of input-output tables. In these tables, the value assigned to a commodity is the market value of that commodity when it is located at the establishment of the producer. Any other services (such as transportation and distribution) performed in relation to the commodity are viewed as ancillary services supplied to the final or intermediate consumer of the commodity. Such an approach attempts to differentiate between (1) commodity output and (2) the rendering of services. In the example given in paragraph 222, use of this approach would produce the following BOP entries for Cromania:

	Credit	**Debit**
Goods		2,000
Freight		250
Reserve assets (or other appropriate financial account item)	2,250	

226. Use of this approach to distinguish between goods per se and related freight services is analytically appealing but difficult to implement statistically—especially for series of data produced at frequent intervals. It is assumed that inter-industry accounts can be used as a basic statistical framework in which flows of goods and services are integrated. With a few exceptions, most countries do not construct input-output tables on a quarterly, or even an annual, basis. Quarterly BOP estimates are necessary for appraising current developments, and statistical sources from which totals of goods are derived must supply data on a quarterly (or at least annual) basis.

227. As it is desirable to adopt a uniform point of valuation for the ***goods*** component, some other approach must be recommended for producing quarterly or annual data. According to the *BPM*, the value existing at the customs frontier of the economy from which goods are exported shall, in principle, be the value recorded (in the ***goods*** component of the balance of payments) for goods and related distributive services. The value includes the costs of loading goods on board carriers at the frontier. (That is, exports and imports of goods are to be valued f.o.b. at the customs frontier of the exporting country.) In the application of this rule, customs bonded warehouses, customs bonded manufacturing plants, and free areas are considered to be within the customs frontiers of the economies that control and supervise them. Customs frontiers need not coincide physically with national boundaries and may be located in the interior at places such as airports.

228. Use of the *BPM* rule on uniform valuation of transactions in goods involves two theoretical concepts: (1) Freight, insurance, and other shipment charges incurred for transporting goods to the point of uniform valuation are always the result of transactions between a resident (usually the exporter) of the exporting economy and the carrier or insurer. (2) Similar costs incurred for transporting goods beyond the point of uniform valuation are always the result of transactions between the importer and the carrier or insurer.

229. The example given in paragraph 223 illustrates the system of entries made if the customs border of the exporting economy is designated as the uniform physical point for valuing goods. The exporter is located in Domestica; the importer, in Cromania; and the carrier, in Daniherland. (Valuation of the goods would be unchanged by different locations for contractual delivery.)

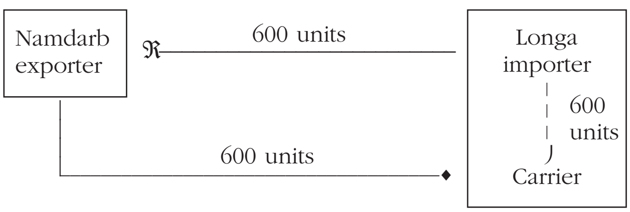
	Domestica		**Cromania**		**Daniherland**	
	Credit	**Debit**	**Credit**	**Debit**	**Credit**	**Debit**
Goods	2,050			2,050		
Freight				200	200	
Reserve assets (orother appropriate financial account item)		2,050	2,250			200

230. In the example, the importer in Cromania took possession of the goods at the establishment of the exporter in Domestica and purchased, from a carrier resident in Domestica, transportation services for moving the goods to the customs border of Domestica. In reality, these transportation services would have been contracted between the carrier and the importer. However, use of a uniform physical point for valuation of goods in the balance of payments requires that the internal transportation cost of 50 units be attributed to a transaction between residents of Domestica—the exporter and the carrier. In this particular case, the total domestic product of Domestica is provided to Cromania in a single component, ***goods***, rather than as a composite of ***goods*** and *transportation*. Although it is possible that nonresidents may, in fact, provide freight services inside the valuation boundary, this circumstance arises rather infrequently. Such a transaction (illustrated in the following paragraph) would arise if an importer hired, in his or her country, a truck to transport goods from a location in the exporting country.

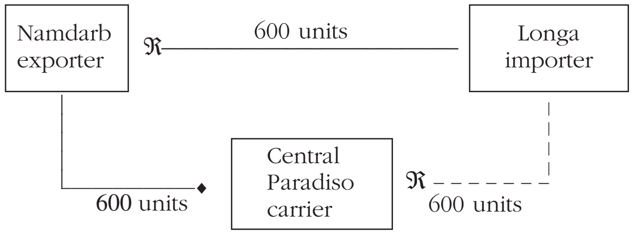
231. Clinstonstan and Bushland are contiguous countries. The importer, a resident of Bushland, takes delivery of goods worth 1,000 units at the establishment of the exporter in Clintonstan. The importer arranges with a trucking company in Bushland to transport the goods to her place of business in that country. Total transportation cost is 200 units, of which 100 units are the estimated cost of moving the goods from the exporter's establishment to the border of Clintonstan. In this case, the freight payment is a transaction between residents of the importing country. In accordance with the convention for distinguishing between goods and associated distributive costs in a uniform and consistent manner, the freight cost for transporting the goods to Clintonstan's border is included in the value of the goods when that value is recorded in the BOP statements of both countries. Consequently, it is necessary to make offsetting entries in the BOP statements of both countries to correct the overstatement of receipts and payments. A freight debit that cancels the overstatement of export receipts is recorded in the balance of payments of the exporting country. (The offsetting element represents a transaction between nonresidents.) In the importing country's BOP statement, the offsetting entry is a freight credit representing a transaction between residents and canceling the overstatement, on the goods account, of payments to nonresidents.

232. The second theoretical concept required by the use of a uniform physical point for valuation of goods is closer to fact. The exporter is regarded as an intermediary in arranging for goods to be shipped beyond the frontiers of his country. If the exporter pays freight charges, he is assumed to do so on behalf of the nonresident importer, who ultimately reimburses the exporter directly or indirectly.

233. For example, a purchaser in Longa agrees to pay a seller in Namdarb 6,600 units for a commodity delivered c.i.f. at the port of entry in Longa. The seller contracts with a Longan carrier to transport the goods for 600 units. Longa, however, wishes to record imports on an f.o.b. basis and therefore considers the 6,000 units to be the price of the commodity and the 600 units to be payment for transportation. There is no problem in recording the 6,000–unit value of the import; this amount is paid to the exporter in Namdarb, and the transaction is completed. The 600 units for transportation, however, are paid to the exporter in Namdarb, who returns the 600 units to Longa in the form of payment to the carrier. (The route of the 600 units is shown in solid lines in the following diagram.) From an economic point of view, however, the transportation service is performed by a resident of Longa (the carrier) for a resident of Longa (the importer). There is no economic significance to the payment being made directly by one resident to another resident or through some nonresident intermediary (the exporter) and, on an overall basis, the balance of payments is not affected. (The significant movement of the 600 units is shown in the diagram, by the broken line and arrow, as a transaction occurring within Longa.)



234. Similar reasoning would apply if the goods were transported in the ships of a third economy. For example, the exporter in Namdarb pays shipping charges to a carrier in Central Paradiso and is reimbursed by the Longan importer (as is indicated in the following diagram). The transportation service is viewed as being rendered to the importer rather than the exporter, who may be regarded as an intermediary. In accordance with the "real flows" principle, the significant movement of the transportation service is from Central Paradiso to Longa. The two offsetting movements in Namdarb's balance of payments (payment of 600 units to Central Paradiso and receipt of the same amount from Longa) are, therefore, excluded from Namdarb's balance of payments.



235. Freight, insurance, and other distributive payments made by residents of the exporting country to nonresidents for the transport of goods beyond the customs frontier of the exporting country are therefore omitted from the balance of payments of the exporting country. Also omitted are the direct or indirect reimbursements made by nonresident importers for such expenditures. While the omission of these transactions may be regarded as unimportant in the majority of cases, the omission in other cases is a clear departure from the resident/nonresident principle. However, as the amounts omitted from the credit and debit sides of the balance of payments are equal, the net balance is not affected.

236. Treating the exporter as an intermediary who arranges for transportation of goods beyond the frontier of the exporting country seems realistic when goods are sold to the nonresident importer before being shipped from the exporting country. This treatment is not so realistic when goods are sold while en route or upon arrival in the importing country. The treatment is clearly unrealistic when goods are shipped on consignment and stored (for the exporter's account) in the importing country before being sold there.

237. Another example illustrates some of the problems described in the preceding paragraph. An exporter in Pokolbin ships goods on consignment to an agent in Coonawarra for sale in that economy. The value of the commodities upon arrival in Coonawarra is 10,000 units, of which 1,000 units represent the cost of shipping the goods from Pokolbin to Coonawarra. Residents of Cromania have provided freight services. If these goods are sold in the same reporting period, the BOP statements of Pokolbin and Coonawarra will (measurement problems notwithstanding) include the following entries:

	Pokolbin		Coonawarra	
	Credit	**Debit**	**Credit**	**Debit**
Goods	9,000			9,000
Freight				1,000
Financial assets/ liabilities		9,000	10,000	

238. The recording of flows of goods and the attribution of associated distributive costs is based on the uniform point of valuation recommended in the *BPM*. Although the direction of the financial flow in its entirety is from Coonawarra to Pokolbin, the direction of "real flows" is, in part, from Pokolbin to Coonawarra and, in part, from Cromania to Coonawarra. The balance of payments of Pokolbin omits from credit and debit entries the 1,000 units of freight services that the exporter in Pokolbin contracted for with a resident of Cromania. In this case, the exporter clearly was not acting as an intermediary for the importer because the goods had not been sold at the time the freight services were contracted.

239. If, the goods in the example in paragraph 237 were consigned in one reporting period and sold in a subsequent reporting period, BOP entries for the three economies would (measurement problems not withstanding) be:

Period 1	Pokolbin		Coonawarra		Cromania	
	Credit	**Debit**	**Credit**	**Debit**	**Credit**	**Debit**
Goods						
Freight		1,000			1,000	
Financial assets/ liabilities	1,000					1,000

Period 2	Pokolbin		Coonawarra		Cromania	
	Credit	**Debit**	**Credit**	**Debit**	**Credit**	**Debit**
Goods	9,000			9,000		
Freight		–1,000		1,000	(1,000 –1,000)	
Financial assets/ liabilities		10,000	10,000			

240. The negative entry shown for freight during period 2 denotes an adjustment to the services acquired by Pokolbin during period 1. As the *BPM* specifies that the shipment of imports beyond the border of the exporting country represents a transaction between the provider of the service and the importing economy, these flows should be attributed to Coonawarra and Cromania—regardless of the fact that the goods were not sold until the period following shipment.

241. An appropriate valuation for the goods item in period 2 could have been 10,000 units as that is the value of production supplied by Pokolbin to Coonawarra. However, the specification, by the *BPM*, of a place (the customs boundary of the exporting country) for the uniform valuation of goods precludes assignment of the 10,000–unit value to the goods.

242. In summary, it was desirable to designate a point at which goods should be uniformly valued. Any of several points could have been chosen as each has comparable analytic advantages. However, statistical problems exist with any valuation point selected. A principal difficulty is that shipping practices are not standard. Documents on which the BOP compiler must usually rely to make estimates of goods and freight will often cover shipping services performed on both sides of the customs frontier (or any other uniform point), and total shipping costs may not be broken down or related to the point of valuation. For example, goods may be shipped by truck from door to door, or goods in containers may be moved between central warehouses that are distant from customs frontiers. A primary consideration in specifying the customs frontier of the exporting country (rather than some other place) is the probability that customs officials value exports at that point. Imports, too, are valued at the customs frontier in a significant number of countries. As data generated by customs are often the basis of BOP entries pertaining to transactions in goods, it is convenient for both series to refer to this point of valuation.

243. Application of the rule for uniform valuation may result in inclusion, in the ***goods*** component, of some flows of services occurring between nonresidents or between residents of the same economy. Specifically, an exporter may deliver goods before the goods reach the customs frontier of the exporter's economy, and the importer may then employ a supplier of distributive services who is not a resident of the exporting economy to ship the goods to the customs frontier. To maintain uniform valuation for the ***goods*** component, an offset to such a flow of services occurring between nonresidents is required in the balance of payments of the exporting country. The *BPM* states that the offsetting entry is made in the freight item. Similarly, if the supplier of the services is the importer or a resident of the importer's economy, the flow of services occurs between residents of the same economy, and an offset in the freight item is also required in the balance of payments of the importing country.

244. The f.o.b. valuation of goods at the customs border of the exporting country includes any costs incurred in loading the goods on board the carrier at that frontier. However, when the service of loading goods on board the carrier at the customs frontier is actually performed, the service is frequently performed by or for the carrier. In these cases, customs statistics are likely to exclude the cost of such services, and data on freight charges will almost certainly include them. For practical reasons, the BPM does not suggest that attempts be made to reallocate such charges from the freight item to the **goods** component. There is explicit recognition that, in practice, most goods are recorded on a *free alongside ship* (f.a.s.), rather than an f.o.b., basis.

245. Goods delivered to an importer at some location within the exporting economy may not be shipped to the customs frontier of that economy during the same recording period. In such a case, an entry for the value of the goods at the point of delivery is made in one period, and another entry for the cost of freight from that point to the customs frontier is made in a subsequent period. Both of these entries are included in the ***goods*** component.

246. There may be practical difficulties in readily distinguishing the distributive service element in imports that are valued on a c.i.f. basis in the basic data source. However, users of the balance of payments would experience real inconvenience if there were no single standard. Lack of comparability between statements compiled on different bases is perceived as a more serious drawback than difficulties (or errors) in allocating certain flows between the ***goods*** component and freight items. Therefore, the *BPM* rule for uniform recording of goods should be followed—even if adherence involves rough estimates.

247. How should services performed by agents in connection with transactions in goods be treated? In principle, fees and commissions paid by exporters to nonresident brokers and agents reflect services rendered to exporters by brokers or agents, and these fees and commissions are classified as such in the balance of payments. Thus, for example, fees paid to nonresident agents by exporters are entered as an integral part of the value of goods (credit) and an offsetting entry (debit) is made in *merchanting and other trade-related services*. For the importing country, these entries are reversed if the agent is a resident of the importing country.

248. What about services rendered to an importer by an agent in the exporting country? Are these services separately portrayed as service items or included in the values of goods? Likewise, how are fees paid by an importer to a resident agent for services pertaining to imports treated in the balance of payments? Are these services—although they may be included in the customs values of imports—construed as transactions between residents? It is recommended in the *BPM* that, for practical reasons, fees paid in connection with transactions in goods by the importer to an agent in the exporting country be included in the value assigned to goods at the customs frontier of the exporting economy. These fees are usually included in the customs values of imports; the exporting country will probably have to add these fees to the customs values of exports. Agent fees paid by the importer to an agent in the importer's country or to an agent in a third country are not included in the value of imports. If these fees are included in customs valuations, the fees should be deducted. This recommendation is made because the exporting country cannot know the value of these fees and therefore cannot incorporate the fees in the customs values of exports. The treatment of agent fees is further discussed in chapter 5.

249. In some cases, fees are paid by exporters to consulates of importing countries. The *BPM* rule is that such fees are not included in the valuation of goods at the frontier of the exporting country. A consular fees is thus treated as a cost incurred beyond the customs frontier of the exporting country; that is, a consular fee is incurred in the importing country.

Adjustments to Basic Data

Overview

250. Basic data from which statistics on the ***goods*** component are derived are seldom available in a form that fits concepts presented in the *BPM*. The two most common sources are external trade statistics, which are usually derived from customs records, and bank records, such as records of foreign exchange transactions. Statistics obtained from these two sources are, or were, collected for purposes other than BOP compilation. Trade statistics based on customs returns are generated as a by-product of customs administration, and exchange records are primarily used as a means of monitoring and controlling foreign exchange. To satisfy *BPM* requirements for compilation of the ***goods*** component of the balance of payments, compilers must usually make adjustments to source data.

251. Discussed in the following paragraphs are adjustments that must be made to compensate for conceptual differences between the ***goods*** component and external trade statistics for which coverage, valuation, and timing are defined by the United Nations,[9] and between the goods component and foreign exchange and similar bank record data covering (at the time of settlement) all transactions in goods paid for through the banking system.

252. However, trade statistics and bank records available to BOP compilers may not conform entirely to the definition stated by the United Nations. Compilers should not adjust source data to conform to these definitions and subsequently adjust data further for use in the balance of payments. Adjustments described in the *Textbook* should be applied only when source data already conform to the United Nations definition and are, thereby, at variance with BOP definitions. Other discrepancies between source data and the ***goods*** component should be eliminated.

253. Adjustments to bring source data into conformity with standards for compilation of the ***goods*** component of the balance of payments are described under the headings of coverage, classification, timing, and valuation. (For additional information on these adjustments, refer to chapter 11 of the *Balance of Payments Compilation Guide.*)

Adjustment for Coverage

254. Coverage adjustments are required when statistics that are the source of BOP ***goods*** component entries (a) include certain goods that have not, in fact, changed ownership and (b) fail to include certain other goods that have, in fact, changed ownership internationally. If external trade statistics are the source of information on transactions in goods, such statistics usually cover all goods that cross the border. To adjust external trade statistics for use in the balance of payments, additions must be made for goods that change ownership (or are construed as changing ownership) without crossing the border, and deductions must be made for goods that cross the border without changing ownership. If foreign exchange records are the source of information on transactions in goods, such data generally cover all goods that are paid for through the banking system. Therefore, additions to foreign exchange and similar bank record data must be made when payment is not made through the banking system for goods that change ownership.

Adjustments for Classification

255. In source data, some transactions may be inappropriately—for BOP purposes—classified as transactions in goods. In addition, transactions that are, for BOP purposes, classified under goods may be otherwise classified in source data. Adjustments are required to correct the improper classifications.

256. One important classification adjustment is the deduction of distributive items from import totals obtained from external trade statistics. When imports are recorded in external trade statistics at c.i.f. valuations that include international freight, insurance, and other distributive services, such services must be eliminated so that goods may be recorded at f.o.b. valuations in the balance of payments. If such services have been provided by nonresidents, the values that have been deducted are included in the freight item or the insurance item or, as appropriate, in other items under services. Certain import transactions may also be valued on a c.i.f. basis (or some basis other than f.o.b.) in bank records. Classification adjustments should be made in these statistics as well.

Adjustments for Timing

257. Timing adjustments are required for BOP purposes when flows of goods are recorded in source data at times that do not coincide with changes in ownership. Goods are usually recorded in external trade statistics when the goods cross the border. Goods are recorded in bank records when payment for the goods is made through the banking system. The time at which the ownership of goods changes may differ from the time at which goods physically move across a border or the time at which payment for the goods is made.

258. For example, an exporter in Essendonia ships goods to an importer in Nostaw in December 1991. The importer in Nostaw acquires ownership of the

[9]"International Trade Statistics: Concepts and Definitions," *United Nations Statistical Papers*, Series M, No. 52, Rev.1 (New York, 1982).

Table 4.1 Timing Adjustments for External Trade Statistics Used as Source Data for BOP *Goods* Component Entries

	Period in Which Goods		Period in Which Adjustment Is Made to Data on Goods		
	Change Ownership	**Cross Frontier**	**Previous**	**Current**	**Subsequent**
Exports					
1	subsequent	current	none	deduction	addition
2	current	previous	deduction	addition	none
3	current	subsequent	none	addition	deduction
4	previous	current	addition	deduction	none
Imports					
5	current	subsequent	none	addition	deduction
6	previous	current	addition	deduction	none
7	subsequent	current	none	deduction	addition
8	current	previous	deduction	addition	none

goods in January when she receives documents forwarded to her bank for collection and accepts, as an account payable, a three-month draft falling due in April 1992. The goods are cleared through customs in Nostaw in March 1992.

Summary of Events

December 1991—exports recorded in customs returns of Essendonia
January 1992—goods change ownership; importer in Nostaw accepts draft as an account payable
March 1992—imports recorded in customs returns of Nostaw
April 1992—draft paid

259. According to the timing principle stated in the *BPM*, a transaction in goods should be recorded, in the balance of payments of both Essendonia and Nostaw, in January. Simultaneous entries ensure that the transaction is recorded symmetrically and on a basis consistent with transactions in the ***financial account*** of each country's balance of payments. In the balance of payments of Essendonia, the export (credit) is offset by the acquisition of a draft (a debit to trade credits). In the balance of payments of Nostaw, the import (debit) is offset by the corresponding increase in trade credits (credit).

260. If external trade statistics in which Essendonia and Nostaw record this transaction serve as source data for BOP entries, a timing adjustment is required only in Essendonia. (It is assumed that Nostaw prepares its BOP statement on a quarterly basis.) The adjustment is made by eliminating the export from 1991 statistics and adding it to 1992 statistics. As both the change of ownership and the recording of the transaction by Nostaw customs officials took place during the first three months of 1992, no timing adjustment is required in Nostaw unless BOP statements are prepared monthly, rather than quarterly, in that country.

261. If bank records in which this transaction is recorded serve as the source from which BOP entries are derived and if quarterly BOP statements are prepared, a timing adjustment is required in the balance of payments of both Essendonia and Nostaw. Whereas bank records attribute the transaction in goods to April (when settlement was made through the banking system), the actual change of ownership took place in January. The adjustment is made by deducting the amount of the transaction from April totals and adding the amount to January totals. Thus, the use of timing adjustments applies to source data from external trade statistics and from bank records.

262. Table 4.1 summarizes timing adjustments that should be made when data from external trade statistics are used as a source for BOP entries in the ***goods*** component.

263. Table 4.1 shows additions and deductions that must, for the purpose of compiling imports and exports for the balance of payments, be made to external trade statistics in various periods. Adjustments made for a current period may require offsetting adjustments in previous or subsequent periods. As line 1 of table 4.1 indicates, when exports move across the frontier in the current

Table 4.2 Timing Adjustments for Bank Records Used as Source Data for BOP *Goods* Component Entries

	Period in Which		Adjustment Made to Current Period Data on Trade Credit		
	Ownership Changes	**Payment Is Made**	**Goods**	**Assets**	**Liabilities**
Exports					
1	subsequent	current	deduction	none	addition
2	current	previous	addition	none	deduction
3	current	subsequent	addition	addition	none
4	previous	current	deduction	deduction	none
Imports					
5	current	subsequent	addition	none	addition
6	previous	current	deduction	none	deduction
7	subsequent	current	deduction	addition	none
8	current	previous	addition	deduction	none

period and change of ownership occurs in a subsequent period, the amount of the transaction in goods is subtracted from the external trade statistics of the current period and added to the statistics for the period in which the goods are sold. The physical movement of goods across the frontier does not alter the ownership of the goods; goods that do not change ownership before crossing the frontier are considered an addition to the exporting economy's stocks held abroad.

264. According to the conventions of the 1993 SNA and the BPM, capital formation in the form of commodity stocks can take place abroad. If goods that are shipped abroad but not sold in the current period relate to current production, the reporting country's domestic product should include an addition to stocks, rather than an export, as indicated by external trade statistics of the current period. The decline in stocks and the actual exports are reflected in the period in which the goods are sold (see line 2 of table 4.1).

265. If goods sold in the current period are shipped abroad in a subsequent period (see line 3 of table 4.1), the reporting economy should add the amount of the transaction in goods to exports of goods for the current period. The nonresident importer would add the goods located in the compiling economy to his stock of goods. These goods should be subtracted from the external trade statistics of the reporting economy for the period in which the goods are shipped (see line 4 of table 4.1). The nonresident importer would then have drawn down his stock of goods held in the reporting economy.

266. Line 5 of table 4.1 illustrates changes, which come about through purchases made abroad, in a country's stocks held abroad. Goods bought in the current period are shipped to the importing country in a subsequent period. The amount of the transaction in goods is added to the external trade statistics for the current period and deducted from the statistics for the period in which the goods cross the frontier of the importing country. There is a reduction in stocks held abroad during the period in which the goods physically enter the country (see line 6 of table 4.1).

267. Some goods do not change ownership until sometime after they arrive in the reporting country. For BOP purposes, these goods are said to be owned by nonresidents from the time the goods arrive until the goods are sold. A deduction is therefore made to exclude the amount of such goods from the external trade statistics of the compiling economy (see line 7 of table 4.1). An addition to the statistics is subsequently made for the period in which the goods are purchased by residents (see line 8 of table 4.1). Both of these adjustments are linked to changes in stocks held by nonresidents in the compiling economy.

268. Table 4.2 summarizes timing adjustments that should be made when data from foreign exchange and similar bank records are used as a source for BOP entries in the **goods** component.

269. Table 4.2 shows additions and deductions that must, for BOP purposes, be made to bank records containing data on exports and imports as well as adjustments that must be made to transactions in trade credits. Trade credit adjustments follow from and serve as offsets to timing adjustments made for exports and imports. As table 4.2 indicates, when banking system data such as foreign exchange records are used to derive the BOP **goods** component, timing adjustments are made to trade credits rather than to changes in stocks. Trade credits may be postpayments (when payment is made after the change in ownership) or prepayments (when payment precedes the change of ownership).

270. Line 1 of table 4.2 refers to prepayments received for exports. Prepayments are not classified as export receipts but as trade credits received (liabilities). These prepayments are deducted from total exports of goods (as shown in bank records), and a corresponding increase in *trade credit liabilities* is entered in the balance of payments. Upon delivery of the goods (see line 2), the prepayment amounts are added to the bank record figure for current year exports, and a corresponding entry is made in the BOP ***financial account*** to record liquidation of the liabilities.

271. When exported goods change ownership before payment is rendered (see line 3), an addition must be made to the bank record figure for exports of goods. The resulting amount is recorded in the balance of payments as a reduction in real assets (exports), and an offsetting increase in financial assets (trade credits) is also recorded. Line 4 refers to adjustments made in the current period when payment is received for exports delivered in a previous period.

272. A country may acquire ownership of goods in the current period and pay for the goods in a subsequent period (see line 5). When postpayments for goods are made, the figure (contained in the importing country's bank records) for imports of goods in the current period must be adjusted by the addition of an amount representing goods imported but not yet paid for. A contra entry must be made in the balance of payments under trade credit liabilities. When goods are paid for through settlement of the trade credit (see line 6), the import total (shown in bank records) for the period in which payment is received must be adjusted to exclude the amount of the settlement. The settlement is recorded as a financial transaction (reduction in trade credit liabilities).

273. When prepayments are made for imports (see line 7), such prepayments are deducted from the estimates of goods contained in bank records and shown in the balance of payments as the creation of a financial claim (assets). When the imports are received (see line 8), the prepayment amounts are added to the amount recorded for goods in bank records, and a contra entry representing the corresponding reduction in trade credit assets is made.

274. If unadjusted statistics from bank records were used in the balance of payments, a number of errors and omissions would ensue. A significant number of transactions in goods would be recorded in the wrong period. Serious omissions would occur in the recording of increases and decreases in international indebtedness as total trade credits for an entire country can constitute a sizeable amount and change rapidly. Statistics portraying the economic relationship between output and capital would be distorted, and an incorrect ratio would be implied.

275. While the principles and the importance of timing adjustments should be understood and appreciated, in practice, it is not always possible to make these adjustments. When basic data for transactions in goods are derived from customs returns, it is generally assumed that there is a rather constant time lag between actual change of ownership and entry of the goods in customs records. No timing adjustments would be required if (1) the level of trade and (2) the lag between change of ownership and recording by customs both remained constant. If trade were expanding or contracting, however, timing adjustments would probably be necessary if substantial time lags existed—even if such lags were constant. If trade were constant, changes in time lags might also create the necessity for major adjustments.

276. There is no clear evidence that changes of ownership normally take place when goods are shipped (in which case a timing adjustment for imports may be required) or when goods arrive at their destination (in which case a timing adjust for exports may be required). A sample survey could be used to obtain information on actual practices in different countries. Timing adjustments could then be made to correct statistics in categories of goods for which changes of ownership and customs entries are recorded at different times. If BOP statistics do not reflect simultaneous recording of exports and imports, aggregations and comparisons of such BOP data are much less meaningful. Discrepancies in times of recording are most apt to arise in periods when rapid changes are occurring in prices, in volumes, or in relationships between the times that goods change ownership and are recorded in source data.

277. In practice, timing adjustments are made to data generated by customs only when it is known that the time at which goods were recorded in customs documents differs from the time at which ownership of the goods changed. It may be necessary to obtain direct records of purchases or sales and to substitute such records for customs documents. For example, wheat is shipped by Canada to the United States for storage. Usually, none of the wheat is sold to the United States; instead, the wheat is sold overseas and shipped directly from the storage location. Shipments of wheat for storage are eliminated from exports in Canada's balance of payments, and wheat sales from storage abroad are added to exports on the basis of special reports obtained from the Canadian Wheat Board. A second example is that of Colombian coffee. The Colombian Coffee Growers Association provides data that enable Colombian BOP compilers to adjust customs returns in respect of coffee stocks held abroad. In countries where marketing boards or special procurement agencies exist, data on actual sales and purchases are often available and can, if necessary, be substituted for customs data.

278. Timing adjustments may also be made to data generated by customs when a single or discrete bulk commodity purchase (especially transportation equipment) is made by an official entity or a large corporation in the reporting country. For example, Australia makes a timing adjustment to the external trade statistics to compensate for the time lag between the acquisition, by Australian enterprises, of items such as aircraft and the recording of the aircraft in the customs returns.

279. The necessity for timing adjustments is much greater when foreign exchange or other bank records serve as the source of data on transactions in goods. Unadjusted statistics for transactions in goods may be misleading if substantial changes have occurred in the terms of payment. For instance, in countries that have exchange controls, it may be customary to make advance cash payments for imports. Nonresident exporters may be unwilling to extend credit to these countries because of uncertainty regarding the allocation of foreign exchange to importers for payment of their debts. If—from the perspective of nonresident exporters—the creditworthiness of such a country improves greatly, or if the market for major categories of goods imported by that country changes from a seller's to a buyer's market, nonresident exporters may decide to extend credit. If changes in credit policy occur suddenly, unadjusted bank records may seriously understate imports during the period of transition.

280. A bank record can be adjusted for timing if data recorded for each transaction include the time of payment and the time of the transaction. It will, of course, be impossible to ascertain the specific date on which the legal change of ownership took place, but that information is not required. Timing adjustments may be made on the basis of some simple rule of thumb. For example, it may be assumed that changes of ownership for both exports and imports coincide with shipment from the exporting country. In this case, a record of the shipment date (which is usually indicated on documents available to the foreign exchange control) will be sufficient as an approximate indication of the time that ownership changed. (However, in the case of postpayments, the necessary adjustments can only be made retroactively.) Alternatively, data available from an official record of export credits extended or import credits received could be used to make timing adjustments to foreign exchange records on total transactions in goods. For example, rice—one of Myanmar's major export commodities—is sold through a state corporation that extends credit on exports. As information on changes in rice credits can be obtained from the accounts of the state corporation, this data can be used to adjust receipts for rice exports from a payment basis to a transaction basis.

Adjustments for Valuation

281. Valuation adjustments are necessary when goods are recorded in source data at other than market values. Thus, when customs-generated data on imports and exports refer to valuations made for the purpose of levying customs duties on goods, adjustments must be made to account for any differences between those values and the market values of the goods.

282. The *BPM* and the United Nations standards for external trade statistics cite market values as the basis for valuing flows of goods; therefore, adjustments on this basis are unnecessary. However, fees payable to consulates of importing countries are treated differently by the two systems. Inclusion of consular fees in the value of exported goods and in imports recorded f.o.b. at the frontier of the exporting country is recommended in the standards for external trade statistics, whereas exclusion of such fees is recommended in the *BPM*. Therefore, international trade statistics valuations of goods must be adjusted for BOP purposes.

283. In some countries, Customs Cooperation Council standards for valuation of imports are used to asses *ad valorem* duties. Values assigned for this purpose to imported goods may differ from those recommended for the balance of payments, and adjustments should be made for (a) differences between contract-stipulated market prices at which goods have been sold and prices at which import duties have been assessed and (b) special quantity discounts.

284. For BOP purposes, goods should generally be recorded at contract prices (adjusted for transfer pricing, taxes, subsidies, etc.) at which the goods were sold. As the customs valuation for goods is also generally based on the purchase/sale price of bona fide sales, no adjustment is necessary in most cases. In a period of abnormal price fluctuations or in the event of an unusually long delay between the purchase/sale contract date and the payment date for customs duty (for example, if goods are stored for some time in a bonded warehouse), the customs valuation may be based on the price fetched by the goods at the time that the duty became payable. In these circumstances, the price used for customs duty valuation will not be the same as the price required for BOP purposes, and an adjustment will be required.

285. Occasionally, a single purchase/sale contract may cover goods destined for import into more than one country. Under such a contract, the buyer may receive a quantity discount that would not be available if the purchase were made in installments. The Customs Cooperation Council recommends that customs statistics reflect the price that the goods would fetch if the special quantity discount were not available. The BOP item for imports, however, should reflect the discount price as it represents the market value of these goods. For example, a multinational enterprise resident in Algornia agrees, under the terms of a single contract, to make a bulk purchase from an enterprise in Coonawarra. Commodities purchased by the multinational enterprise are shipped to three branches located in Cromania, Dromesia, and Essendonia. If three separate purchases were made, the market price of the commodities would be 100 units per purchase or 300 units in total. However, the multinational enterprise receives a 20 percent discount for buying in bulk and therefore pays only 240 units. According to the Customs Cooperation Council, Cromania, Dromesia, and Essendonia should value the imports at 100 units each. In accordance with the *BPM* concept of market price, however, Cromania, Dromesia, and Essendonia should value the imports at 80 units each. Upward adjustments made by customs officials for the purpose of eliminating special quantity discounts received by importers should not be recorded in the balance of payments.

286. As foreign exchange and other bank records covering transactions in goods settled through the banking system reflect prices actually paid for goods, valuation adjustments generally need not be applied to data contained in such records. An exception is any adjustment required to convert a transaction price to a market price for goods such as those transferred, at prices significantly distorted from market values, between related enterprises.